HEALTHSTREAM INC
Form 10-Q
May 07, 2018
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2018

Commission File No.: 000-27701

HealthStream, Inc.

(Exact name of registrant as specified in its charter)

Tennessee	**62-1443555**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

209 10th Avenue South, Suite 450

Nashville, Tennessee	**37203**
(Address of principal executive offices)	**(Zip Code)**

(615) 301-3100

(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 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 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 May 3, 2018, there were 32,302,581 shares of the registrant s common stock outstanding.

Table of Contents

Index to Form 10-Q

HEALTHSTREAM, INC.

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. ***Financial Statements***

HEALTHSTREAM, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(In thousands)

	March 31, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 156,028	$ 84,768
Marketable securities	39,346	46,350
Accounts receivable, net of allowance for doubtful accounts of $2,281 and $1,979 at March 31, 2018 and December 31, 2017, respectively	36,503	36,691
Accounts receivable unbilled	2,958	1,327
Prepaid royalties, net of amortization	17,702	16,137
Other prepaid expenses and other current assets	5,962	8,330
Current assets of discontinued operations		6,125
Total current assets	258,499	199,728
Property and equipment, net of accumulated depreciation of $25,816 and $24,392 at March 31, 2018 and December 31, 2017, respectively	8,297	8,092
Capitalized software development, net of accumulated amortization of $39,533 and $37,174 at March 31, 2018 and December 31, 2017, respectively	16,130	16,014
Goodwill	86,144	86,144
Customer-related intangibles, net of accumulated amortization of $18,586 and $17,033 at March 31, 2018 and December 31, 2017, respectively	58,128	59,681
Other intangible assets, net of accumulated amortization of $8,443 and $7,708 at March 31, 2018 and December 31, 2017, respectively	8,082	8,816
Deferred tax assets		45
Deferred commissions	12,378	
Non-marketable equity investments	3,779	3,772
Other assets	5,746	754
Long-term assets of discontinued operations		28,073
Total assets	$ 457,183	$ 411,119
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 24,519	$ 16,507
Accrued dividends	32,518	
Accrued royalties	13,356	12,849

Deferred revenue	69,238	64,938
Current liabilities of discontinued operations		6,772
Total current liabilities	139,631	101,066
Deferred tax liabilities	4,833	
Deferred revenue, noncurrent	3,005	6,287
Other long term liabilities	670	1,048
Long-term liabilities of discontinued operations		2,548
Commitments and contingencies		
Shareholders equity:		
Common stock, no par value, 75,000 shares authorized; 32,302 and 31,908 shares issued and outstanding at March 31, 2018 and December 31, 2017, respectively	285,065	282,666
Retained earnings	24,002	17,542
Accumulated other comprehensive loss	(23)	(38)
Total shareholders equity	309,044	300,170
Total liabilities and shareholders equity	$ 457,183	$ 411,119

See accompanying notes to the unaudited condensed consolidated financial statements.

1

Table of Contents

HEALTHSTREAM, INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)

(In thousands, except per share data)

	Three Months Ended March 31, 2018	Three Months Ended March 31, 2017
Revenues, net	$ 54,858	$ 51,967
Operating costs and expenses:		
Cost of revenues (excluding depreciation and amortization)	22,248	21,152
Product development	6,001	5,775
Sales and marketing	9,064	9,556
Other general and administrative expenses	7,742	7,217
Depreciation and amortization	6,073	5,902
Total operating costs and expenses	51,128	49,602
Operating income	3,730	2,365
Other income, net	313	130
Income from continuing operations before income tax provision	4,043	2,495
Income tax provision	414	786
Income from continuing operations	3,629	1,709
Discontinued operations (Note 8)		
Loss from discontinued operations before income tax provision	(64)	(532)
Gain on sale of discontinued operations	30,991	
Income tax provision	10,710	(108)
Income (loss) from discontinued operations	20,217	(424)
Net income	$ 23,846	$ 1,285
Earnings (loss) per share basic:		
Continuing operations	$ 0.11	$ 0.05
Discontinued operations	$ 0.63	$ (0.01)
Earnings per share basic	$ 0.74	$ 0.04
Earnings (loss) per share diluted:		
Continuing operations	$ 0.11	$ 0.05
Discontinued operations	$ 0.63	$ (0.01)
Earnings per share diluted	$ 0.74	$ 0.04

Weighted average shares of common stock outstanding:		
Basic	32,097	31,774
Diluted	32,132	32,104
Dividends declared per share	$ 1.00	$

See accompanying notes to the unaudited condensed consolidated financial statements.

2

Table of Contents

HEALTHSTREAM, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

(In thousands)

	Three Months Ended March 31,	
	2018	**2017**
Net income	$ 23,846	$ 1,285
Other comprehensive income, net of taxes:		
Unrealized gain on marketable securities	15	2
Total other comprehensive income	15	2
Comprehensive income	$ 23,861	$ 1,287

See accompanying notes to the unaudited condensed consolidated financial statements.

3

Table of Contents

HEALTHSTREAM, INC.

CONDENSED CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY (UNAUDITED)

THREE MONTHS ENDED MARCH 31, 2018

(In thousands)

	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders Equity
Balance at December 31, 2017	31,908	$ 282,666	$ 17,542	$ (38)	$ 300,170
Cumulative effect of accounting change			15,132		15,132
Net income			23,846		23,846
Comprehensive income				15	15
Dividends declared on common stock ($1.00 per share)			(32,518)		(32,518)
Stock based compensation		328			328
Common stock issued under stock plans, net of shares withheld for employee taxes	394	2,071			2,071
Balance at March 31, 2018	32,302	$ 285,065	$ 24,002	$ (23)	$ 309,044

See accompanying notes to the unaudited condensed consolidated financial statements.

Table of Contents

HEALTHSTREAM, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(In thousands)

	Three Months Ended March 31, 2018	2017
OPERATING ACTIVITIES:		
Net income	$ 23,846	$ 1,285
(Income) loss from discontinued operations	(20,217)	424
Adjustments:		
Depreciation and amortization	6,073	5,902
Stock based compensation expense	419	404
Provision for doubtful accounts	390	200
Deferred income taxes	608	526
(Gain) loss on non-marketable equity investments	(7)	5
Other	30	148
Changes in operating assets and liabilities:		
Accounts and unbilled receivables	(1,864)	4,558
Prepaid royalties	(2,467)	(431)
Other prepaid expenses and other current assets	(530)	589
Other assets	421	(94)
Accounts payable and accrued expenses	(6,074)	(976)
Accrued royalties	506	(1,024)
Deferred revenue	8,417	3,541
Net cash provided by continuing operating activities	9,551	15,057
Net cash (used in) provided by discontinued operating activities	(1,002)	1,470
Net cash provided by operating activities	8,549	16,527
INVESTING ACTIVITIES:		
Proceeds from sale of discontinued operations	58,203	
Proceeds from maturities of marketable securities	19,600	19,340
Purchases of marketable securities	(12,612)	(28,211)
Payments associated with capitalized software development	(2,541)	(2,420)
Purchases of property and equipment	(1,858)	(931)
Net cash provided by (used in) continuing investing activities	60,792	(12,222)
Net cash used in discontinued investing activities	(115)	(637)
Net cash provided by (used in) investing activities	60,677	(12,859)
FINANCING ACTIVITIES:		
Proceeds from exercise of stock options	2,368	99

Taxes paid related to net settlement of equity awards	(297)	(367)
Payment of earn-outs related to acquisitions	(37)	
Net cash provided by (used in) continuing financing activities	2,034	(268)
Net cash provided by (used in) discontinued financing activities		
Net cash provided by (used in) financing activities	2,034	(268)
Net increase in cash and cash equivalents	71,260	3,400
Cash and cash equivalents at beginning of period	84,768	49,634
Cash and cash equivalents at end of period	$ 156,028	$ 53,034

See accompanying notes to the unaudited condensed consolidated financial statements.

5

Table of Contents

HEALTHSTREAM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (US GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, condensed consolidated financial statements do not include all of the information and footnotes required by US GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. All intercompany transactions have been eliminated in consolidation. Operating results for the three months ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018.

On February 12, 2018, the Company divested its Patient Experience (PX) business to Press Ganey Associates, Inc. (Press Ganey). This sale of the PX business resulted in the Company s divestiture of the Company s patient experience solutions business segment. The Company has classified the results of its PX segment as discontinued operations in its condensed consolidated statements of income and cash flows for all periods presented. Additionally, the related assets and liabilities have been reported as assets and liabilities of discontinued operations in the Company s condensed consolidated balance sheet as of December 31, 2017. See Note 8 for additional information.

The condensed consolidated balance sheet at December 31, 2017 has been derived from the audited consolidated financial statements at that date and adjusted for discontinued operations as noted above but does not include all of the information and footnotes required by US GAAP for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended December 31, 2017 (included in the Company s Annual Report on Form 10-K, filed with the Securities and Exchange Commission on February 26, 2018).

2. RECENT ACCOUNTING PRONOUNCEMENTS

Accounting Standards Recently Adopted

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This guidance supersedes the revenue recognition requirements in Accounting Standards Codification (ASC) Topic 605, *Revenue Recognition (Topic 605)*, and most industry-specific revenue recognition guidance throughout the Industry Topics of the Accounting Standards Codification. The updated guidance states that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Topic 606 also includes Subtopic 340-40, *Other Assets and Deferred Costs Contracts with Customers*, which requires deferral of incremental costs of obtaining a contract with a customer. Collectively, Topic 606 and Subtopic 340-40 are referred to as the new standard.

The Company adopted the new standard effective January 1, 2018 utilizing the modified retrospective approach. Adoption of the new standard resulted in changes to the Company s accounting policies for revenue recognition, trade and other receivables, and deferred commissions. See Note 3 for additional information regarding Topic 606 and its impact on the Company s balance sheet and statement of income.

In January 2016, the FASB issued ASU 2016-01, *Financial Instruments Overall (Sub Topic 825-10)*, which addresses certain aspects of the recognition, measurement, presentation, and disclosure of financial instruments. The guidance, among other things, requires equity investments (except those accounted for under the equity method of accounting or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. The Company adopted ASU 2016-01 effective January 1, 2018 on a prospective basis.

Accounting Standards Not Yet Adopted

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842),* which requires lessees to recognize assets and liabilities for most leases. The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee is not expected to significantly change under such guidance. The standard will be effective for the first interim period within annual reporting periods beginning after December 15, 2018. The Company will adopt this ASU on January 1, 2019 and is currently evaluating the impact that adoption of this ASU will have on the Company s consolidated financial position and results of operations.

Table of Contents

HEALTHSTREAM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3. REVENUE RECOGNITION AND SALES COMMISSIONS

Adoption of ASC Topic 606, Revenue from Contracts with Customers

On January 1, 2018, the Company adopted the new standard using the modified retrospective approach applied to those contracts which were not completed as of January 1, 2018. As such, results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts continue to be reported in accordance with Topic 605.

The cumulative effect of the changes made to the Company s consolidated January 1, 2018 balance sheet in connection with the adoption of Topic 606 was as follows (in thousands):

Balance Sheet	Balance at December 31, 2017	ASC 606 Adjustments	Balance at January 1, 2018
Assets			
Unbilled receivables	$ 1,327	$ 31	$ 1,358
Prepaid royalties, net	16,137	(902)	15,235
Other prepaid expenses and other current assets	8,330	(2,900)	5,430
Current assets of discontinued operations	6,125	(274)	5,851
Deferred commissions		12,552	12,552
Deferred tax assets	45	(45)	
Non-current assets of discontinued operations	28,073	3,166	31,239
Liabilities			
Deferred revenue, current	64,938	(4,488)	60,450
Current liabilities of discontinued operations	6,772	(1,374)	5,398
Deferred tax liabilities		5,205	5,205
Deferred revenue, noncurrent	6,287	(2,848)	3,439
Shareholders equity			
Retained earnings	17,542	15,132	32,674

The impact of the adoption of Topic 606 on the Company s condensed consolidated balance sheet as of March 31, 2018 and statement of income for the three months ended March 31, 2018 was as follows (in thousands):

Balance Sheet	March 31, 2018 As reported	Balances without Adoption of ASC 606	Effect of Change Higher/(Lower)
Assets			
Unbilled receivables	$ 2,958	$ 2,831	$ 127
Prepaid royalties, net	17,702	18,671	(969)
Other prepaid expenses and other current assets	5,962	7,220	(1,258)
Deferred commissions	12,378		12,378
Liabilities			
Deferred revenue, current	69,238	73,726	(4,488)
Deferred revenue, noncurrent	3,005	5,845	(2,840)
Shareholders equity			
Retained earnings	24,002	22,965	1,0 37

7

HEALTHSTREAM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3. REVENUE RECOGNITION AND SALES COMMISSIONS (continued)

	For the period ended March 31, 2018		
Income Statement	As reported	Balances without Adoption of ASC 606	Effect of Change Higher/(Lower)
Revenue, net	$ 54,858	$ 54,866	$ (8)
Costs and expenses			
Cost of revenues (excluding depreciation and amortization)	22,248	22,181	67
Sales and marketing	9,064	10,541	(1,477)
Operating income	3,730	2,328	1,402
Income from continuing operations before income tax provision	4,043	2,641	1,402
Income tax provision	414	49	365
Income from continuing operations	3,629	2,592	1,037
Net income	23,846	22,809	1,037

Revenue Recognition

Revenues are recognized when control of the promised goods or services is transferred to the customer in an amount that reflects the consideration the Company expects to be entitled to in exchange for transferring those goods or services.

Revenue is recognized based on the following five step model:

Identification of the contract with a customer

Identification of the performance obligations in the contract

Determination of the transaction price

Allocation of the transaction price to the performance obligations in the contract

Recognition of revenue when, or as, the Company satisfies a performance obligation

The following table represents our revenues included in continuing operations from contracts with customers disaggregated by revenue source for the three months ended March 31, 2018 (in thousands). Sales taxes are excluded from revenues.

Segments	Workforce Solutions	Provider Solutions	Consolidated
Subscription/SaaS services	$ 43,702	$ 9,032	$ 52,734
Professional services	1,245	879	2,124
Total revenues	$ 44,947	$ 9,911	$ 54,858

Subscription/SaaS services revenues primarily consist of fees that provide customers access to one or more of our SaaS-based platforms and/or courseware subscriptions, with routine customer support. Revenue is generally recognized over time over the contract term beginning on the date that the service is made available to the customer. Subscription/SaaS contracts are generally one to five years in length, billed annually, semi-annually, quarterly, or monthly in advance, and are non-cancelable.

Professional services revenues primarily consist of fees for implementation services, custom courseware development, as well as training. The majority of our professional services contracts are billed in advance based on a fixed price basis, and revenue is recognized over time as the services are performed. For both subscription/SaaS services and professional services, the time between billing the customer and when performance obligations are satisfied is not significant.

Our contracts with customers often contain multiple performance obligations. For these contracts, the Company accounts for individual performance obligations separately if they are distinct. The contract price, which represents transaction price, is allocated to the separate performance obligations on a relative standalone selling price basis. We generally determine standalone selling prices based on the standard price list price for each product, taking into consideration certain factors, including contract length and the number of subscribers within the contract.

We receive payments from customers based on billing schedules established in our contracts. Accounts receivable unbilled represent contract assets related to our conditional right to consideration for subscription/SaaS and professional services contracts where performance has occurred under the contract. Accounts receivable are primarily comprised of trade receivables that are recorded at the invoice amount, net of an allowance for doubtful accounts, when the right to consideration becomes unconditional.

Table of Contents

HEALTHSTREAM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

3. REVENUE RECOGNITION AND SALES COMMISSIONS (continued)

Other receivables, which are included within Accounts Receivable, include receivables from certain content partners and are not material. For the three months ended March 31, 2018 and 2017, the Company recognized $390,000 and $200,000 in impairment losses on receivables and contract assets arising from the Company s contracts with customers.

Deferred revenue represents contract liabilities that are recorded when cash payments are received or are due in advance of our satisfaction of performance obligations. During the three months ended March 31, 2018, we recognized approximately $29.2 million of revenue from amounts included in deferred revenues at the beginning of the period. As of March 31, 2018, approximately $355 million of revenue is expected to be recognized from remaining performance obligations under contract with customers. We expect to recognize revenue on approximately 45% of these remaining performance obligations over the next 12 months, with the remaining amounts recognized thereafter.

Sales Commissions

Sales commissions earned by our sales force are considered incremental and recoverable costs of obtaining a contract with a customer. The Company s sales commission plans include multiple payments, including initial payments in the period a customer contract is obtained and subsequent payments either 15 or 27 months after the initial payment. Under Topic 606, costs to acquire contracts with customers, such as the initial sales commission payment, is capitalized and amortized consistent with the pattern of revenue recognition, whereas subsequent sales commission payments which require a substantive performance condition of the employee are expensed ratably through the payment date. In contrast, under Topic 605, initial sales commission payments were expensed. Under Topic 606, the initial commission payments are capitalized in the period a customer contract is obtained and are amortized consistent with the transfer of the goods or services to the customer over the expected period of benefit. The capitalized contract cost is included in Deferred commissions in the accompanying condensed consolidated balance sheet. The expected period of benefit is the contract term, except when the commission payment is expected to provide economic benefit to the Company for a period longer than the contract term, such as for new customer or incremental sales where renewals are expected and renewal commissions are not commensurate with initial commissions. Non-commensurate commissions will be amortized over the greater of contract term or technological obsolescence period, which has been determined to be three years. The Company recorded amortization of deferred commissions of approximately $1.8 million for the three months ended March 31, 2018, which is included in Sales and marketing expenses in the accompanying condensed consolidated statements of operations.

4. INCOME TAXES

Income taxes are accounted for using the asset and liability method, whereby deferred tax assets and liabilities are determined based on the temporary differences between the financial statement and tax bases of assets and liabilities measured at tax rates that will be in effect for the year in which the differences are expected to affect taxable income.

During the three months ended March 31, 2018 and 2017, the Company recorded a provision for income taxes from continuing operations of approximately $414,000 and $786,000, respectively. The Company s effective tax rate for the three months ended March 31, 2018 and 2017 was 10.2% and 31.5%, respectively. During the three months ended March 31, 2018 and 2017, the Company recorded excess tax benefits primarily from stock option exercises of approximately $636,000 and $57,000, respectively, as a component of the provision for income taxes. The Company s effective tax rate primarily reflects the statutory corporate income tax rate, the net effect of state taxes, and the effect of various permanent tax differences.

5. STOCKHOLDERS EQUITY

Dividends on Common Stock

On February 12, 2018, the Company s Board of Directors declared a $1.00 per common share special cash dividend which was paid on April 3, 2018 to shareholders of record on March 6, 2018. The dividend payment is included in Accrued dividends in the condensed consolidated balance sheet as of March 31, 2018.

HEALTHSTREAM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

5. STOCKHOLDERS EQUITY (continued)

Stock Based Compensation

The Company has stock awards outstanding under two stock incentive plans: the Company s 2016 Omnibus Incentive Plan and 2010 Stock Incentive Plan. The Company accounts for its stock based compensation plans using the fair-value based method for costs related to share based payments, including stock options and restricted share units (RSUs). During the three months ended March 31, 2018, the Company issued 83,168 RSUs, subject to service-based time vesting, with a weighted average grant date fair value of $24.70 per share, measured based on the closing fair market value of the Company s stock on the date of grant. During the three months ended March 31, 2017, the Company issued 86,727 RSUs, subject to service-based time vesting, with a weighted average grant date fair value of $23.54 per share, measured based on the closing fair market value of the Company s stock on the date of grant.

Total stock based compensation expense recorded for the three months ended March 31, 2018 and 2017, which is recorded within continuing operations in the condensed consolidated statements of income, is as follows (in thousands):

	Three Months Ended March 31, 2018	Three Months Ended March 31, 2017
Cost of revenues (excluding depreciation and amortization)	$ 8	$ 14
Product development	74	64
Sales and marketing	31	62
Other general and administrative	306	264
Total stock based compensation expense	$ 419	$ 404

6. EARNINGS PER SHARE

Basic earnings per share is computed by dividing the net income available to common shareholders for the period by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing the net income available to common shareholders for the period by the weighted average number of potentially dilutive common and common equivalent shares outstanding during the period. Common equivalent shares are composed of incremental common shares issuable upon the exercise of stock options and RSUs subject to vesting. The dilutive effect of common equivalent shares is included in diluted earnings per share by application of the treasury stock method. The total number of common equivalent shares excluded from the calculations of diluted earnings per share, due to their anti-dilutive effect or contingent performance conditions, was approximately 159,000 and 143,000 for the three months ended March 31, 2018 and 2017, respectively.

The following table sets forth the computation of basic and diluted earnings per share for the three months ended March 31, 2018 and 2017 (in thousands, except per share data):

	Three Months Ended March 31, 2018	Three Months Ended March 31, 2017
Numerator:		
Income from continuing operations	$ 3,629	$ 1,709
Income (loss) from discontinued operations, net of income taxes	20,217	(424)
Net income	$ 23,846	$ 1,285
Denominator:		
Weighted-average shares outstanding	32,097	31,774
Effect of dilutive shares	35	330
Weighted-average diluted shares	32,132	32,104
Earnings (loss) per share basic:		
Continuing operations	$ 0.11	$ 0.05
Discontinued operations	$ 0.63	$ (0.01)
Earnings per share basic	$ 0.74	$ 0.04
Earnings (loss) per share diluted:		
Continuing operations	$ 0.11	$ 0.05
Discontinued operations	$ 0.63	$ (0.01)
Earnings per share diluted	$ 0.74	$ 0.04

10

Table of Contents

HEALTHSTREAM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

7. MARKETABLE SECURITIES

At March 31, 2018 and December 31, 2017, the fair value of marketable securities, which were all classified as available for sale, included the following (in thousands):

	March 31, 2018			
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
Level 2:				
Corporate debt securities	$ 34,384	$ 5	$ (29)	$ 34,360
Government-sponsored enterprise debt securities	4,985	2	(1)	4,986
Total	$ 39,369	$ 7	$ (30)	$ 39,346

	December 31, 2017			
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value
Level 2:				
Corporate debt securities	$ 41,900	$ 1	$ (39)	$ 41,862
Government-sponsored enterprise debt securities	4,488	1	(1)	4,488
Total	$ 46,388	$ 2	$ (40)	$ 46,350

The carrying amounts reported in the condensed consolidated balance sheet approximate the fair value based on quoted market prices or alternative pricing sources and models utilizing market observable inputs. As of March 31, 2018, the Company does not consider any of its marketable securities to be other than temporarily impaired. During the three months ended March 31, 2018 and 2017, the Company did not reclassify any items out of accumulated other comprehensive income to net income. All investments in marketable securities are classified as current assets on the balance sheet because the underlying securities mature within one year from the balance sheet date.

8. DISCONTINUED OPERATIONS

Patient Experience

On February 12, 2018, the Company divested its PX business to Press Ganey for $65.5 million in cash (subject to adjustment based on the working capital of the PX business at closing), of which $6.55 million will be held in escrow for a period of time following the closing as a source of recovery for indemnification claims by Press Ganey. The sale of the PX business was effected (i) by the contribution by the Company of specified assets and certain liabilities used in the PX business to a newly-formed wholly-owned subsidiary of the Company, and (ii) immediately thereafter, the sale by the Company to Press Ganey of all the outstanding equity interests of such wholly-owned subsidiary. In connection with such contribution, the Company retained certain liabilities related to the PX business.

This sale of the PX business resulted in the Company s divestiture of the Company s patient experience solutions business segment. The Company has classified the results of its patient experience solutions business segment as discontinued operations in its condensed consolidated statements of income and cash flows for all periods presented. Additionally, the related assets and liabilities have been reported as assets and liabilities of discontinued operations in the Company s condensed consolidated balance sheet as of December 31, 2017.

The financial results of the PX business for the period prior to divestiture during the three months ended March 31, 2018, and during the three months ended March 31, 2017, are presented in discontinued operations in the Company s condensed consolidated statement of income. The following table presents financial results of the PX business (in thousands):

Table of Contents

HEALTHSTREAM, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

8. DISCONTINUED OPERATIONS (continued)

	Three Months Ended March 31,	
	2018	2017
Revenues, net	$ 3,342	$ 7,902
Operating costs and expenses:		
Cost of revenues (excluding depreciation and amortization)	1,982	5,124
Product development	554	824
Sales and marketing	460	1,278
Other general and administrative expenses	229	722
Depreciation and amortization	181	486
Total operating costs and expenses	3,406	8,434
Loss from operations of discontinued operations	(64)	(532)
Other income, net		
Loss from discontinued operations before income tax provision	(64)	(532)
Income tax provision (benefit)		(108)
Loss from discontinued operations, net of income taxes	$ (64)	$ (424)

The following table presents the aggregate carrying amounts of the classes of assets and liabilities of discontinued operations as of December 31, 2017 (in thousands):

Carrying amounts of assets included as part of discontinued operations:	
Accounts receivable, net	$ 4,158
Accounts receivable unbilled	1,275
Prepaid royalties, net of amortization	37
Other prepaid expenses and other current assets	655
Current assets of discontinued operations	6,125
Property and equipment, net	901
Capitalized software development, net	2,683
Goodwill	24,154
Customer-related intangibles, net	276
Other intangible assets, net	42

Other assets		17
Long-term assets of discontinued operations		28,073
Total assets of discontinued operations in the condensed consolidated balance sheet	$	34,198
Carrying amounts of liabilities included as part of discontinued operations:		
Accounts payable and accrued expenses	$	2,728
Accrued royalties		27
Deferred revenue		4,017