K12 INC
Form 10-Q
April 24, 2019
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2019

OR

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

For the transition period from to

Commission File Number: 001-33883

K12 Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	95-4774688 (I.R.S. Employer Identification No.)
2300 Corporate Park Drive Herndon, VA (Address of Principal Executive Offices)	20171 (Zip Code)

(703) 483-7000

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 (Do not check if a smaller reporting company)	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 April 19, 2019, the Registrant had 40,201,223 shares of common stock, $0.0001 par value per share outstanding.

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Form 10-Q

For the Quarterly Period Ended March 31, 2019

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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited).

K12 INC.

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2019	June 30, 2018 (audited)
	(In thousands except share and per share data)	
ASSETS		
Current assets		
Cash and cash equivalents	$ 234,025	$ 231,113
Accounts receivable, net of allowance of $9,008 and $12,384 at March 31, 2019 and June 30, 2018, respectively	238,614	176,319
Inventories, net	17,195	31,134
Prepaid expenses	17,958	10,278
Other current assets	14,181	10,388
Total current assets	521,973	459,232
Property and equipment, net	32,778	28,868
Capitalized software, net	51,693	55,488
Capitalized curriculum development costs, net	51,160	53,558
Intangible assets, net	15,723	17,951
Goodwill	90,197	90,197
Deposits and other assets	45,486	36,669
Total assets	$ 809,010	$ 741,963
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Current portion of capital lease obligations	$ 24,499	$ 13,353
Accounts payable	23,208	29,362
Accrued liabilities	17,706	14,345
Accrued compensation and benefits	30,549	36,050
Deferred revenue	52,827	23,114
Total current liabilities	148,789	116,224
Capital lease obligations, net of current portion	6,698	12,665
Deferred rent, net of current portion	2,524	3,270
Deferred tax liability	18,211	12,577
Other long-term liabilities	8,048	10,038
Total liabilities	184,270	154,774

Commitments and contingencies	—	—
Stockholders’ equity		
Common stock, par value $0.0001; 100,000,000 shares authorized; 45,542,026 and 44,902,567 shares issued; and 40,207,283 and 39,567,824 shares outstanding at March 31, 2019 and June 30, 2018, respectively	4	4
Additional paid-in capital	708,269	703,351
Accumulated other comprehensive loss	(181)	(252)
Retained earnings (accumulated deficit)	19,130	(13,432)
Treasury stock of 5,334,743 shares at cost at March 31, 2019 and June 30, 2018	(102,482)	(102,482)
Total stockholders’ equity	624,740	587,189
Total liabilities and stockholders' equity	$ 809,010	$ 741,963

See accompanying notes to unaudited condensed consolidated financial statements.

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K12 INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
	(In thousands except share and per share data)			
Revenues	$ 253,252	$ 232,864	$ 759,438	$ 678,860
Cost and expenses				
Instructional costs and services	168,260	148,878	487,574	435,408
Selling, administrative, and other operating expenses	59,382	62,267	222,143	220,507
Product development expenses	2,343	2,002	6,916	7,276
Total costs and expenses	229,985	213,147	716,633	663,191
Income from operations	23,267	19,717	42,805	15,669
Interest income, net	754	261	1,547	535
Other income (expense), net	556	—	(40)	—
Income before income taxes, loss from equity method investments and noncontrolling interest	24,577	19,978	44,312	16,204
Income tax benefit (expense)	(5,842)	(6,935)	(9,858)	1,869
Loss from equity method investments	(273)	—	(562)	—
Net income	18,462	13,043	33,892	18,073
Add net loss attributable to noncontrolling interest	—	27	—	200
Net income attributable to common stockholders	$ 18,462	$ 13,070	$ 33,892	$ 18,273
Net income attributable to common stockholders per share:				
Basic	$ 0.47	$ 0.33	$ 0.87	$ 0.46
Diluted	$ 0.44	$ 0.32	$ 0.84	$ 0.45
Weighted average shares used in computing per share amounts:				
Basic	39,008,990	39,644,074	38,753,236	39,366,497
Diluted	41,753,323	40,766,203	40,548,959	40,771,437

See accompanying notes to unaudited condensed consolidated financial statements.

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K12 INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
	(In thousands)			
Net income	$ 18,462	$ 13,043	$ 33,892	$ 18,073
Other comprehensive income, net of tax:				
Foreign currency translation adjustment	(122)	(198)	71	(392)
Total other comprehensive income, net of tax	18,340	12,845	33,963	17,681
Comprehensive loss attributable to noncontrolling interest	—	27	—	200
Comprehensive income attributable to common stockholders	$ 18,340	$ 12,872	$ 33,963	$ 17,881

See accompanying notes to unaudited condensed consolidated financial statements.

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K12 INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(In thousands except share data)	K12 Inc. Stockholders' Equity							
	Common Stock		Additional Paid-in	Accumulated Other Comprehensive	Retained Earnings (Accumulated	Treasury Stock		
	Shares	Amount	Capital	Loss	Deficit)	Shares	Amount	Total
Balance, June 30, 2018	44,902,567	$ 4	$ 703,351	$ (252)	$ (13,432)	(5,334,743)	$ (102,482)	$ 587,189
Adjustment related to new revenue recognition guidance	—	—	—	—	(1,330)	—	—	(1,330)
Net loss	—	—	—	—	(8,282)	—	—	(8,282)
Foreign currency translation adjustment	—	—	—	72	—	—	—	72
Stock-based compensation expense	—	—	4,109	—	—	—	—	4,109
Exercise of stock options	687	—	10	—	—	—	—	10
Vesting of performance share units, net of tax withholding	258,263	—	—	—	—	—	—	—
Issuance of restricted stock awards	722,809	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(122,242)	—	—	—	—	—	—	—
Repurchase of restricted stock for tax withholding	(188,804)	—	(6,072)	—	—	—	—	(6,072)
Balance, September 30, 2018	45,573,280	$ 4	$ 701,398	$ (180)	$ (23,044)	(5,334,743)	$ (102,482)	$ 575,696
Net income	—	—	—	—	23,712	—	—	23,712
	—	—	—	121	—	—	—	121

Foreign currency translation adjustment								
Stock-based compensation expense	—	—	4,235	—	—	—	—	4,235
Exercise of stock options	51,050	—	1,025	—	—	—	—	1,025
Issuance of restricted stock awards	26,000	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(54,054)	—	—	—	—	—	—	—
Repurchase of restricted stock for tax withholding	(45,960)	—	(833)	—	—	—	—	(833)
Balance, December 31, 2018	45,550,316	$ 4	$ 705,825	$ (59)	$ 668	(5,334,743)	$ (102,482)	$ 603,956
Net income	—	—	—	—	18,462	—	—	18,462
Foreign currency translation adjustment	—	—	—	(122)	—	—	—	(122)
Stock-based compensation expense	—	—	4,047	—	—	—	—	4,047
Exercise of stock options	54,753	—	1,148	—	—	—	—	1,148
Issuance of restricted stock awards	73,524	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(51,435)	—	—	—	—	—	—	—
Repurchase of restricted stock for tax withholding	(85,132)	—	(2,751)	—	—	—	—	(2,751)
Balance, March 31, 2019	45,542,026	$ 4	$ 708,269	$ (181)	$ 19,130	(5,334,743)	$ (102,482)	$ 624,740

See accompanying notes to unaudited condensed consolidated financial statements.

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K12 INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(In thousands except share data)	K12 Inc. Stockholders' Equity Common Stock Shares	Amount	Additional Paid-in Capital	Other Accumulated Comprehensive Loss	Accumulated Deficit	Treasury Stock Shares	Amount	Total
Balance, June 30, 2017	44,325,772	$ 4	$ 690,488	$ (170)	$ (40,976)	(3,502,598)	$ (75,000)	$ 574,34
Adjustment related to new stock-based compensation guidance	—	—	112	—	(69)	—	—	43
Net loss	—	—	—	—	(8,056)	—	—	(8,056
Foreign currency translation adjustment	—	—	—	(155)	—	—	—	(155)
Stock-based compensation expense	—	—	4,832	—	—	—	—	4,832
Exercise of stock options	3,350	—	58	—	—	—	—	58
Issuance of restricted stock awards	867,388	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(129,286)	—	—	—	—	—	—	—
Adjustment to redeemable noncontrolling interest to estimated redemption value	—	—	(103)	—	—	—	—	(103)
Repurchase of restricted stock for tax withholding	(230,158)	—	(4,093)	—	—	—	—	(4,093
Balance, September 30,	44,837,066	$ 4	$ 691,294	$ (325)	$ (49,101)	(3,502,598)	$ (75,000)	$ 566,87

2017								
Net income	—	—	—	—	13,259	—	—	13,259
Foreign currency translation adjustment	—	—	—	(39)	—	—	—	(39)
Stock-based compensation expense	—	—	7,284	—	—	—	—	7,284
Vesting of performance share units, net of tax withholding	60,324	—	—	—	—	—	—	—
Issuance of restricted stock awards	88,924	—	—	—	—	—	—	—
Forfeiture of restricted stock awards	(28,438)	—	—	—	—	—	—	—
Adjustment to redeemable noncontrolling interest to estimated redemption value	—	—	130	—	—	—	—	130
Repurchase of restricted stock for tax withholding	(59,446)	—	(1,664)	—	—	—	—	(1,664
Balance, December 31, 2017	44,898,430	$ 4	$ 697,044	$ (364)	$ (35,842)	(3,502,598)	$ (75,000)	$ 585,84
Net income	—	—	—	—	13,070	—	—	13,070
Foreign currency translation adjustment	—	—	—	(198)	—	—	—	(198)
Stock-based compensation expense	—	—	4,625	—	—	—	—	4,625
Exercise of stock options	10,250	—	126	—	—	—	—	126
Vesting of performance share units, net of tax withholding	89,352	—	—	—	—	—	—	—
Issuance of restricted stock	55,293	—	—	—	—	—	—	—

awards								
Forfeiture of restricted stock awards	(173,539)	—	—	—	—	—	—	—
Adjustment to redeemable noncontrolling interest to estimated redemption value	—	—	(27)	—	—	—	—	(27)
Repurchase of restricted stock for tax withholding	(214,988)	—	(4,006)	—	—	—	—	(4,006
Balance, March 31, 2018	44,664,798	$ 4	$ 697,762	$ (562)	$ (22,772)	(3,502,598)	$ (75,000)	$ 599,43

See accompanying notes to unaudited condensed consolidated financial statements.

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K12 INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine Months Ended March 31,	
	2019	2018
	(In thousands)	
Cash flows from operating activities		
Net income	$ 33,892	$ 18,073
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization expense	53,259	57,612
Stock-based compensation expense	12,114	14,853
Deferred income taxes	5,327	(4,978)
Provision for doubtful accounts	2,854	605
Other	5,291	4,757
Changes in assets and liabilities:		
Accounts receivable	(65,147)	(16,220)
Inventories, prepaid expenses, deposits and other current and long-term assets	4,620	(24,138)
Accounts payable	(3,134)	(9,215)
Accrued liabilities	5,211	(7,364)
Accrued compensation and benefits	(5,501)	111
Deferred revenue, rent and other liabilities	24,510	21,134
Net cash provided by operating activities	73,296	55,230
Cash flows from investing activities		
Purchase of property and equipment	(2,397)	(6,580)
Capitalized software development costs	(20,580)	(18,852)
Capitalized curriculum development costs	(13,746)	(7,770)
Sale of long-lived assets	389	—
Acquisitions and investments	(11,652)	(3,274)
Net cash used in investing activities	(47,986)	(36,476)
Cash flows from financing activities		
Repayments on capital lease obligations	(13,898)	(10,313)
Payments of contingent consideration	(1,027)	(1,819)
Proceeds from exercise of stock options	2,183	184
Repurchase of restricted stock for income tax withholding	(9,656)	(9,763)
Net cash used in financing activities	(22,398)	(21,711)
Net change in cash, cash equivalents and restricted cash	2,912	(2,957)
Cash, cash equivalents and restricted cash, beginning of period	233,113	230,864
Cash, cash equivalents and restricted cash, end of period	$ 236,025	$ 227,907
Reconciliation of cash, cash equivalents and restricted cash to balance sheet as of March 31st:		
Cash and cash equivalents	$ 234,025	$ 227,907
Deposits and other assets (restricted cash)	2,000	—
Total cash, cash equivalents and restricted cash	$ 236,025	$ 227,907

See accompanying notes to unaudited condensed consolidated financial statements.

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K12 INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Description of the Business

K12 Inc., together with its subsidiaries ("K12" or the "Company"), is a technology-based education company. The Company offers proprietary and third party curriculum, software systems and educational services designed to facilitate individualized learning for students primarily in kindergarten through 12th grade, or K-12. The Company's learning systems combine curriculum, instruction, and related support services to create an individualized learning approach well-suited for virtual and blended public schools, school districts, charter schools, and private schools that utilize varying degrees of online and traditional classroom instruction, and other educational applications. These products and services are provided through three lines of business:

· Managed Public School Programs (programs which offer an integrated package of systems, services, products, and professional expertise that K12 manages in order to support an online or blended public school, including administrative support, information technology, academic support services, online curriculum, learning system platforms, and instructional services);
· Institutional (Non-managed Public School Programs – programs which provide instruction, curriculum, supplemental courses, marketing, enrollment and other educational services where K12 does not provide primary administrative support services, and Institutional Software and Services – educational software and services provided to school districts, public schools and other educational institutions); and
· Private Pay Schools and Other (private schools for which the Company charges student tuition and makes direct consumer sales).

The Company works closely as a partner with public schools, school districts, charter schools, and private schools, enabling them to offer their students an array of solutions, including full-time virtual programs, semester courses and supplemental solutions. In addition to curriculum, systems and programs, the Company provides teacher training, teaching services, and other academic and technology support services.

2. Basis of Presentation

The accompanying condensed consolidated balance sheet as of March 31, 2019, the condensed consolidated statements of operations and comprehensive income for the three and nine months ended March 31, 2019 and 2018, the condensed consolidated statements of cash flows for the nine months ended March 31, 2019 and 2018, and the condensed consolidated statements of stockholders' equity for the three and nine months ended March 31, 2019 and 2018 are unaudited. The unaudited interim financial statements have been prepared on the same basis as the annual financial statements, and in the opinion of management, reflect all adjustments, which include only normal recurring adjustments, necessary to present fairly the Company’s financial position and results of operations for the periods presented. The results for the three and nine months ended March 31, 2019 are not necessarily indicative of the results to be expected for the year ending June 30, 2019, for any other interim period or for any other future fiscal year. The condensed consolidated balance sheet as of June 30, 2018 has been derived from the audited consolidated financial statements at that date.

The accompanying unaudited condensed consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Accordingly, the Company does not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, these statements include all adjustments (consisting of normal recurring adjustments) considered necessary to present a fair statement of the Company’s condensed consolidated results of operations, financial position and cash flows. Preparation of the Company’s financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts in the financial statements and footnotes. Actual results could differ from those estimates. This quarterly report on Form 10-Q should be read in conjunction with the financial statements and the notes thereto included in the Company’s latest annual report on Form 10-K filed with the Securities and Exchange Commission (the “SEC”) on August 8, 2018, which contains the Company’s audited financial statements for the fiscal year ended June 30, 2018.

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K12 INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The Company operates in one operating and reportable business segment as a technology-based education company providing proprietary and third party curriculum, software systems and educational services designed to facilitate individualized learning for students primarily in kindergarten through 12th grade. The Chief Operating Decision Maker evaluates profitability based on consolidated results.

3. Summary of Significant Accounting Policies

Recent Accounting Pronouncements

Accounting Standards Adopted

In August 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-15, Statement of Cash Flows (Topic 230) (“ASU 2016-15”) to establish the classification of certain cash receipts and disbursements into the appropriate operating, investing, or financing categories; where there was diversity in practice previously. The Company has evaluated the standard and determined that the classification of contingent consideration payments should be moved from operating activities to financing activities. The Company retrospectively adopted this standard during the first quarter of fiscal year 2019. The adoption required the restatement of $1.8 million from cash flows from operations to cash flows from financing activities in fiscal year 2018.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (“ASU 2014-09”), also known as Accounting Standards Codification Topic 606 (“ASC 606”), which supersedes most existing revenue recognition guidance under ASC Topic 605 (“ASC 605”). The core principal of ASC 606 is to recognize revenues when contracted goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASC 606 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than were required under previous GAAP.

The Company performed a detailed review of each of its revenue streams by comparing historical accounting policies and practices to the new standard. The majority of the Company’s business is based on contracts where annual revenue is recognized within each fiscal year, mirroring the school year.

The Company adopted this standard during the first quarter of fiscal year 2019 using the modified retrospective approach. Under this method, the Company applied ASC 606 to those contracts whose terms extend beyond July 1, 2018. The comparative information for prior periods has not been restated and continues to be reported under the accounting standards in effect for those periods. The adoption of ASC 606 resulted in an adjustment to decrease retained earnings by $1.3 million.

The key impact of ASC 606 was to streamline the recognition of all revenues from the Company's lines of businesses over the service period, including:

- Revenues that had been previously recognized over a 10-month school year;
- Revenues from materials, supplies and professional services that had been previously recognized upon delivery; and
- Revenues in which the Company is the primary obligor, and were recognized when expenses were incurred.

In addition, the adoption of ASC 606 impacted how the Company accounts for its sales commissions. See "Costs to Obtain a Contract with a Customer" section below.

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K12 INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

The impact of adoption on the Company's condensed consolidated statements of operations for the three and nine months ended March 31, 2019 was as follows:

	Three Months Ended March 31, 2019			Nine Months Ended March 31, 2019		
	As Reported Under ASC 606	Adjustment due to ASC 606	Amounts under ASC 605	As Reported Under ASC 606	Adjustment due to ASC 606	Amounts under ASC 605
	(In thousands)					
Revenues	$ 253,252	$ 6,536	$ 259,788	$ 759,438	$ 3,799	$ 763,237
Selling, administrative, and other operating expenses	59,382	(68)	59,314	222,143	(193)	221,950
Income from operations	23,267	6,604	29,871	42,805	3,992	46,797
Net income	18,462	6,604	25,066	33,892	3,992	37,884
Net income attributable to common stockholders	$ 18,462	$ 6,604	$ 25,066	$ 33,892	$ 3,992	$ 37,884

The impact of adoption on the Company's condensed consolidated balance sheets as of March 31, 2019 was as follows:

	March 31, 2019		
	As Reported Under ASC 606	Adjustment due to ASC 606	Amounts under ASC 605
	(In thousands)		
Other current assets	$ 14,181	$ (266)	$ 13,915
Deposits and other assets	45,486	(574)	44,912
Total assets	809,010	(840)	808,170
Deferred revenue	52,827	(6,264)	46,563
Total liabilities	184,270	(6,264)	178,006

Retained earnings (accumulated deficit)	19,130	3,992	23,122
Total stockholders' equity	624,740	3,992	628,732

The following table presents the Company’s revenues disaggregated based on its three lines of business for the three and nine months ended March 31, 2019:

	Three Months Ended March 31, 2019	Nine Months Ended March 31, 2019
	(In thousands)	
Managed Public School Programs	$ 222,645	$ 665,981
Institutional		
Non-managed Public School Programs	12,776	37,398
Institutional Software & Services	8,530	29,515
Total Institutional	21,306	66,913
Private Pay Schools and Other	9,301	26,544
Total Revenues	$ 253,252	$ 759,438

For more discussion surrounding the Company’s revenue recognition accounting policies, please refer to the “Contracts with Customers” section below.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

Accounting Standards Not Yet Adopted

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842) ("ASU 2016-02" or "Topic 842"). The new standard establishes a right-of-use ("ROU") model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the statement of operations.

In July 2018, the FASB issued ASU 2018-10, Codification Improvements to Topic 842, Leases ("ASU 2018-10") and ASU 2018-11, Leases (Topic 842), Targeted Improvements ("ASU 2018-11") to provide additional guidance for the adoption of Topic 842. ASU 2018-10 clarifies certain provisions and corrects unintended applications of the guidance such as the application of implicit rate; lessee reassessment of lease classification; lease term or bargain purchase option; variable lease payments; and certain transition guidance. ASU 2018-11 provides an alternative transition method and practical expedient for separating contract components for the adoption of Topic 842. ASU 2018-11, ASU 2018-10, and ASU 2016-02 (collectively, "ASC 842") are effective for the Company's fiscal year beginning July 1, 2019, including interim periods therein.

The modified retrospective transition approach under ASU 2016-02 requires lessees to include capital and operating leases that exist at, or are entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. ASU 2018-11 allows lessees to initially apply the new lease standard at the adoption date and recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. The Company anticipates that the impact of ASC 842 will be centered around its facility leases. The Company will record a lease liability with an expected present value in the range of $22 - $25 million and a ROU asset in the range of $17 - $20 million, based on its current leasing arrangements. The impact on the statements of operations is expected to be immaterial. The Company continues to evaluate ASC 842, as well as the effect on its condensed consolidated financial statements.

In August 2018, the FASB issued ASU 2018-15, Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40) ("ASU 2018-15"). ASU 2018-15 aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal-use software license). It requires an entity in a hosting arrangement that is a service contract to follow the guidance in Subtopic 350-40 to determine which implementation costs to capitalize as an asset related to the service contract and which costs to expense. ASU 2018-15 is effective for the Company's fiscal year beginning July 1, 2020. The Company is currently evaluating the impact of this ASU on its condensed consolidated financial statements.

Contracts with Customers

Revenues are principally earned from contractual agreements to provide online curriculum, books, materials, computers and management services to virtual and blended schools, traditional public schools, school districts, and private schools through its three lines of business; Managed Public School Programs, Institutional, and Private Pay and Other.

Under ASC 606, revenue is recognized when control of the promised goods or services is transferred to the Company's customers, in an amount that reflects the consideration it expects to be entitled to in exchange for those goods or services using the following steps:

- identify the contract, or contracts, with a customer;
- identify the performance obligations in the contract;
- determine the transaction price;
- allocate the transaction price to the performance obligations in the contract; and
- recognize revenue when, or as, the Company satisfies a performance obligation.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - Continued

Revenue Recognition

Managed Public School Programs

The Company provides an integrated package of systems, services, products, and professional expertise that we manage to support online or blended public schools. Contractual agreements generally span multiple years with performance obligations being isolated to annual periods. Customers for these programs can obtain the administrative support, information technology, academic support services, online curriculum, learning systems platforms and instructional services under the terms of a negotiated service agreement. The schools receive funding on a per student basis from the state in which the public school or school district is located. Shipments of materials for schools that occur in the fourth fiscal quarter and for the upcoming school year are recorded in deferred revenue.

The Company generates revenues under contracts with virtual and blended public schools and include the following components, where required:

- providing each of a school’s students with access to the Company’s online school and lessons;
- offline learning kits, which include books and materials to supplement the online lessons;
- the use of a personal computer and associated reclamation services;
- internet access and technology support services;
- instruction by a state-certified teacher; and
- management and technology services necessary to support a virtual public or blended school. In certain managed school contracts, revenues are determined directly by per enrollment funding.

To determine the pro rata amount of revenue to recognize in a fiscal quarter, the Company estimates the total funds each school will receive in a particular school year. Total funds for a school are primarily a function of the number of students enrolled in the school and established per enrollment funding levels, which are generally published on an annual basis by the state or school district. The Company reviews its estimates of funding periodically, and revises as necessary, amortizing any adjustments to earned revenues over the remaining portion of the fiscal year. Actual school funding may vary from these estimates and the impact of these differences could impact the Company’s results of operations. Since the end of the school year coincides with the end of the Company’s fiscal year, annual revenues are generally based on actual school funding and actual costs incurred (including costs for the Company’s services to the schools plus other costs the schools may incur) in the calculation of school operating losses. The Company’s schools’ reported results are subject to annual school district financial audits, which incorporate enrollment counts, funding and other routine financial audit considerations. The results of these audits are incorporated into the Company’s monthly funding estimates for the three and nine months ended March 31, 2019 and 2018.

Each state and/or school district has variations in the school funding formulas and methodologies that it uses to estimate funding for revenue recognition at its respective schools. As the Company estimates funding for each school, it takes into account the state definition for count dates on which reported enrollment numbers will be used for per pupil funding. The parameters the Company considers in estimating funding for revenue recognition purposes include school district count definitions, withdrawal rates, average daily attendance, special needs enrollment, student demographics, academic progress and historical completion, student location, funding caps and other state specified categorical program funding.

Under the contracts where the Company provides services to schools, the Company has generally agreed to absorb any operating losses of the schools in a given school year. These school operating losses represent the excess of costs incurred over revenues earned by the virtual or blended public school as reflected on its respective financial statements, including Company charges to the schools. To the extent a school does not receive funding for each student enrolled in the school, the school would still incur costs associated with serving the unfunded enrollment. If losses due to unfunded enrollments result in a net operating loss for the year that loss is reflected as a reduction in the revenues and net receivables that the Company collects from the school. A school net operating loss in one year does not necessarily mean the Company anticipates losing money on the entire contract with the school. However, a school operating loss may reduce the Company’s ability to collect its management fees in full and recognized revenues are reduced accordingly to reflect the expected cash collections from such schools. The Company amortizes the estimated school operating loss

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against revenues based upon the percentage of actual revenues in the period to total estimated revenues for the fiscal year.

Management periodically reviews its estimates of full-year school revenues and operating expenses, and amortizes the net impact of any changes to these estimates over the remainder of the fiscal year. Actual school operating losses may vary from these estimates or revisions, and the impact of these differences could have a material impact on results of operations. For the three months ended March 31, 2019 and 2018, the Company’s revenues included a reduction for these school operating losses for $9.2 million and $18.7 million, respectively, and $43.2 million and $50.2 million for the nine months ended March 31, 2019 and 2018, respectively.

The Company has certain contracts where it is responsible for substantially all of the expenses incurred by the school. For these contracts, the Company records both revenue and expenses incurred by the schools. Amounts recorded as revenues for the three months ended March 31, 2019 and 2018 were $85.8 million and $81.4 million, respectively, and for the nine months ended March 31, 2019 and 2018 were $259.9 million and $221.0 million, respectively.

Institutional

The products and services delivered to the Company’s Institutional customers include curriculum and technology for full-time virtual and blended programs, as well as instruction, curriculum and associated materials, supplemental courses, marketing, enrollment and other educational services. Each of these contracts are considered to be one performance obligation under ASC 606.

The Company provides certain online curriculum and services to schools and school districts under subscription agreements. Revenues from the licensing of curriculum under subscription arrangements are recognized on a ratable basis over the subscription period. Revenues from professional consulting, training and support services are deferred and recognized ratably over the service period.

Private Pay Schools and Other

Private Pay Schools and Other revenues are generated from individual customers who prepay and have access for one to two years to company-provided online curriculum. Each of these contracts are considered to be one performance obligation under ASC 606. The Company recognizes these revenues pro rata over the maximum term of the customer contract.

Concentration of Customers

During the three and nine months ended March 31, 2019 and nine months ended March 31, 2018, the Company had one contract that represented 10% of revenues. For the three months ended March 31, 2018, the Company had no contracts greater than 10% of revenues.

Contract Balances

The timing of revenue recognition, invoicing, and cash collection results in accounts receivable, unbilled receivables (a contract asset) and deferred revenue (a contract liability) in the condensed consolidated balance sheets. Accounts receivable is recorded when there is an executed customer contract and the customer is billed. The collectability of outstanding receivables is evaluated regularly by the Company and an allowance is recorded to reflect anticipated losses. Unbilled receivables are created when revenue is earned prior to the customer being billed. Deferred revenue is recorded when customers are billed in advance of services being provided.

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The opening and closing balances of the Company’s accounts receivable, unbilled receivables and deferred revenue are as follows:

	March 31, 2019	July 1, 2018
	(In thousands)	
Accounts receivable	$ 238,614	$ 176,319
Unbilled receivables (included in accounts receivable)	22,617	12,143
Deferred revenue	52,827	25,580

The difference between the opening and closing balance of the accounts receivable and unbilled receivables relates to the timing of the Company’s billing in relation to month end and contractual agreements. The difference between the opening and closing balance of the deferred revenue relates to the timing difference between billings to customers and the Company’s performance under the contract. Typically, each of these balances are at their highest during the first quarter of the fiscal year and lowest at the end of the fiscal year. The amount of revenue recognized during the three months ended March 31, 2019 that was included in the opening January 1, 2019 deferred revenue balance was $24.9 million. The amount of revenue recognized during the nine months ended March 31, 2019 that was included in the opening July 1, 2018 deferred revenue balance was $21.5 million.

During the three and nine months ended March 31, 2019, the Company recorded revenues of $3.2 million and $3.7 million, respectively, related to performance obligations satisfied in prior periods.

Performance Obligations

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer, and is the unit of account in ASC 606. A contract’s transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. For the majority of its contracts, the Company’s performance obligations are satisfied over time, as the Company delivers, and the customer receives the services, over the service period of the contract. The Company’s payment terms are generally net 30 or net 45, but can vary depending on when the school receives its funding from the state.

The Company has elected, as a practical expedient, to not report the value of unsatisfied performance obligations for contracts with customers that have an expected duration of one year or less. The amount of unsatisfied performance obligations for contracts with customers which extend beyond one year as of March 31, 2019 was $1.7 million.

Significant Judgments

The Company determined that the majority of its contracts with customers contain one performance obligation. The Company markets the products and services as an integrated package building off its curriculum offerings. It does not market distinct products or services to be sold independently from the curriculum offering.

The Company has determined that the time elapsed method as described under ASC 606 is the most appropriate measure of progress towards the satisfaction of the performance obligation. The Company delivers the integrated products and services package related to its Managed Public School Programs largely over the course of the Company's fiscal year. This package includes enrollment, marketing, teacher training, etc. in addition to the core curriculum and instruction. All of these activities are necessary and contribute to the overall education of its students, which occurs evenly throughout the year. Accordingly, the Company will recognize revenue on a straight-line basis.

As discussed above, the Company estimates the total funds each school will receive in a particular school year and the amount of full-year school revenues and operating expenses to determine the amount of revenue the Company will receive. To the extent the estimates change during the year, the cumulative impact of the change is recognized over the remaining service period.

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Costs to Obtain a Contract with a Customer

Where permitted, the Company pays commissions on certain sales contracts to its employees and third parties. Commissions that are directly tied to a particular sale are capitalized if they relate to either new business or a renewal whose contract has a duration of greater than one year. The Company has elected, as a practical expedient, to not capitalize commissions paid on contracts that have a duration of one year or less. Commissions that are not directly tied to a particular sale are expensed as incurred.

Commissions related to new business are amortized over a four year life which represents the average life of customers in the institutional and private pay businesses, while commissions related to renewals greater than one year are amortized over the contract life. The current portion of deferred commissions is recorded within other current assets and the long-term portion of deferred commissions is recorded within deposits and other assets on the condensed consolidated balance sheets. The amortization of deferred commissions is recorded as selling, administrative and other operating expenses.

Consolidation

The condensed consolidated financial statements include the accounts of the Company, the wholly-owned and affiliated companies that the Company owns, directly or indirectly, and all controlled subsidiaries. All significant intercompany transactions and balances have been eliminated in consolidation.

Inventories

Inventories consist primarily of textbooks and curriculum materials, a majority of which are supplied to virtual public schools and blended public schools, and utilized directly by students. Inventories represent items that are purchased and held for sale and are recorded at the lower of cost (first-in, first-out method) or net realizable value. The provision for excess and obsolete inventory is established based upon the evaluation of the quantity on hand relative to demand. The excess and obsolete inventory reserve was $4.1 million and $3.5 million at March 31, 2019 and June 30, 2018, respectively.

Other Current Assets

Other current assets consist primarily of textbooks, curriculum materials and other supplies which are expected to be returned upon the completion of the school year. Materials not returned are expensed as part of instructional costs and services.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation and amortization expense is calculated using the straight-line method over the estimated useful life of the asset (or the lesser of the term of the lease and the estimated useful life of the asset under capital lease). Amortization of assets capitalized under capital lease arrangements is included in depreciation expense. Leasehold improvements are amortized over the lesser of the lease term or the estimated useful life of the asset. The Company determines the lease term in accordance with ASC 840, Leases (“ASC 840”), as the fixed non-cancelable term of the lease plus all periods for which failure to renew the lease imposes a penalty on the lessee in an amount such that renewal appears, at the inception of the lease, to be reasonably assured.

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Property and equipment are depreciated over the following useful lives:

	Useful Life
Student and state testing computers	3 - 5 years
Computer hardware	3 years
Computer software	3 - 5 years
Web site development	3 years
Office equipment	5 years
Furniture and fixtures	7 years
Leasehold improvements	3 - 12 years

The Company makes an estimate of unreturned student computers based on an analysis of recent trends of returns. The Company recorded accelerated depreciation of $0.5 million and $0.8 million for the three months ended March 31, 2019 and 2018, respectively, and $1.6 million and $1.7 million for the nine months ended March 31, 2019 and 2018, respectively, related to unreturned student computers. Depreciation expense for property and equipment, including accelerated depreciation, for the three months ended March 31, 2019 and 2018 was $4.9 million and $4.8 million, respectively, and $15.2 million and $13.7 million for the nine months ended March 31, 2019 and 2018, respectively.

The Company fully expenses computer peripheral equipment (e.g. keyboards, mouses) upon purchase as recovery has been determined to be uneconomical. These expenses totaled $0.7 million and $0.8 million for the three months ended March 31, 2019 and 2018, respectively, and $4.0 million and $3.3 million for the nine months ended March 31, 2019 and 2018, respectively, and are recorded as instructional costs and services.

Capitalized Software Costs

The Company develops software for internal use. Software development costs incurred during the application development stage are capitalized in accordance with ASC 350, Intangibles – Goodwill and Other (“ASC 350”). The Company amortizes these costs over the estimated useful life of the software, which is generally three years. Capitalized software development costs are stated at cost less accumulated amortization.

Capitalized software additions totaled $20.6 million and $18.9 million for the nine months ended March 31, 2019 and 2018, respectively. Amortization expense for the three months ended March 31, 2019 and 2018 was $7.0 million and $8.2 million, respectively, and $22.4 million and $26.9 million for the nine months ended March 31, 2019 and 2018, respectively.

During the three months ended September 30, 2017, the Company recorded an out of period adjustment related to the capitalization of software and curriculum development. The adjustment increased capitalized software development costs and capitalized curriculum development costs by $2.3 million and $0.6 million, respectively, and decreased net loss by $1.4 million for the period. The Company assessed the materiality of these errors on its prior quarterly and annual financial statements, assessing materiality both quantitatively and qualitatively, in accordance with the SEC's Staff Accounting Bulletin ("SAB") No. 99 and SAB No. 108 and concluded that the errors were not material to any of its previously issued financial statements.

Capitalized Curriculum Development Costs

The Company internally develops curriculum, which is primarily provided as online content and accessed via the Internet. The Company also creates textbooks and other materials that are complementary to online content.

The Company capitalizes curriculum development costs incurred during the application development stage in accordance with ASC 350. The Company capitalizes curriculum development costs during the design and deployment phases of the project. As a result, a significant portion of the Company's courseware development costs qualify for capitalization due to the concentration of its development efforts on the content of the courseware. Capitalization ends

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when a course is available for general release to its customers, at which time amortization of the capitalized costs begins. The period of time over which these development costs are amortized is generally five years.

Total capitalized curriculum development additions were $13.7 million and $7.8 million for the nine months ended March 31, 2019 and 2018, respectively. These amounts are recorded on the accompanying condensed consolidated balance sheets net of amortization charges. Amortization is recorded in instructional costs and services on the accompanying condensed consolidated statements of operations. Amortization expense for the three months ended March 31, 2019 and 2018 was $4.5 million and $4.7 million, respectively, and $13.5 million and $14.8 million for the nine months ended March 31, 2019 and 2018, respectively. As mentioned above, capitalized curriculum development additions for the nine months ended March 31, 2018 included an out of period adjustment of $0.6 million.

Income Taxes

The Company accounts for income taxes in accordance with ASC 740, Income Taxes (“ASC 740”). Under ASC 740, deferred tax assets and liabilities are computed based on the difference between the financial reporting and income tax bases of assets and liabilities using the enacted marginal tax rate. ASC 740 requires that the net deferred tax asset be reduced by a valuation allowance if, based on the weight of available evidence, it is more likely than not that some portion or all of the net deferred tax asset will not be realized.

Redeemable Noncontrolling Interests

Earnings or losses attributable to minority shareholders of a consolidated affiliated company are classified separately as “noncontrolling interest” in the Company’s condensed consolidated statements of operations. Noncontrolling interests in subsidiaries that are redeemable outside of the Company’s control for cash or other assets are classified outside of permanent equity at redeemable value, which approximates fair value. If the redemption amount is other than fair value (e.g. fixed or variable), the redeemable noncontrolling interest is accounted for at the fixed or variable redeemable value. The redeemable noncontrolling interests are adjusted to their redeemable value at each balance sheet date. The resulting increases or decreases in the estimated redemption amount are affected by corresponding charges against retained earnings, or in the absence of retained earnings, additional paid-in capital.

Goodwill and Intangible Assets

The Company records as goodwill the excess of the purchase price over the fair value of the identifiable net assets acquired. Finite-lived intangible assets acquired in business combinations subject to amortization are recorded at their fair value. Finite-lived intangible assets include trade names, acquired customers and distributors, developed technology and non-compete agreements. Such intangible assets are amortized on a straight-line basis over their estimated useful lives. Amortization expense for the three months ended March 31, 2019 and 2018 was $0.7 million and $0.7 million, respectively, and for the nine months ended March 31, 2019 and 2018 was $2.2 million and $2.2 million, respectively. Future amortization of intangible assets is expected to be $0.7 million, $2.9 million, $2.4 million, $2.2 million, and $2.0 million in the fiscal years ending June 30, 2019 through June 30, 2023, respectively and $5.2 million thereafter. At March 31, 2019 and June 30, 2018, the goodwill balance was $90.2 million.

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 fully recoverable. If the total of the expected undiscounted future cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between fair value and the carrying value of the asset. There were no such events during the three and nine months ended March 31, 2019 and 2018.

ASC 350 prescribes a two-step process for impairment testing of goodwill and intangible assets with indefinite lives, which is performed annually, as well as when an event triggering impairment may have occurred based on one reporting unit. ASC 350 also allows preparers to qualitatively assess goodwill impairment through a screening process which would permit companies to forgo Step 1 of their annual goodwill impairment process. This qualitative screening process will hereinafter be referred to as “Step 0”. The Company performs its annual assessment on May 31st. During the year ended June 30, 2018, the Company performed “Step 0” of the impairment test and determined that there were no facts and circumstances that indicated that the fair value of the reporting unit may be less than its carrying amount, and as a result, the Company determined that no impairment was required. During the three and nine months ended March 31, 2019 and 2018, there were no events or changes in circumstances that would indicate that the carrying amount of the goodwill was impaired.

The following table represents the balance of the Company's intangible assets as of March 31, 2019 and June 30, 2018:

	March 31, 2019			June 30, 2018		
($ in millions)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
Trade names	$ 17.6	$ (9.2)	$ 8.4	$ 17.6	$ (8.5)	$ 9.1
Customer and distributor relationships	20.5	(14.4)	6.1	20.5	(13.4)	7.1
Developed technology	3.2	(2.6)	0.6	3.2	(2.2)	1.0
Other	1.4	(0.8)	0.6	1.4	(0.6)	0.8
Total	$ 42.7	$ (27.0)	$ 15.7	$ 42.7	$ (24.7)	$ 18.0

Impairment of Long-Lived Assets

Long-lived assets include property, equipment, capitalized curriculum and software developed or obtained for internal use. In accordance with ASC 360, Property, Plant and Equipment ("ASC 360"), management reviews the Company's recorded long-lived assets for impairment annually or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be fully recoverable. The Company determines the extent to which an asset may be impaired based upon its expectation of the asset's future usability as well as on a reasonable assurance that the future cash flows associated with the asset will be in excess of its carrying amount. If the total of the expected undiscounted future cash flows is less than the carrying amount of the asset, a loss is recognized for the difference between fair value and the carrying value of the asset. There was no such impairment charge during the three and nine months ended March 31, 2019 and 2018.

Fair Value Measurements

ASC 820, Fair Value Measurements and Disclosures ("ASC 820"), defines fair value as the price that would be received to sell an asset or paid to transfer a liability, in the principal or most advantageous market for the asset or liability, in an orderly transaction between market participants at the measurement date. ASC 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

ASC 820 describes three levels of inputs that may be used to measure fair value:

Level 1: Inputs based on quoted market prices for identical assets or liabilities in active markets at the measurement date.

Level 2: Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Inputs reflect management's best estimate of what market participants would use in pricing the asset or liability at the measurement date. The inputs are unobservable in the market and significant to the instrument's valuation.

The carrying values reflected in the accompanying condensed consolidated balance sheets for cash and cash equivalents, receivables, and short and long term debt approximate their fair values. The lease exit liability is discussed

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in more detail in Note 9, "Restructuring." The Tallo, Inc. convertible note is discussed in more detail in Note 10, "Investments."

The following table summarizes certain fair value information at March 31, 2019 for assets or liabilities measured at fair value on a nonrecurring basis:

	Fair Value Measurements Using:			
Description	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Input (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)			
Lease exit liability	$ 2,185	$ —	$ —	$ 2,185

The following table summarizes certain fair value information at June 30, 2018 for assets and liabilities measured at fair value on a nonrecurring basis:

	Fair Value Measurements Using:			
Description	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Input (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)			
Lease exit liability	$ 2,758	$ —	$ —	$ 2,758

The following table summarizes certain fair value information at March 31, 2019 for assets or liabilities measured at fair value on a recurring basis:

	Fair Value Measurements Using:			
Description	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Input (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)			
Convertible note	$ 5,006	$ —	$ —	$ 5,006

The following table summarizes certain fair value information at June 30, 2018 for assets and liabilities measured at fair value on a recurring basis:

	Fair Value Measurements Using:			
Description	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Input (Level 2)	Significant Unobservable Inputs (Level 3)
	(In thousands)			
Contingent consideration associated with acquisitions	$ 1,345	$ —	$ —	$ 1,345

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The following tables summarize the activity during the three and nine months ended March 31, 2019 and 2018 for assets and liabilities measured at fair value on a recurring basis:

	Three Months Ended March 31, 2019			
Description	Fair Value December 31, 2018	Purchases, Issuances, and Settlements	Unrealized Gains/(Losses)	Fair Value March 31, 2019
	(In thousands)			
Contingent consideration associated with acquisitions	$ 40	$ (40)	$ —	$ —
Convertible note	5,006	—	—	5,006

	Three Months Ended March 31, 2018			
Description	Fair Value December 31, 2017	Purchases, Issuances, and Settlements	Unrealized Gains/(Losses)	Fair Value March 31, 2018
	(In thousands)			
Contingent consideration associated with acquisitions	$ 1,340	$ —	$ 2	$ 1,342

	Nine Months Ended March 31, 2019			
Description	Fair Value June 30, 2018	Purchases, Issuances, and Settlements	Unrealized Gains (Losses)	Fair Value March 31, 2019
	(In thousands)			
Contingent consideration associated with acquisitions	$ 1,345	$ (1,347)	$ 2	$ —

Convertible note	—	5,006	—	5,006

	Nine Months Ended March 31, 2018			
Description	Fair Value June 30, 2017	Purchases, Issuances, and Settlements	Unrealized Gains (Losses)	Fair Value March 31, 2018
	(In thousands)			
Contingent consideration associated with acquisitions	2,806	(1,319)	(145)	1,342

Net Income (Loss) Per Common Share

The Company calculates net income (loss) per share in accordance with ASC 260, Earnings Per Share ("ASC 260"). Under ASC 260, basic net income (loss) per common share is calculated by dividing net income (loss) by the weighted-average number of common shares outstanding during the reporting period. The weighted average number of shares of common stock outstanding includes vested restricted stock awards. Diluted net income (loss) per share ("EPS") reflects the potential dilution that could occur assuming conversion or exercise of all dilutive unexercised stock options. The dilutive effect of stock options and restricted stock awards was determined using the treasury stock method. Under the treasury stock method, the proceeds received from the exercise of stock options and restricted stock awards, the amount of compensation cost for future service not yet recognized by the Company and the amount of tax benefits that would be recorded as income tax expense when the stock options become deductible for income tax purposes are all assumed to be used to repurchase shares of the Company's common stock. Stock options and restricted stock awards are not included in the computation of diluted net income (loss) per share when they are antidilutive. Common stock outstanding reflected in the Company's condensed consolidated balance sheets includes restricted stock awards outstanding. Securities that may participate in undistributed net income with common stock are considered participating securities.

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The following schedule presents the calculation of basic and diluted net income per share:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2019	2018	2019	2018
	(In thousands except share and per share data)			
Basic net income per share computation:				
Net income attributable to common stockholders	$ 18,462	$ 13,070	$ 33,892	$ 18,273
Weighted average common shares — basic	39,008,990	39,644,074	38,753,236	39,366,497
Basic net income per share	$ 0.47	$ 0.33	$ 0.87	$ 0.46
Diluted net income per share computation:				
Net income attributable to common stockholders	$ 18,462	$ 13,070	$ 33,892	$ 18,273
Share computation:				
Weighted average common shares — basic	39,008,990	39,644,074	38,753,236	39,366,497
Effect of dilutive stock options and restricted stock awards	2,744,333	1,122,129	1,795,723	1,404,940
Weighted average common shares — diluted	41,753,323	40,766,203	40,548,959	40,771,437
Diluted net income per share	$ 0.44	$ 0.32	$ 0.84	$ 0.45

During the three months ended March 31, 2019 and 2018, 119,343 and 1,422,500 shares issuable in connection with stock options and restricted stock were excluded from the diluted income per share calculation because the effect would have been antidilutive. During the nine months ended March 31, 2019 and 2018, 148,355 and 1,086,880 shares were excluded, respectively. As of March 31, 2019, the Company had 45,542,026 shares issued and 40,207,283 shares outstanding.

Reclassification

Certain previous year amounts have been reclassified to conform with current year presentations, as related to the statement of cash flows.

4. Income Taxes

The provision for income taxes is based on earnings reported in the condensed consolidated financial statements. A deferred income tax asset or liability is determined by applying currently enacted tax laws and rates to the expected reversal of the cumulative temporary differences between the carrying value of assets and liabilities for financial statement and income tax purposes. Deferred income tax expense or benefit is measured by the change in the deferred income tax asset or liability during the period. For the three months ended March 31, 2019 and 2018, the Company's effective income tax rate was 23.8% and 34.7%, respectively, and for the nine months ended March 31, 2019 and 2018, the rate was 22.2% and (11.5)%, respectively.

On December 22, 2017, the Tax Cuts and Job Act (the "Tax Act") was enacted into law, which among other provisions, reduced the U.S. statutory federal income tax rate from 35% to 21%. The Company has included the amount for the impact of the re-measurement of the Company's net U.S. deferred tax liabilities and the transition tax on the Company's accumulated unremitted foreign earnings in the Company's financial statements for the year ended June 30, 2018.

The SEC staff issued Staff Accounting Bulletin No. 118 ("SAB 118") to allow the registrant to record provisional amounts during a measurement period not to extend beyond one year of the enactment date. The Company has included in its taxable income the provisional impact related to the one-time transition tax and the revaluation of deferred tax balances and included these estimates in its consolidated financial statements for the year ended June 30, 2018. During the three months ended December 31, 2018, the Company completed the analysis of the various provisions of the Tax

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Act and recognized immaterial adjustments to the provisional amounts. The Company included these adjustments within income tax expense from continuing operations.

5. Long-term Obligations

Capital Leases

The Company incurs capital lease obligations for student computers and peripherals under agreements with PNC Equipment Finance, LLC (“PNC”) and Banc of America Leasing & Capital, LLC (“BALC”). As of March 31, 2019 and June 30, 2018, the outstanding balance of capital leases (as discussed in more detail below) was $31.2 million and $26.0 million, respectively, with lease interest rates ranging from 1.97% to 4.05%. The gross carrying value of leased student computers as of March 31, 2019 and June 30, 2018 was $52.9 million and $42.2 million, respectively. The accumulated depreciation of leased student computers as of March 31, 2019 and June 30, 2018 was $30.1 million and $26.0 million, respectively.

Individual leases under the agreement with PNC include 36-month payment terms, at varying rates, with a $1 purchase option at the end of each lease term. The Company has pledged the assets financed to secure the outstanding leases.

The Company’s $16.0 million agreement with BALC that was executed in December 2018, was increased to $25 million in February 2019 and extended through December 2019 at a fluctuating rate of LIBOR plus 1.25%. Individual leases with BALC include 12-month payment terms, a fixed rate of 4.05%, and a $1 purchase option at the end of each lease term. The Company has pledged the assets financed to secure the outstanding leases.

The following is a summary as of March 31, 2019 of the present value of the net minimum lease payments on capital leases under the Company’s commitments:

As of June 30,	Capital Leases

	(in thousands)
2019 (remaining three months)	$ 7,859
2020	18,987
2021	4,819
2022	340
Total minimum payments	32,005
Less amount representing interest (imputed weighted average capital lease interest rate of 3.67%)	(808)
Net minimum payments	31,197
Less current portion	(24,499)
Present value of minimum payments, less current portion	$ 6,698

6. Equity Transactions

On December 15, 2016 (the “Effective Date”), the Company’s stockholders approved the 2016 Incentive Award Plan (the “Plan”). The Plan is designed to attract, retain and motivate employees who make important contributions to the Company by providing such individuals with equity ownership opportunities. Awards granted under the Plan may include stock options, stock appreciation rights, restricted stock, restricted stock units, and other stock-based awards. Under the Plan, the following types of shares go back into the pool of shares available for issuance:

· unissued shares related to forfeited or cancelled restricted stock and stock options from Plan awards and Prior Plan awards (that were outstanding as of the Effective Date); and

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- shares tendered to satisfy the tax withholding obligation related to the vesting of restricted stock (but not stock options).

Unlike the Company's 2007 Equity Incentive Award Plan (the "Prior Plan"), the Plan has no evergreen provision to increase the shares available for issuance; any new shares would require stockholder approval. The Prior Plan expired in October 2017; however, with the approval of the Plan, the Company will no longer award equity from the Prior Plan. As of March 31, 2019, the remaining aggregate number of shares of the Company's common stock authorized for future issuance under the Plan was 2,098,278. As of March 31, 2019, there were 4,823,629 shares of the Company's common stock that remain outstanding or nonvested under the Plan and Prior Plan.

Stock Options

Stock option activity including stand-alone agreements during the nine months ended March 31, 2019 was as follows:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value
Outstanding, June 30, 2018	1,199,307	$ 19.97		
Granted	—	—		
Exercised	(106,490)	20.50		
Forfeited or canceled	(13,000)	29.82		
Outstanding, March 31, 2019	1,079,817	$ 19.80	2.91	$ 15,457,203
Exercisable, March 31, 2019	1,046,552	$ 20.00	2.86	$ 14,792,194

The total intrinsic value of options exercised during the nine months ended March 31, 2019 and 2018 was $0.7 million and zero, respectively.

As of March 31, 2019, there was $0.2 million of total unrecognized compensation expense related to nonvested stock options granted. The cost is expected to be recognized over a weighted average period of 0.4 years. During the three months ended March 31, 2019 and 2018, the Company recognized $0.2 million and $0.2 million, respectively, of stock-based compensation expense related to stock options. During the nine months ended March 31, 2019 and 2018, the expense was $0.5 million and $1.0 million, respectively.

Restricted Stock Awards

Restricted stock award activity during the nine months ended March 31, 2019 was as follows:

	Shares	Weighted Average Grant-Date Fair Value
Nonvested, June 30, 2018	1,676,907	$ 15.12
Granted	822,333	18.34
Vested	(918,196)	14.67
Canceled	(227,731)	17.42
Nonvested, March 31, 2019	1,353,313	$ 16.99

Performance Based Restricted Stock Awards (included above)

During the nine months ended March 31, 2019, 37,378 new performance based restricted stock awards were granted and 271,455 remain nonvested at March 31, 2019. During the nine months ended March 31, 2019, 312,383 performance based restricted stock awards vested. Vesting of the performance based restricted stock awards is contingent on the achievement of certain financial performance goals and service vesting conditions.

During fiscal year 2018, the Company granted performance based restricted stock awards which were subject to the achievement of a target free cash flow metric in fiscal year 2018 and adjusted upwards or downwards based on the Company's relative total shareholder return for fiscal year 2018 ranked against other companies in the Russell 2000 Index. On August 1, 2018, the free cash flow metric was certified by the Compensation Committee of the Board of Directors as Outperform and the total shareholder return metric was certified as below Threshold resulting in the performance based restricted stock awards granted at 100% of target, or 46,845 shares earned by Company executives.

Equity Incentive Market Based Restricted Stock Awards (included above)

During fiscal year 2017, the Company granted equity incentive market based restricted stock awards which were subject to the attainment of an average stock price of $14.35 for 30 consecutive days after the date of the Company's earnings release for the fourth quarter and fiscal year ended June 30, 2017. During the nine months ended March 31, 2019, 18,400 of these equity incentive market based restricted stock awards vested. As of March 31, 2019, 6,800 equity incentive market based restricted stock awards remain nonvested.

Service Based Restricted Stock Awards (included above)

During the nine months ended March 31, 2019, 784,955 new service based restricted stock awards were granted and 1,075,058 remain nonvested at March 31, 2019. During the nine months ended March 31, 2019, 587,413 service based restricted stock awards vested.

Summary of All Restricted Stock Awards

As of March 31, 2019, there was $17.2 million of total unrecognized compensation expense related to nonvested restricted stock awards. The cost is expected to be recognized over a weighted average period of 1.7 years. The fair value of restricted stock awards granted for the nine months ended March 31, 2019 and 2018 was $15.1 million and

$17.5 million, respectively. The total fair value of shares vested for the nine months ended March 31, 2019 and 2018 was $19.6 million and $21.7 million, respectively. During the three months ended March 31, 2019 and 2018, the Company recognized $2.6 million and $3.9 million, respectively, of stock-based compensation expense related to restricted stock awards. During the nine months ended March 31, 2019 and 2018, the expense was $9.5 million and $11.7 million, respectively.

Performance Share Units ("PSU")

Certain PSUs vest upon achievement of performance criteria associated with a Board-approved Long Term Incentive Plan ("LTIP") and continuation of employee service over a defined period. The level of performance will determine the number of PSUs earned as measured against threshold, target and outperform achievement levels of the LTIP. Each PSU represents the right to receive one share of the Company's common stock, or at the option of the Company, an equivalent amount of cash, and is classified as an equity award in accordance with ASC 718.

In addition to the LTIP performance conditions, there is a service vesting condition which is dependent upon continuing service by the grantee as an employee of the Company, unless the grantee is eligible for earlier vesting upon a change in control and qualifying termination, as defined by the PSU agreement. For equity performance awards, including the PSUs, subject to graduated vesting schedules for which vesting is based on achievement of a performance metric in addition to grantee service, stock-based compensation expense is recognized on an accelerated basis by treating each vesting tranche as if it was a separate grant.

Fiscal Year 2016 LTIP

During fiscal year 2016, the Company granted PSUs under a LTIP that was driven by an academic measure and a lifetime value measure. Thirty percent of the earned award ("Tranche #1") vested quarterly beginning November 15, 2017 and seventy percent of the earned award ("Tranche #2") vested on August 15, 2018, in both cases dependent upon continuing service by the grantee as an employee of the Company.

For the year ended June 30, 2017, the Company determined the achievement of the performance condition was probable on Tranche #1. Achievement was believed to be probable at the highest level which equals 150% of the target award. Therefore, the Company recorded $3.8 million of expense for the period of grant date (September 2015) through June 2017. On August 2, 2017, the Compensation Committee of the Company's Board of Directors certified that as of August 1, 2017, 97% of the MPS schools were not in academic jeopardy, as determined by the independent members of the Academic Committee of the Board of Directors on that date, and that the Academic Metric for Tranche #1 of the LTIP was achieved at the Outperform level. This resulted in 446,221 PSUs (including 138,241 additional PSUs due to the Outperform level) earned by the participants, consisting of 90,000 PSUs for Mr. Davis and 70,021 PSUs for Mr. Udell.

For the year ended June 30, 2018, the Company determined the achievement of one of the two performance conditions were probable on Tranche #2 at Target. Tranche #2 is comprised of two performance measures, an academic measure (similar to Tranche #1) and a lifetime value measure. Therefore, the Company recorded $3.9 million of expense for the period of grant date (September 2015) through June 2018. On August 1, 2018, the Compensation Committee of the Company's Board of Directors certified that as of August 1, 2018, the Company achieved less than 1% below Target for the academic measure. This resulted in 349,996 PSUs (including a reduction of 15,345 PSUs due to the below Target performance) earned by the participants, consisting of 76,640 PSUs for Mr. Davis and 59,626 PSUs for Mr. Udell. The Compensation Committee also certified that achievement of the performance conditions associated with the lifetime value measure of Tranche #2 were not met and therefore no expense was recorded.

Fiscal Year 2019 LTIP

During the third quarter of fiscal 2019, the Company granted 263,936 PSUs at target under a LTIP that was driven by certain revenue targets and enrollment levels, as well as students' academic progress. These PSUs had a grant date fair value of $7.9 million, or $30.05 per share. Forty-five percent of the earned award is based on students' academic progress ("Tranche #1") and twenty-five percent of the earned award is based on certain enrollment levels ("Tranche 2"), both of which will vest on October 15, 2021. The remaining thirty percent of the earned award is based on certain revenue targets ("Tranche #3") will vest on August 15, 2022. In all cases, vesting is dependent upon continuing service by the grantee as an employee of the Company. The Company determined the achievement of the performance conditions associated with all three tranches were not probable and therefore no expense was recorded during the three and nine months ended March 31, 2019.

Fiscal Year 2019 SPP

During fiscal year 2019, the Company adopted a new long-term shareholder performance plan (“2019 SPP”) that provides for incentive award opportunities to its key senior executives. The awards were granted in the form of PSUs and will be earned based on the Company’s market capitalization growth over a completed three-year performance period. The 2019 SPP was designed to provide the executives with a percentage of shareholder value growth. No amounts will be earned if total stock price growth over the three-year period is below 25% (7.6% annualized). An amount of 6% of total value growth will be earned based on achieving total stock price growth of 33% (10% annualized) and a maximum of 7.5% of total value growth will be earned if total stock price growth equals or exceeds 95% (25% annualized).

During the first quarter of fiscal year 2019, the Company granted 1,766,932 PSUs from the 2019 SPP with a grant date fair value of $10.5 million, or $5.97 per share, based on the highest level of performance. During the third quarter of fiscal year 2019, there was a modification of certain terms of the original grant which resulted in an increase of 23,670 shares with a fair value of $0.4 million, or $17.45 per share. Additionally, the Company granted 317,703 PSUs from the 2019 SPP with a grant date fair value of $6.3 million, or $19.76 per share, based on the highest level of performance. The final amount of PSUs will be determined (and vesting will occur) based on the 30-day average price of the Company’s stock subsequent to seven days after the release of fiscal year 2021 results. The fair value was determined using a Monte Carlo simulation model and will be amortized on a straight-line basis over the vesting period.

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Summary of All Performance Share Units

As of March 31, 2019, there was $14.9 million of total unrecognized compensation expense related to nonvested PSUs. The cost is expected to be recognized over a weighted average period of 2.5 years. During the three months ended March 31, 2019 and 2018, the Company recognized $1.3 million and $0.6 million, respectively, of stock-based compensation expense related to PSUs. During the nine months ended March 31, 2019 and 2018, the expense was $2.4 million and $4.1 million, respectively.

Performance share unit activity during the nine months ended March 31, 2019 was as follows:

	Shares	Weighted Average Grant-Date Fair Value
Nonvested, June 30, 2018	708,979	$ 13.15
Granted	2,372,241	10.61
Vested	(427,954)	13.24
Canceled	(281,025)	13.02
Nonvested, March 31, 2019	2,372,241	$ 10.61

Deferred Stock Units (“DSU”)

During fiscal year 2019, the Company granted 18,258 DSUs at a weighted average grant-date fair value of $25.41. The DSUs vest on the grant-date anniversary and are settled in the form of shares of common stock issued to the holder upon separation from the Company. The DSUs are excluded from the tables above. As of March 31, 2019, 18,258 DSUs remain nonvested.

7. Related Party Transactions

During fiscal years 2019 and 2018, the Company contributed to The Foundation for Blended and Online Learning ("Foundation"). The Foundation is a related party as an executive officer of the Company serves on the Board of the Foundation. For the three months ended March 31, 2019 and 2018, contributions made by the Company to the Foundation were $0.1 million and $0.0 million, respectively, and $0.9 million and $0.3 million for the nine months ended March 31, 2019 and 2018, respectively.

8. Commitments and Contingencies

Litigation

In the ordinary conduct of the Company's business, the Company is subject to lawsuits, arbitrations and administrative proceedings from time to time. The Company believes that the outcome of any existing or known threatened proceedings, even if determined adversely, should not have a material adverse effect on the Company's business, financial condition, liquidity or results of operations.

On July 20 and September 15, 2016, two securities class action lawsuits—captioned Babulal Tarapara v. K12 Inc., et al., Case No. 3:16-cv-04069, and Gil Tuinenburg v. K12 Inc., et al., Case No. 3:16-cv-05305, respectively—were filed against the Company, two of its officers and one of its former officers in the United States District Court for the Northern District of California. On October 6, 2016, the Court consolidated the cases and recaptioned the matter as In Re K12 Inc. Securities Litigation, Master File No. 4:16-cv-04069-PJH. On August 30, 2017, the Court dismissed the plaintiffs' claims alleging false or misleading statements and omissions related to Scantron results and the quality and effectiveness of K12's academic services and offerings. On September 5, 2018, and as a result of a Court ordered mediation, the parties reached an agreement in principle to settle the remaining claim concerning disclosure of a notice

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of non-automatic renewal of a managed school contract. Although we believe that the remaining claim in this matter lacked merit, we agreed to settle the case to avoid continued distraction and management time, and our insurance carriers agreed to pay $3.5 million into a settlement fund for the alleged class and attorneys' fees and costs. The Court granted preliminary approval of the settlement on February 14, 2019, and a final hearing is scheduled for July 10, 2019.

Employment Agreements

The Company has entered into employment agreements with certain executive officers that provide for severance payments and, in some cases other benefits, upon certain terminations of employment. Except for the agreement with the Company's Chairman and Chief Executive Officer with an amended extended term to September 30, 2019, all other agreements provide for employment on an "at-will" basis. If the employee resigns for "good reason" or is terminated without cause, the employee is entitled to salary continuation, and in some cases benefit continuation, for varying periods depending on the agreement.

Off-Balance Sheet Arrangements

As of March 31, 2019, the Company provided guarantees of approximately $1.7 million related to lease commitments on the buildings for certain of the Company's schools.

In addition, the Company contractually guarantees that certain schools under the Company's management will not have annual operating deficits and the Company's management fees from these schools may be reduced accordingly to cover any school operating deficits.

Other than these lease and operating deficit guarantees, the Company did not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

9. Restructuring

In the third quarter of fiscal year 2017, the Company exited three facilities that were no longer being utilized, which were subject to operating leases.

The present value of the remaining lease payments was calculated using a credit adjusted risk-free rate and estimated sublease rentals for each lease. In aggregate, during fiscal year 2017, the Company recorded an impairment of $5.4 million for the three leases. The current portion of the liability of $1.7 million was included in accrued liabilities and the long-term portion of $3.7 million was included in other long-term liabilities on the condensed consolidated balance sheet as of March 31, 2017. In addition to the lease impairment, the Company accelerated the useful life of each lease's property and equipment to the cease-use date and recorded accelerated depreciation of $1.4 million. The Company also wrote off the deferred rent and the liability for tenant improvements associated with each lease which resulted in income of $1.9 million. The $4.9 million net impact of these actions was recorded in selling, administrative, and other operating expenses in the condensed consolidated statements of operations.

The following table summarizes the activity during the nine months ended March 31, 2019:

Description	Initial Value	Balance at June 30, 2018	Payments, net of sublease income	Accretion Expense	Adjustments	Balance at March 31, 2019
	(In thousands)					
Lease #1	$ 1,652	$ 1,092	$ (275)	$ 22	$ —	$ 839
Lease #2	1,311	475	(355)	5	—	125
Lease #3	2,443	1,191	6	24	—	1,221
Total	$ 5,406	$ 2,758	$ (624)	$ 51	$ —	$ 2,185

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10. Investments

Investment in Tallo (FKA STEM Premier Inc.)

In August 2018, the Company invested $6.7 million for a 39.5% minority interest in Tallo, Inc. (“Tallo”). This investment in preferred stock that contains additional rights over common stock and has no readily determinable fair value, was recorded at cost and will be adjusted, as necessary, for impairment. In the event Tallo issues equity at a materially different price than what the Company paid, the Company would also assess changing the carrying value. Tallo also issued a convertible note to the Company for $5.0 million that will be accounted for as an available-for-sale debt security and adjusted to fair value quarterly. The note bears interest at the mid-term Applicable Federal Rate plus 25 bps per annum with a maturity of 48 months. The note is convertible at the Company’s option into 3.67 million Series D Preferred Shares that would give the Company an effective ownership of 56% if exercised. The Company’s investment in Tallo is included in deposits and other assets on the condensed consolidated balance sheet.

11. Supplemental Disclosure of Cash Flow Information

	Nine Months Ended March 31,	
	2019	2018
	(In thousands)	
Cash paid for interest	$ 862	$ 546
Cash paid for taxes	$ 1,010	$ 11,211
Supplemental disclosure of non-cash financing activities:		
Property and equipment financed by capital lease obligations, including student peripherals	$ 19,076	$ 16,119
Supplemental disclosure of non-cash investing activities:		
Stock-based compensation expense capitalized on software development	$ 101	$ 1,053
Stock-based compensation expense capitalized on curriculum development	$ 176	$ 835
Business combinations:		

Current assets	$ —	$ 209
Intangible assets	—	695
Goodwill	—	2,983
Assumed liabilities	—	(734)
Deferred revenue	—	(361)

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Certain statements in Management's Discussion and Analysis or MD&A, other than purely historical information, including estimates, projections, statements relating to our business plans, objectives and expected operating results, and the assumptions upon which those statements are based, are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These forward-looking statements generally are identified by the words "believe," "project," "expect," "anticipate," "estimate," "inter "strategy," "plan," "may," "should," "will," "would," "will be," "will continue," "will likely result," and similar expressions. H results may not indicate future performance. Our forward-looking statements reflect our current views about future events, are based on assumptions and are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from those contemplated by these statements. Factors that may cause differences between actual results and those contemplated by forward-looking statements include, but are not limited to, those discussed in "Risk Factors" in Part I, Item 1A, of our Annual Report on Form 10-K for the fiscal year ended June 30, 2018, which we refer to as our Annual Report. We undertake no obligation to publicly update or revise any forward-looking statements, including any changes that might result from any facts, events or circumstances after the date hereof that may bear upon forward-looking statements. Furthermore, we cannot guarantee future results, events, levels of activity, performance or achievements.

This MD&A is intended to assist in understanding and assessing the trends and significant changes in our results of operations and financial condition. As used in this MD&A, the words, "we," "our" and "us" refer to K12 Inc. and its consolidated subsidiaries. This MD&A should be read in conjunction with our condensed consolidated financial statements and related notes included elsewhere in this report, as well as the consolidated financial statements and MD&A of our Annual Report. The following overview provides a summary of the sections included in our MD&A:

· Executive Summary — a general description of our business and key highlights of the nine months ended March 31, 2019.

· Critical Accounting Policies and Estimates — a discussion of critical accounting policies requiring judgments and estimates.

· Results of Operations — an analysis of our results of operations in our condensed consolidated financial statements.

· Liquidity and Capital Resources — an analysis of cash flows, sources and uses of cash, commitments and contingencies and quantitative and qualitative disclosures about market risk.

Executive Summary

We are a technology-based education company and offer proprietary and third party curriculum, software systems and educational services designed to facilitate individualized learning for students primarily in kindergarten through 12th grade, or K-12. Our learning systems combine curriculum, instruction and related support services to create an individualized learning approach well-suited for virtual and blended public schools, school districts, charter schools, and private schools that utilize varying degrees of online and traditional classroom instruction, and other educational applications. These products and services are provided through three lines of business: Managed Public School Programs; Institutional; and Private Pay Schools and Other.

Managed Public School Programs accounted for approximately 88% of our revenues during the nine months ended March 31, 2019. The Managed Public School Programs offer an integrated package of systems, services, products, and professional expertise that we manage to support online or blended public schools, including: administrative support (e.g., budget proposals, financial reporting, student data reporting, and staff recruitment), information technology, academic support services, curriculum, learning systems, and instructional services. We provide our Managed Public School Programs to virtual and blended public charter schools and school districts. These contracts are negotiated with and approved by the governing authorities of the customer. The duration of the Managed Public School Program service agreements are typically 2-5 years, and most provide for automatic renewals absent a customer notification within a negotiated time frame. During any fiscal year, the Company may enter into new Managed Public School agreements, receive non-automatic renewal notices and negotiate replacement agreements, terminate the contract or receive notice of

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termination, or transition a school between a Managed Public School Program and a Non-managed Public School Program. The governing boards may also establish school policies and other terms and conditions over the course of a contract, such as enrollment parameters. The authorizers who issue the charters to our Managed Public School customers can renew, revoke, or modify those charters as well.

As of March 31, 2019, we provided our Managed Public School Programs to 75 schools in a majority of states throughout the United States and the District of Columbia. During this period, we entered into a new contract in one state to open a Managed Public School Program, auto renewed eight agreements for schools in five states, are now engaged in renewal negotiations in one state and completed renewal negotiations in five states, with varying degrees of contract modifications. At four schools, the applicable authorizer invoked its right not to renew its agreement for the upcoming 2019-2020 school year and thereafter, and therefore such schools will close unless a new authorizer is found.

Our Institutional business consists of both Non-managed Public School Programs and Institutional Software and Services. Unlike Managed Public School Programs, the Institutional business does not offer primary administrative support services, which remain the responsibility of the school district or the school customer. Rather, the Institutional business offers options whereby the school can contract for instruction, curriculum, supplemental courses, marketing, enrollment and other educational services. The Institutional Software and Services offerings provide school districts, individual public schools, charter schools and private schools with educational solutions. In addition to curriculum, systems and programs, the services we offer to Institutional customers can also assist them in launching their own online and blended learning programs tailored to their own requirements and may include instructional support, reporting tools and content libraries. For the 2017-18 school year, we served school districts or individual schools in all 50 states and the District of Columbia, including those states where the regulatory environment restricts or prohibits statewide online programs.

Our Private Pay Schools and Other include three accredited, tuition-based private schools that meet a range of student needs from individual course credit recovery to college preparatory programs. These schools are: (1) K12 International Academy, an online private school that enables us to offer students worldwide the same full-time education programs and curriculum that we provide to the virtual and blended public schools, (2) The Keystone School, a private school that offers online and correspondence courses, and (3) the George Washington University Online High School, a school that offers a college preparatory program and is designed for middle and high school students who are seeking a challenging academic experience.

For the nine months ended March 31, 2019, revenues increased to $759.4 million from $678.9 million in the prior year, an increase of 11.9%. Over the same period, operating income increased to $42.8 million, from $15.7 million in the prior year. Net income to common stockholders was $33.9 million, as compared to $18.3 million in the prior year.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“GAAP”) requires us to make estimates and assumptions about future events that affect the amounts reported in our condensed consolidated financial statements and accompanying notes. Future events and their effects cannot be determined with certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results could differ from those estimates, and any such differences may be material to our consolidated financial statements. Critical accounting policies are disclosed in our Annual Report. Other than revenue recognition (discussed below), there have been no significant updates to our critical accounting policies disclosed in our Annual Report.

Contracts with Customers

Revenues are principally earned from contractual agreements to provide online curriculum, books, materials, computers and management services to virtual and blended schools, traditional public schools, school districts, and private schools through its three lines of business; Managed Public School Programs, Institutional, and Private Pay and Other.

Under ASC 606, revenue is recognized when control of the promised goods or services is transferred to the Company's customers, in an amount that reflects the consideration it expects to be entitled to in exchange for those goods or services using the following steps:

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- identify the contract, or contracts, with a customer;
- identify the performance obligations in the contract;
- determine the transaction price;
- allocate the transaction price to the performance obligations in the contract; and
- recognize revenue when, or as, the Company satisfies a performance obligation.

Revenue Recognition

Managed Public School Programs

The Company provides an integrated package of systems, services, products, and professional expertise that we manage to support online or blended public schools. Contractual agreements generally span multiple years with performance obligations being isolated to annual periods. Customers for these programs can obtain the administrative support, information technology, academic support services, online curriculum, learning systems platforms and instructional services under the terms of a negotiated service agreement. The schools receive funding on a per student basis from the state in which the public school or school district is located. Shipments of materials for schools that occur in the fourth fiscal quarter and for the upcoming school year are recorded in deferred revenue.

The Company generates revenues under contracts with virtual and blended public schools and include the following components, where required:

- providing each of a school's students with access to the Company's online school and lessons;
- offline learning kits, which include books and materials to supplement the online lessons;
- the use of a personal computer and associated reclamation services;
- internet access and technology support services;
- instruction by a state-certified teacher; and
- management and technology services necessary to support a virtual public or blended school. In certain managed school contracts, revenues are determined directly by per enrollment funding.

To determine the pro rata amount of revenue to recognize in a fiscal quarter, the Company estimates the total funds each school will receive in a particular school year. Total funds for a school are primarily a function of the number of students enrolled in the school and established per enrollment funding levels, which are generally published on an annual basis by the state or school district. The Company reviews its estimates of funding periodically, and revises as necessary, amortizing any adjustments to earned revenues over the remaining portion of the fiscal year. Actual school funding may vary from these estimates and the impact of these differences could impact the Company's results of operations. Since the end of the school year coincides with the end of the Company's fiscal year, annual revenues are generally based on actual school funding and actual costs incurred (including costs for the Company's services to the schools plus other costs the schools may incur) in the calculation of school operating losses. The Company's schools' reported results are subject to annual school district financial audits, which incorporate enrollment counts, funding and other routine financial audit considerations. The results of these audits are incorporated into the Company's monthly funding estimates for the three and nine months ended March 31, 2019 and 2018.

Each state and/or school district has variations in the school funding formulas and methodologies that it uses to estimate funding for revenue recognition at its respective schools. As the Company estimates funding for each school, it takes into account the state definition for count dates on which reported enrollment numbers will be used for per pupil funding. The parameters the Company considers in estimating funding for revenue recognition purposes include school district count definitions, withdrawal rates, average daily attendance, special needs enrollment, student demographics, academic progress and historical completion, student location, funding caps and other state specified categorical program funding.

Under the contracts where the Company provides services to schools, the Company has generally agreed to absorb any operating losses of the schools in a given school year. These school operating losses represent the excess of costs incurred over revenues earned by the virtual or blended public school as reflected on its respective financial statements, including Company charges to the schools. To the extent a school does not receive funding for each student enrolled in the school, the school would still incur costs associated with serving the unfunded enrollment. If losses due to unfunded enrollments result in a net operating loss for the year that loss is reflected as a reduction in the revenues and net receivables that the Company collects from the school. A school net operating loss in one year does not necessarily mean

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the Company anticipates losing money on the entire contract with the school. However, a school operating loss may reduce the Company’s ability to collect its management fees in full and recognized revenues are reduced accordingly to reflect the expected cash collections from such schools. The Company amortizes the estimated school operating loss against revenues based upon the percentage of actual revenues in the period to total estimated revenues for the fiscal year.

Management periodically reviews its estimates of full-year school revenues and operating expenses, and amortizes the net impact of any changes to these estimates over the remainder of the fiscal year. Actual school operating losses may vary from these estimates or revisions, and the impact of these differences could have a material impact on results of operations.

The Company has certain contracts where it is responsible for substantially all of the expenses incurred by the school. For these contracts, the Company records both revenue and expenses incurred by the schools.

Institutional

The products and services delivered to the Company’s Institutional customers include curriculum and technology for full-time virtual and blended programs, as well as instruction, curriculum and associated materials, supplemental courses, marketing, enrollment and other educational services. Each of these contracts are considered to be one performance obligation under ASC 606.

The Company provides certain online curriculum and services to schools and school districts under subscription agreements. Revenues from the licensing of curriculum under subscription arrangements are recognized on a ratable basis over the subscription period. Revenues from professional consulting, training and support services are deferred and recognized ratably over the service period.

Private Pay Schools and Other

Private Pay Schools and Other revenues are generated from individual customers who prepay and have access for one to two years to company-provided online curriculum. Each of these contracts are considered to be one performance obligation under ASC 606. The Company recognizes these revenues pro rata over the maximum term of the customer contract.

Performance Obligations

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer, and is the unit of account in ASC 606. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. For the majority of its contracts, the Company's performance obligations are satisfied over time, as the Company delivers, and the customer receives the services, over the service period of the contract. The Company's payment terms are generally net 30 or net 45, but can vary depending on when the school receives its funding from the state.

Significant Judgments

The Company determined that the majority of its contracts with customers contain one performance obligation. The Company markets the products and services as an integrated package building off its curriculum offerings. It does not market distinct products or services to be sold independently from the curriculum offering.

The Company has determined that the time elapsed method as described under ASC 606 is the most appropriate measure of progress towards the satisfaction of the performance obligation. The Company delivers the integrated products and services package related to its Managed Public School Programs largely over the course of the Company's fiscal year. This package includes enrollment, marketing, teacher training, etc. in addition to the core curriculum and instruction. All of these activities are necessary and contribute to the overall education of its students, which occurs evenly throughout the year. Accordingly, the Company will recognize revenue on a straight-line basis.

As discussed above, the Company estimates the total funds each school will receive in a particular school year and the amount of full-year school revenues and operating expenses to determine the amount of revenue the Company will

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receive. To the extent the estimates change during the year, the cumulative impact of the change is recognized over the remaining service period.

Results of Operations

We have three lines of business: Managed Public School Programs; Institutional; and Private Pay Schools and Other.

Managed Public School Programs	Institutional	Private Pay Schools and Other
Virtual public schools	Non-managed Public School Programs	Managed private schools
		—K12 International Academy
Blended public schools	Institutional software and services	—George Washington University Online High School
		—The Keystone School

Enrollment Data

The following table sets forth total enrollment data for students in our Managed Public School Programs and Non-managed Public School Programs. Our Managed Public School Programs offer an integrated package of systems, services, products, and professional expertise that we manage in order to support an online or blended public school. Customers for these programs can obtain the administrative support, information technology, academic support services, online curriculum, learning system platforms and instructional services under the terms of a negotiated service agreement. Unlike Managed Public School Programs, Non managed Public School Programs do not offer primary administrative support services, which remain the responsibility of the school district or the school customer. Rather, Non-Managed Public School Programs offer options whereby the school can contract for instruction, curriculum, supplemental courses, marketing, enrollment and other educational services. Enrollments in Managed Public School Programs on average generate more revenues than enrollments served through our Institutional business where we provide limited or no management services. We do not award or permit incentive compensation to be paid to our public school program enrollment staff or contractors based on the number of students enrolled. If the mix of enrollments changes, our revenues will be impacted to the extent the average revenues per enrollments are significantly different.

	Three Months Ended March 31,		2019 / 2018		Nine Months Ended March 31,		2019 / 2018	
	2019	2018	Change	Change %	2019	2018	Change	Change %

(In thousands, except percentages)

Managed Public School Programs (1)(2)	117.1	110.8	6.3	5.7%	117.0	109.8	7.2	6.6%
Non-managed Public School Programs (1)	24.5	24.3	0.2	0.8%	24.0	24.1	(0.1)	(0.4%)

(1) If a school changes from a Managed to a Non-managed Public School Program, the corresponding enrollment classification would change in the period in which the contract arrangement changed. Enrollments reported for the first quarter are equal to the official count date number, which is the first Wednesday of October in a year, or October 3, 2018 for the first quarter of fiscal year 2019 and October 4, 2017 for the first quarter of fiscal year 2018.

(2) Managed Public School Programs include enrollments for which K12 receives no public funding or revenue.

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Revenues by Business Lines

Revenues are captured by business line based on the underlying customer contractual agreements. Periodically, a customer may change business line classification. Alternatively, a Managed Public School may become a Non-managed Public School and seek to renegotiate an existing contract or the scope of services we provide to the school. A re-classification of a public school from one business line to another would be reflected in our disclosure of revenues and total student enrollment between the two business lines. For example, a district that purchases a single course (Institutional business customer) may decide to convert to a full time virtual school program (Managed Public School customer). Changes in business line classification occur at the time the contractual agreement is modified. The mix of our revenue between our Managed Public School Programs and our Institutional business could change as one or more of our managed schools transitions to a self-managed model such that we would provide only selected services to the school. This transition could occur due to a change in focus sought by the independent school board, or by state legislative or regulatory developments, and thus reducing revenue we generate from the school. The following represents our revenues for each of the periods indicated:

	Three Months Ended March 31,		Change 2019 / 2018		Nine Months Ended March 31,		Change 2019 / 2018	
	2019	2018	$	%	2019	2018	$	%
	(In thousands, except percentages)							
Managed Public School Programs	$ 222,645	$ 200,580	$ 22,065	11.0%	$ 665,981	$ 572,478	$ 93,503	16.3%
Institutional Non-managed Public School Programs	12,776	13,250	(474)	(3.6%)	37,398	44,401	(7,003)	(15.8%)
Institutional Software & Services	8,530	9,605	(1,075)	(11.2%)	29,515	34,500	(4,985)	(14.4%)
Total Institutional	21,306	22,855	(1,549)	(6.8%)	66,913	78,901	(11,988)	(15.2%)
Private Pay Schools and Other	9,301	9,429	(128)	(1.4%)	26,544	27,481	(937)	(3.4%)
Total Revenues	$ 253,252	$ 232,864	$ 20,388	8.8%	$ 759,438	$ 678,860	$ 80,578	11.9%

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Financial Information

The following table sets forth statements of operations data and the amounts as a percentage of revenues for each of the periods indicated:

	Three Months Ended March 31,				Nine Months Ended March 31,			
	2019		2018		2019		2018	
	(Dollars in thousands)							
Revenues	$ 253,252	100.0 %	$ 232,864	100.0 %	$ 759,438	100.0 %	$ 678,860	100.0 %
Cost and expenses								
Instructional costs and services	168,260	66.4	148,878	63.9	487,574	64.2	435,408	64.1
Selling, administrative, and other operating expenses	59,382	23.4	62,267	26.7	222,143	29.3	220,507	32.5
Product development expenses	2,343	0.9	2,002	0.9	6,916	0.9	7,276	1.1
Total costs and expenses	229,985	90.8	213,147	91.5	716,633	94.4	663,191	97.7
Income from operations	23,267	9.2	19,717	8.5	42,805	5.6	15,669	2.3
Interest income, net	754	0.3	261	0.1	1,547	0.2	535	0.1
Other income (expense), net	556	0.2	—	—	(40)	(0.0)	—	—
Income before income taxes, loss from equity method investments and noncontrolling interest	24,577	9.7	19,978	8.6	44,312	5.8	16,204	2.4
Income tax benefit (expense)	(5,842)	(2.3)	(6,935)	(3.0)	(9,858)	(1.3)	1,869	0.3
Loss from equity method investments	(273)	(0.1)	—	—	(562)	(0.1)	—	—

Net income	18,462	7.3		13,043	5.6		33,892	4.5		18,073	2.7	
Add net loss attributable to noncontrolling interest	—	—		27	0.0		—	—		200	0.0	
Net income attributable to common stockholders	$ 18,462	7.3	%	$ 13,070	5.6	%	$ 33,892	4.5	%	$ 18,273	2.7	%

Comparison of the Three Months Ended March 31, 2019 and 2018

Revenues. Our revenues for the three months ended March 31, 2019 were $253.3 million, representing an increase of $20.4 million, or 8.8%, from $232.9 million for the same period in the prior year. Managed Public School Program revenues increased $22.1 million, or 11.0%, year over year. The increase in Managed Public School Program revenues was primarily due to the 5.7% increase in enrollments and increases in the per-pupil achieved funding, school mix (distribution of enrollments by school), and other factors.

Total Institutional revenues decreased $1.5 million, or 6.8%, primarily due to a decline in software sales, partially offset by a slight increase in enrollments in our Non-managed Public School Programs. Private Pay Schools and Other revenues decreased $0.1 million, or 1.4%, over the prior year period.

Instructional costs and services expenses. Instructional costs and services expenses for the three months ended March 31, 2019 were $168.3 million, representing an increase of $19.4 million, or 13.0%, from $148.9 million for the same period in the prior year. This increase in expense was primarily due to the incremental personnel and related benefit costs due to supporting higher enrollments. Instructional costs and services expenses were 66.4% of revenues during the three months ended March 31, 2019, an increase from 63.9% for the three months ended March 31, 2018.

Selling, administrative, and other operating expenses. Selling, administrative, and other operating expenses for the three months ended March 31, 2019 were $59.4 million, representing a decrease of $2.9 million, or 4.7% from $62.3 million for the same period in the prior year. The decrease was primarily due to a decrease in personnel and related benefit costs. Selling, administrative, and other operating expenses were 23.4% of revenues during the three months ended March 31, 2019, a decrease from 26.7% for the three months ended March 31, 2018.

Product development expenses. Product development expenses for the three months ended March 31, 2019 were $2.3 million, representing an increase of $0.3 million, or 15.0% from $2.0 million for the same period in the prior year. The increase was primarily due to an increase in personnel salary expenses. Product development expenses were 0.9% of revenues during the three months ended March 31, 2019 and 2018.

Income tax benefit (expense). We had an income tax expense of $5.8 million for the three months ended March 31, 2019, or 23.8% of income before income taxes, as compared to $6.9 million, or 34.7% of income before income taxes for the same period in the prior year. The decrease in the effective tax rate for the three months ended March 31, 2019 was primarily due to the impact of the Tax Cuts and Job Act (the "Tax Act") in the prior year.

Net income. Net income was $18.5 million for the three months ended March 31, 2019, compared to $13.0 million for the same period in the prior year, representing an increase of $5.5 million.

Comparison of the Nine Months Ended March 31, 2019 and 2018

Revenues. Our revenues for the nine months ended March 31, 2019 were $759.4 million, representing an increase of $80.5 million, or 11.9%, from $678.9 million for the same period in the prior year. Managed Public School Program revenues increased $93.5 million, or 16.3%, year over year. The increase in Managed Public School Program revenues was primarily due to the 6.6% increase in enrollments and increases in the per-pupil achieved funding, school mix (distribution of enrollments by school), and other factors.

Total Institutional revenues decreased $12.0 million, or 15.2%, primarily due to a slight decrease in enrollments in our Non-managed Public School Programs, and a decline in software sales. Private Pay Schools and Other revenues decreased $0.9 million, or 3.4%, over the prior year period.

Instructional costs and services expenses. Instructional costs and services expenses for the nine months ended March 31, 2019 were $487.6 million, representing an increase of $52.2 million, or 12.0%, from $435.4 million for the same period in the prior year. This increase in expense was primarily due to the incremental personnel and related benefit costs due to supporting higher enrollments. Instructional costs and services expenses were 64.2% of revenues during the nine months ended March 31, 2019, an increase from 64.1% for the nine months ended March 31, 2018.

Selling, administrative, and other operating expenses. Selling, administrative, and other operating expenses for the nine months ended March 31, 2019 were $222.1 million, representing an increase of $1.6 million, or 0.7% from $220.5 million for the same period in the prior year. This increase was due to an increase in outside professional services and marketing, partially offset by a decrease in personnel and related benefits costs. Selling, administrative, and other operating expenses were 29.3% of revenues during the nine months ended March 31, 2019, a decrease from 32.5% for the nine months ended March 31, 2018.

Product development expenses. Product development expenses for the nine months ended March 31, 2019 were $6.9 million, representing a decrease of $0.4 million, or 5.5% from $7.3 million for the same period in the prior year. Product development expenses were 0.9% of revenues during nine months ended March 31, 2019, a decrease from 1.1% for the nine months ended March 31, 2018.

Income tax benefit (expense). We had an income tax expense of $9.9 million for the nine months ended March 31, 2019, or 22.2% of income before income taxes, as compared to a benefit of $1.9 million, or (11.5)% of income before income taxes for the same period in the prior year. The increase in the effective tax rate for the nine months ended March 31, 2019 was primarily due to the impact of the Tax Act in the prior year.

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Net income. Net income was $33.9 million for the nine months ended March 31, 2019, compared to $18.1 million for the same period in the prior year, representing an increase in net income of $15.8 million.

Liquidity and Capital Resources

As of March 31, 2019, we had net working capital, or current assets minus current liabilities, of $373.2 million. Our working capital includes cash and cash equivalents of $234.0 million and accounts receivable of $238.6 million. Our working capital provides a significant source of liquidity for our normal operating needs. Our accounts receivable balance fluctuates throughout the fiscal year based on the timing of customer billings and collections and tends to be highest in our first fiscal quarter as we begin billing for students. In addition, our cash and accounts receivable were significantly in excess of our accounts payable and short-term accrued liabilities at March 31, 2019.

We incur capital lease obligations for student computers and peripherals under agreements with PNC Equipment Finance, LLC ("PNC") and Banc of America Leasing & Capital, LLC ("BALC"). As of March 31, 2019 and June 30, 2018, the outstanding balance of capital leases was $31.2 million and $26.0 million, respectively, with lease interest rates ranging from 1.97% to 4.05%.

Individual leases with PNC include 36-month payment terms, at varying rates, with a $1 purchase option at the end of each lease term. We have pledged the assets financed to secure the outstanding leases.

Our $16.0 million agreement with BALC that was executed in December 2018, was increased to $25 million in February 2019 and extended through December 2019 at a fluctuating rate of LIBOR plus 1.25%. Individual leases with BALC include 12-month payment terms, a fixed rate of 4.05%, and a $1 purchase option at the end of each lease term. We pledged the assets financed to secure the outstanding leases.

Our cash requirements consist primarily of day-to-day operating expenses, capital expenditures and contractual obligations with respect to office facility leases, capital equipment leases and other operating leases. We expect to make future payments on existing leases from cash generated from operations. We believe that the combination of funds to be generated from operations, net working capital on hand and access to our line of credit will be adequate to finance our ongoing operations for the foreseeable future. In addition, to a lesser degree, we continue to explore acquisitions, strategic investments and joint ventures related to our business that we may acquire using cash, stock, debt, contribution of assets or a combination thereof.

Operating Activities

Net cash provided by operating activities for the nine months ended March 31, 2019 was $73.3 million compared to $55.2 million for the nine months ended March 31, 2018. The increase of $18.1 million in cash provided by operations between periods was primarily due to an increase in net income of $15.8 million.

Investing Activities

Net cash used in investing activities for the nine months ended March 31, 2019 was $48.0 million compared to $36.5 million for the nine months ended March 31, 2018, an increase of $11.5 million. The increase is primarily due to the investment in Tallo, Inc. (FKA Stem Premier, Inc.) in August 2018.

During the nine months ended March 31, 2018, we recorded an adjustment related to the capitalization of software and curriculum development. See Note 3 – "Summary of Significant Accounting Policies," to our condensed consolidated financial statements for further detail.

Financing Activities

Net cash used in financing activities for the nine months ended March 31, 2019 was $22.4 million compared to $21.7 million during the nine months ended March 31, 2018, an increase of $0.7 million. The increase is primarily due to an increase in payments of capital lease obligations incurred for the acquisition of student computers of $3.6 million, partially offset by an increase in proceeds from stock option exercises of $2.0 million.

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Off Balance Sheet Arrangements, Contractual Obligations and Commitments

As of March 31, 2019, we provided guarantees of approximately $1.7 million related to lease commitments on the buildings for certain of the Company's schools.

In addition, we contractually guarantee that certain schools under our management will not have annual operating deficits and our management fees from these schools may be reduced accordingly to cover any school operating deficits.

Other than these lease and operating deficit guarantees, we do not have any off balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Interest Rate Risk

As of March 31, 2019 and June 30, 2018, we had cash and cash equivalents totaling $234.0 million and $231.1 million, respectively. Our excess cash has been invested primarily in U.S. Treasury money market funds although we may also invest in money market accounts, government securities, corporate debt securities and similar investments. Future interest and investment income is subject to the impact of interest rate changes and we may be subject to changes, in the fair value of our investment portfolio as a result of changes in interest rates. At March 31, 2019, a 1% gross increase in interest rates earned on cash would result in a $2.3 million annualized increase in interest income.

Our short-term debt obligations under our revolving credit facility are subject to interest rate exposure; however, as we had no outstanding balance on this facility as of March 31, 2019, fluctuations in interest rates had no impact on our interest expense.

Foreign Currency Exchange Risk

We currently operate in several foreign countries, but we do not transact a material amount of business in a foreign currency. If we enter into any material transactions in a foreign currency or establish or acquire any subsidiaries that measure and record their financial condition and results of operations in a foreign currency, we will be exposed to currency transaction risk and/or currency translation risk. Exchange rates between U.S. dollars and many foreign currencies have fluctuated significantly over the last few years and may continue to do so in the future. Accordingly, we may decide in the future to undertake hedging strategies to minimize the effect of currency fluctuations on our financial condition and results of operations.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rule 13a-15(f) of the Exchange Act) that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission’s rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost benefit relationship of possible controls and procedures.

We carried out an evaluation, required by paragraph (b) of Rule 13a-15 or Rule 15d-15 under the Exchange Act, under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) or Rule 15d-15(e) of the Exchange Act) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this review, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of March 31, 2019.

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Changes to Internal Control over Financial Reporting

There have been no changes in our internal controls over financial reporting during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

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Part II. Other Information

Item 1. Legal Proceedings.

In the ordinary conduct of our business, we are subject to lawsuits, arbitrations and administrative proceedings from time to time. We vigorously defend these claims; however, no assurances can be given as to the outcome of any pending legal proceedings. We believe, based on currently available information, that the outcome of any existing or known threatened proceedings, even if determined adversely, should not have a material adverse effect on our business, financial condition, liquidity or results of operations.

On July 20 and September 15, 2016, two securities class action lawsuits—captioned Babulal Tarapara v. K12 Inc., et al., Case No. 3:16-cv-04069, and Gil Tuinenburg v. K12 Inc., et al., Case No. 3:16-cv-05305, respectively—were filed against the Company, two of its officers and one of its former officers in the United States District Court for the Northern District of California. On October 6, 2016, the Court consolidated the cases and recaptioned the matter as In Re K12 Inc. Securities Litigation, Master File No. 4:16-cv-04069-PJH. On August 30, 2017, the Court dismissed the plaintiffs' claims alleging false or misleading statements and omissions related to Scantron results and the quality and effectiveness of K12's academic services and offerings. On September 5, 2018, and as a result of a Court ordered mediation, the parties reached an agreement in principle to settle the remaining claim concerning disclosure of a notice of non-automatic renewal of a managed school contract. Although we believe that the remaining claim in this matter lacked merit, we agreed to settle the case to avoid continued distraction and management time, and our insurance carriers agreed to pay $3.5 million into a settlement fund for the alleged class and attorneys' fees and costs. This proposed settlement is subject to final documentation and court approval. The Court granted preliminary approval of the settlement on February 14, 2019, and a final settlement hearing is scheduled for July 10, 2019.

Item 1A. Risk Factors.

There have been no material changes to the risk factors disclosed in "Risk Factors" in Part I, Item 1A, of our Annual Report on Form 10-K for the fiscal year ended June 30, 2018 as filed with the SEC on August 8, 2018.

Item 2. Issuer Purchases of Equity Securities.

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

None.

Item 5. Other Information.

None.

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Item 6. Exhibits

(a) Exhibits.

Number	Description
31.1	Certification of Principal Executive Officer Required Under Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
31.2	Certification of Principal Financial Officer Required Under Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended.
32.1	Certification of Principal Executive Officer Required Under Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350.
32.2	Certification of Principal Financial Officer Required Under Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended, and 18 U.S.C. Section 1350.
101	The following financial statements and footnotes from the K12 Inc. Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2019, formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets (unaudited), (ii) Condensed Consolidated Statements of Operations (unaudited), (iii) Condensed Consolidated Statements of Comprehensive Income, (iv) Condensed Consolidated Statement of Equity (unaudited), (v) Condensed Consolidated Statements of Cash Flows (unaudited), and (vi) Notes to Condensed Consolidated Financial Statements (unaudited).

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SIGNATURES

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

	K12 Inc.
	/s/ JAMES J. RHYU
Name:	James J. Rhyu
Title:	Chief Financial Officer, Principal Accounting Officer and Authorized Signatory

Date: April 24, 2019