CONTROL4 CORP
Form 10-Q
November 03, 2017

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 September 30, 2017

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 001-36017

Control4 Corporation

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	42-1583209 (I.R.S. Employer Identification No.)
11734 S. Election Road Salt Lake City, Utah (Address of principal executive offices)	84020 (Zip Code)

(801) 523-3100
(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 (§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 Smaller reporting company Emerging growth company

(Do not check if a
smaller
reporting 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

On October 27, 2017, 25,266,497 shares of the registrant's Common Stock, $0.0001 par value, were outstanding.

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PART I — Financial Information

ITEM 1. Condensed Consolidated Financial Statements

CONTROL4 CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	September 30, 2017 (unaudited)	December 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	$ 28,627	$ 34,813
Restricted cash	271	247
Short-term investments	41,467	22,970
Accounts receivable, net	29,992	24,727
Inventories	33,149	26,231
Prepaid expenses and other current assets	3,418	3,662
Total current assets	136,924	112,650
Property and equipment, net	7,419	6,463
Long-term investments	1,513	4,008
Intangible assets, net	25,675	23,120
Goodwill	21,855	16,809
Other assets	3,121	2,008
Total assets	$ 196,507	$ 165,058
Liabilities and stockholders’ equity		
Current liabilities:		
Accounts payable	$ 22,953	$ 17,010
Accrued liabilities	9,397	8,912
Current portion of deferred revenue	2,151	1,553

Total current liabilities	34,501	27,475
Other long-term liabilities	879	701
Total liabilities	35,380	28,176
Commitments and contingencies (Note 10)	—	—
Stockholders’ equity:		
Common stock, $0.0001 par value; 500,000,000 shares authorized; 25,266,497 and 23,729,780 shares issued and outstanding at September 30, 2017 and December 31, 2016, respectively	3	2
Additional paid-in capital	234,640	220,370
Accumulated deficit	(73,038)	(82,626)
Accumulated other comprehensive loss	(478)	(864)
Total stockholders’ equity	161,127	136,882
Total liabilities and stockholders’ equity	$ 196,507	$ 165,058

See accompanying notes to condensed consolidated financial statements (unaudited).

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CONTROL4 CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
	(unaudited)		(unaudited)	
Revenue	$ 64,742	$ 55,185	$ 176,386	$ 151,435
Cost of revenue	31,520	27,566	86,572	77,303
Gross margin	33,222	27,619	89,814	74,132
Operating expenses:				
Research and development	10,347	9,190	30,246	26,708
Sales and marketing	12,692	10,852	36,082	32,101
General and administrative	5,109	5,407	16,413	15,279
Litigation settlement	—	—	—	400
Total operating expenses	28,148	25,449	82,741	74,488
Income (loss) from operations	5,074	2,170	7,073	(356)
Other income (expense), net:				
Interest, net	125	12	224	17
Other income (expense), net	79	(89)	183	(306)
Total other income (expense), net	204	(77)	407	(289)
Income (loss) before income taxes	5,278	2,093	7,480	(645)
Income tax expense (benefit)	93	316	(2,441)	(9,585)
Net income	$ 5,185	$ 1,777	$ 9,921	$ 8,940
Net income per common share:				
Basic	$ 0.21	$ 0.08	$ 0.40	$ 0.38
Diluted	$ 0.19	$ 0.07	$ 0.38	$ 0.37
Weighted-average number of shares:				
Basic	25,050	23,424	24,551	23,307
Diluted	27,122	24,530	26,393	24,149

See accompanying notes to condensed consolidated financial statements (unaudited).

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CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
	(unaudited)		(unaudited)	
Net income	$ 5,185	$ 1,777	$ 9,921	$ 8,940
Other comprehensive income (loss):				
Foreign currency translation adjustment, net of tax	(155)	172	383	197
Net unrealized gains (losses) on available-for-sale investments, net of tax	6	(10)	3	60
Total other comprehensive income (loss)	(149)	162	386	257
Comprehensive income	$ 5,036	$ 1,939	$ 10,307	$ 9,197

See accompanying notes to condensed consolidated financial statements (unaudited).

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Nine Months Ended September 30, 2017	2016
	(unaudited)	
Operating activities		
Net income	$ 9,921	$ 8,940
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	2,703	2,402
Amortization of intangible assets	3,885	3,393
(Gain) loss on disposal of fixed assets	(1)	13
Provision for doubtful accounts	491	313
Investment discount and premium amortization	(57)	293
Stock-based compensation	9,191	5,933
Tax benefit from business acquisition	(2,415)	(9,402)
Changes in assets and liabilities:		
Accounts receivable, net	(4,890)	(3,469)
Inventories	(5,347)	(6,776)
Restricted cash	(3)	—
Prepaid expenses and other current assets	390	1,740
Other assets	(1,002)	(341)
Accounts payable	3,495	2,333
Accrued liabilities	(1,675)	421
Deferred revenue	588	291
Other long-term liabilities	172	(451)
Net cash provided by operating activities	15,446	5,633
Investing activities		
Purchases of available-for-sale investments	(52,472)	(10,147)
Proceeds from sales of available-for-sale investments	1,950	900
Proceeds from maturities of available-for-sale investments	34,580	33,858
Purchases of property and equipment	(3,003)	(1,780)
Business acquisitions, net of cash acquired	(7,881)	(32,891)
Net cash used in investing activities	(26,826)	(10,060)
Financing activities		
Proceeds from exercise of options for common stock	11,290	3,021
Payments for taxes related to net share settlement of equity awards	(4,591)	—
Repurchase of common stock	(1,821)	(3,242)

Repayment of notes payable	—	(581)
Proceeds from revolving credit facility	—	5,000
Repayment of revolving credit facility	—	(3,500)
Payment of debt issuance costs	—	(89)
Net cash provided by financing activities	4,878	609
Effect of exchange rate changes on cash and cash equivalents	316	(41)
Net change in cash and cash equivalents	(6,186)	(3,859)
Cash and cash equivalents at beginning of period	34,813	29,530
Cash and cash equivalents at end of period	$ 28,627	$ 25,671
Supplemental disclosure of cash flow information		
Cash paid for interest	$ 65	$ 164
Cash paid for taxes	1,120	858
Supplemental schedule of non-cash investing and financing activities		
Business acquisitions holdback liability	1,068	—
Purchases of property and equipment financed by accounts payable	396	—
Net unrealized gains on available-for-sale investments	3	60

See accompanying notes to condensed consolidated financial statements (unaudited).

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Notes to Condensed Consolidated Financial Statements

(unaudited)

1. Description of Business and Summary of Significant Accounting Policies

Control4 Corporation (''Control4'' or the ''Company'') is a leading provider of smart home and business solutions that are designed to personalize and enhance how consumers engage with an ever-changing connected world. Our entertainment, smart lighting, comfort and convenience, safety and security, and networking solutions unlock the potential of connected devices, making entertainment systems easier to use and more accessible, homes and businesses more comfortable and energy efficient, and individuals more secure. The Company was incorporated in the state of Delaware on March 27, 2003.

Unaudited Interim Financial Statements

The accompanying condensed consolidated balance sheets, condensed consolidated statements of operations, condensed consolidated statements of comprehensive income, and condensed consolidated statements of cash flows are unaudited. These unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (''GAAP'') on the same basis as the audited consolidated financial statements and, in the opinion of management, reflect all adjustments, consisting only of normal recurring adjustments, considered necessary to present fairly the Company's financial position, results of operations and cash flows. The results of operations for the three and nine months ended September 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017, or any other future interim or annual period.

These unaudited interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission (the "SEC") on February 15, 2017. The December 31, 2016 condensed consolidated balance sheet included herein was derived from the audited financial statements as of that date.

Basis of Presentation

The unaudited condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All intercompany balances and transactions have been eliminated in the unaudited condensed consolidated financial statements.

Segment Reporting

Operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision-maker, the Chief Executive Officer, in making decisions regarding resource allocation and assessing performance. To date, the Company has viewed its operations and manages its business as one operating segment.

Concentrations of Risk

The Company’s accounts receivable are derived from revenue earned from its worldwide network of independent dealers and distributors. The Company’s sales to dealers and distributors located outside the United States are generally denominated in U.S. dollars, except for sales to dealers and distributors located in the United Kingdom, Canada, Australia, and the European Union, which are generally denominated in pounds sterling, Canadian dollars, Australian dollars, and euros, respectively. There were no individual account balances greater than 10% of total accounts receivable as of September 30, 2017 and December 31, 2016.

No dealer or distributor accounted for more than 10% of total revenue for the three and nine months ended September 30, 2017 and 2016.

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While the Company partners with many manufacturers, in many cases one manufacturer is our sole source for a particular product or product family. A significant disruption in the operations of one of these manufacturers would impact the production of the Company's products for a substantial period of time, which could have a material adverse effect on the Company's business, financial condition and results of operations.

Geographic Information

The Company's revenue includes amounts earned through sales to dealers and distributors located outside of the United States. There was no single foreign country that accounted for more than 10% of total revenue for the three and nine months ended September 30, 2017 and 2016. The following table sets forth revenue from U.S., Canadian and all other international dealers and distributors combined (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue-United States	$ 44,839	$ 39,670	$ 122,993	$ 108,506
Revenue-Canada	5,403	4,246	14,911	11,355
Revenue-all other international sources	14,500	11,269	38,482	31,574
Total revenue	$ 64,742	$ 55,185	$ 176,386	$ 151,435
International revenue (excluding Canada) as a percent of total revenue	22 %	20 %	22 %	21 %

Use of Accounting Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an ongoing basis, the Company evaluates its estimates, including those related to revenue recognition, sales returns, provisions for doubtful accounts, product warranty, inventory obsolescence, litigation, determination of fair value of stock options, deferred tax asset valuation allowances and income taxes. Actual results may differ from those estimates.

Limited Product Warranties

The Company provides its customers a limited product warranty of two, three, or ten years depending on product type and brand. The limited product warranties require the Company, at its option, to repair or replace defective products during the warranty period at no cost to the customer or refund the purchase price. The Company estimates the costs that may be incurred to replace, repair or issue a refund for defective products and records a reserve at the time revenue is recognized. Factors that affect the Company's warranty liability include the cost of the products sold, the Company's historical experience, and management's judgment regarding anticipated rates of product warranty returns, net of refurbished products. The Company assesses the adequacy of its recorded warranty liability each period and makes adjustments to the liability as necessary. Warranty costs accrued include amounts accrued for products at the time of shipment, adjustments for changes in estimated costs for warranties on products shipped in the period, and changes in estimated costs for warranties on products shipped in prior periods. It is not practicable for the Company to determine the amounts applicable to each of these components.

The following table presents the changes in the product warranty liability for the nine months ended September 30, 2017 (in thousands):

	Warranty Liability
Balance at December 31, 2016	$ 1,945
Warranty costs accrued	2,854
Warranty claims	(2,509)
Balance at September 30, 2017	$ 2,290

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Net Income Per Share

Basic net income per share is computed using the weighted-average number of common shares outstanding during the period. Diluted net income per share is computed using the weighted-average number of common shares outstanding and potentially dilutive common shares outstanding during the period that have a dilutive effect on net income per share. Potentially dilutive common shares result from the assumed exercise of outstanding stock options and settlement of restricted stock units.

The following table presents the reconciliation of the numerator and denominator used in the calculation of basic and diluted net income per share (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Numerator:				
Net income	$ 5,185	$ 1,777	$ 9,921	$ 8,940
Denominator:				
Weighted average common stock outstanding for basic net income per common share	25,050	23,424	24,551	23,307
Effect of dilutive securities—stock options and restricted stock units	2,072	1,106	1,842	842
Weighted average common shares and dilutive securities outstanding	27,122	24,530	26,393	24,149

Potentially dilutive securities, including common equivalent shares, in which the assumed proceeds exceed the average market price of common stock for the applicable period, were not included in the calculation of diluted net income per share as their impact would be anti-dilutive. The following weighted-average common stock equivalents were anti-dilutive and therefore were excluded from the calculation of diluted net income per share (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Options to purchase common stock	23	2,221	881	2,490
Restricted stock units	—	—	6	23
Total	23	2,221	887	2,513

Recent Accounting Pronouncements

In January 2017, the FASB issued ASU 2017-04, “Intangibles—Goodwill and Other (Topic 350), Simplifying the Test for Goodwill Impairment”. The amendments in this update simplify how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. This update is effective for annual or interim goodwill impairment tests in fiscal years beginning after December 31, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing after January 1, 2017. The Company notes that this guidance applies to its reporting requirements and will implement the new guidance accordingly in performing goodwill impairment testing; however, the Company does not believe this update will have a material impact on the consolidated financial statements.

In January 2017, the FASB issued ASU 2017-01, “Business Combinations (Topic 805): Clarifying the Definition of a Business,” which narrows the definition of a business. This update is effective for annual periods beginning after December 15, 2017, including interim periods within those years. Early adoption is permitted. The guidance will impact the Company’s acquisitions beginning January 1, 2018 and could cause fewer acquired sets of assets to be identified as a business.

In November 2016, the FASB issued ASU 2016-18, “Statement of Cash Flows (Topic 230): Restricted Cash,” which provides amendments to current guidance to address the classifications and presentation of changes in restricted cash in the statement of cash flows. The effective date for the standard is for fiscal years beginning after

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December 15, 2017. Early adoption is permitted. Upon the adoption of this standard, the Company will combine restricted cash with unrestricted cash and cash and cash equivalents in the statement of cash flows.

In October 2016, the FASB issued ASU 2016-16, “Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory.” The amendments in this update will require recognition of current and deferred income taxes resulting from an intra-entity transfer of an asset other than inventory when the transfer occurs. This update is effective for annual and interim periods beginning after December 15, 2017. Early adoption is permitted. The Company is currently evaluating the impact of adopting this guidance.

In August 2016, the FASB issued ASU 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments,” which clarifies how companies present and classify certain cash receipts and cash payments in the statement of cash flows. This standard is effective for fiscal periods beginning after December 15, 2017, including interim periods within those years. Early adoption is permitted, and the guidance must be applied using a retrospective transition method. The Company is currently evaluating the impact of adopting this guidance.

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments – Credit Losses (Topic 326)” which introduces new guidance for the accounting for credit losses on instruments within its scope. The new guidance introduces an approach based on expected losses to estimate credit losses on certain types of financial instruments. For trade receivables, the Company will be required to use a forward-looking expected loss model rather than the incurred loss model for recognizing credit losses which reflects losses that are probable. The guidance is effective for fiscal years beginning after December 31, 2019, including interim periods within those years. Early application of the guidance is permitted for all entities for fiscal years beginning after December 15, 2018, including the interim periods within those fiscal years. Application of the amendments is through a cumulative-effect adjustment to retained earnings as of the effective date. The Company is currently evaluating the impact of this update on the consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, “Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting.” The amendments in this update simplify several aspects of the accounting for employee share-based payment transactions, including the accounting for income taxes, forfeitures and statutory tax withholding requirements, as well as classification in the statement of cash flows. The Company adopted the new guidance on January 1, 2017. The primary impact of adoption was the recognition of excess tax benefits in our provision for income taxes rather than paid-in capital. Adoption of the new standard resulted in the recognition of excess tax benefits in our provision for income taxes rather than paid-in capital of $9.6 million for the nine months ended September 30, 2017. However, as the Company has a full valuation allowance against its domestic net deferred tax asset, a corresponding adjustment was recorded to increase the valuation allowance by $9.6 million.

As of December 31, 2016, the Company had $20.6 million and $17.6 million of gross federal and state net operating losses (“NOLs”), respectively, attributable to excess windfall benefits from share-based compensation. As a result of the adoption of this new standard, on January 1, 2017, the Company increased its net deferred tax asset for NOL carryforwards, with an offsetting cumulative effect of adoption adjustment to accumulated deficit, in the amount of

$7.7 million. A corresponding adjustment was recorded to increase the valuation allowance by $7.7 million with an offsetting adjustment to accumulated deficit, resulting in no net impact to the financial statements. In addition, the Company has elected to apply the presentation requirements for cash flows related to excess tax benefits retrospectively which had no impact on the statement of cash flows for the nine months ended September 30, 2016. Further, under the provisions of ASU 2016-09, the Company has elected to recognize forfeitures as they occur to determine the amount of compensation cost to be recognized in each period. This resulted in an increase of $0.3 million to accumulated deficit with a corresponding increase to additional paid-in capital on January 1, 2017. The amendment related to the accounting for minimum statutory withholding requirements had no impact on retained earnings as of January 1, 2017.

In February 2016, the FASB issued ASU 2016-02, “Leases (Topic 842),” which supersedes the guidance in ASC 840, “Leases.” The purpose of the new standard is to improve transparency and comparability related to the accounting and reporting of leasing arrangements. The guidance will require balance sheet recognition for assets and liabilities associated with rights and obligations created by leases with terms greater than twelve months. The guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those years. Modified retrospective application is required. Early adoption is permitted. The Company is evaluating the impact of adopting this guidance.

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)," which amends the guidance in ASC 605, "Revenue Recognition." The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14, deferring the effective date of this standard for one year, and it is now effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. The Company does not plan to early adopt, and accordingly, will adopt the new standard effective January 1, 2018.

The guidance permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (modified retrospective method). The Company plans to adopt the standard using the full retrospective method to restate each prior reporting period presented. The Company's ability to adopt using the full retrospective method is dependent on completion of the analysis of information necessary to restate prior period financial statements.

The Company has reached conclusions on key provisions of this standard as it relates to the sale of the Company's products to dealers, retailers and distributors. The Company is in the process of finalizing revenue recognition policies under the new standard and will be calculating the expected impact during the final quarter of 2017.

The Company is making progress on its assessment of the impact of this new standard as it relates to other ancillary revenue streams such as software licenses, subscription services, and third-party products sold through an online dealer portal. As these revenue streams represented less than 5% of overall revenue in 2016, the results of this assessment are not expected to have a significant impact on the Company's financial statements.

2. Balance Sheet Components

Inventories consisted of the following (in thousands):

	September 30, 2017	December 31, 2016
Finished goods	$ 29,667	$ 24,138
Component parts	3,312	1,880
Work-in-process	170	213
	$ 33,149	$ 26,231

Property and equipment, net consisted of the following (in thousands):

	September 30, 2017	December 31, 2016
Computer equipment and software	$ 4,801	$ 3,855
Manufacturing tooling and test equipment	4,962	4,216
Lab and warehouse equipment	4,661	3,649
Leasehold improvements	3,780	3,438
Furniture and fixtures	3,671	3,254
Other	1,215	753
	23,090	19,165
Less: accumulated depreciation	(15,671)	(12,702)
	$ 7,419	$ 6,463

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Accrued liabilities consisted of the following (in thousands):

	September 30, 2017	December 31, 2016
Sales returns and current portion of warranty accruals	$ 2,917	$ 2,892
Compensation accruals	4,533	4,445
Other accrued liabilities	1,947	1,575
	$ 9,397	$ 8,912

3. Financial Instruments

Fair Value Measurements

The Company's financial assets that are measured at fair value on a recurring basis consist of money market funds and available-for-sale investments. The following three levels of inputs are used to measure the fair value of financial instruments:

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

Level 2: Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3: Unobservable inputs are used when little or no market data is available.

The fair values for substantially all of the Company's financial assets are based on quoted prices in active markets or observable inputs. For Level 2 securities, the Company uses a third-party pricing service which provides documentation on an ongoing basis that includes, among other things, pricing information with respect to reference data, methodology, inputs summarized by asset class, pricing application and corroborative information.

Cash, Cash Equivalents and Marketable Securities

The Company determines realized gains or losses on the sale of marketable securities on a specific identification method. During the three and nine months ended September 30, 2017 and 2016, the Company did not record significant realized gains or losses on the sales of available-for-sale investments.

The following tables show the Company's cash and available-for-sale investments' adjusted cost, gross unrealized gains, gross unrealized losses and fair value by significant investment category, recorded as cash and cash equivalents or short- or long-term investments as of September 30, 2017 and December 31, 2016 (in thousands):

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	September 30, 2017						
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-term Investments	Long-term Investments
Cash	$ 20,170	$ —	$ —	$ 20,170	$ 20,170	$ —	$ —
Level 1:							
Money market funds	5,061	—	—	5,061	5,061	—	—
U.S. government notes	6,998	—	(4)	6,994	1,899	5,095	—
Subtotal	12,059	—	(4)	12,055	6,960	5,095	—
Level 2:							
Asset-backed securities	1,000	—	—	1,000	—	1,000	—
Corporate bonds	18,367	—	(8)	18,359	—	16,846	1,513
Commercial paper	20,023	—	—	20,023	1,497	18,526	—
Subtotal	39,390	—	(8)	39,382	1,497	36,372	1,513
Total	$ 71,619	$ —	$ (12)	$ 71,607	$ 28,627	$ 41,467	$ 1,513

	December 31, 2016						
	Adjusted Cost	Unrealized Gains	Unrealized Losses	Fair Value	Cash and Cash Equivalents	Short-term Investments	Long-term Investments
Cash	$ 24,708	$ —	$ —	$ 24,708	$ 24,708	$ —	$ —
Level 1:							
Money market funds	10,105	—	—	10,105	10,105	—	—
U.S. government notes	2,001	—	(1)	2,000	—	2,000	—
Subtotal	12,106	—	(1)	12,105	10,105	2,000	—
Level 2:							
Asset-backed securities	4,008	—	—	4,008	—	—	4,008
Corporate bonds	13,902	—	(14)	13,888	—	13,888	—
Commercial paper	7,082	—	—	7,082	—	7,082	—
Subtotal	24,992	—	(14)	24,978	—	20,970	4,008
Total	$ 61,806	$ —	$ (15)	$ 61,791	$ 34,813	$ 22,970	$ 4,008

As of September 30, 2017, the Company considers the declines in market value of its investment portfolio to be temporary in nature and does not consider any of its investments other-than-temporarily impaired. During the three and nine months ended September 30, 2017 and 2016, the Company did not recognize any significant impairment charges. The Company invests in highly-rated securities, and its investment policy limits the amount of credit exposure to any one issuer. The policy requires investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss. Fair values were determined for each individual security in the investment portfolio. The maturities of the Company’s long-term investments range from one to two years. When evaluating an investment for other-than-temporary impairment the Company reviews factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, changes in market interest rates, and the Company’s intent to sell, as well as the fact it is not more likely than not that the Company will be required to sell the investment before recovery of the investment’s cost basis, which may be maturity.

Fair Value of Other Financial Instruments

The carrying amounts reported in the accompanying condensed consolidated financial statements for cash and cash equivalents, restricted cash, accounts payable and accrued liabilities approximate their fair value because of the short-term nature of the accounts.

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Derivative Financial Instruments

The Company has foreign currency exposure related to the operations in the United Kingdom, Canada, Australia, the European Union, as well as other foreign locations. The Company has entered into forward contracts to help offset the exposure to movements in foreign currency exchange rates in relation to certain U.S. dollar denominated balance sheet accounts of its subsidiaries in the United Kingdom and Australia. The foreign currency derivatives are not designated as accounting hedges. The Company recognizes these derivative instruments as either assets or liabilities in the accompanying Condensed Consolidated Balance Sheets at fair value. The Company records changes in the fair value (i.e. gains or losses) of these derivative instruments in the accompanying Condensed Consolidated Statements of Operations as Other income (expense), net.

The Company settles its foreign exchange contracts on the last day of every month and enters into a new forward contract for the next month. As a result, there are no assets or liabilities recorded in the accompanying Condensed Consolidated Balance Sheets related to derivative instruments as of September 30, 2017. However, the notional principal of foreign exchange contracts for October 2017 was $12.8 million as of September 30, 2017.

The following table shows the pre-tax losses of the Company’s derivative instruments not designated as hedging instruments (in thousands):

		Three Months Ended September 30,		Nine Months Ended September 30,	
	Income Statement Location	2017	2016	2017	2016
Foreign exchange forward contracts	Other income (expense), net	$ (501)	$ (60)	$ (1,433)	$ (17)

4. Acquisitions

Acquisition of Triad Holdings, Inc.

On February 27, 2017, the Company entered into a definitive agreement to acquire Triad Holdings, Inc., ("Triad Holdings"), along with its wholly owned subsidiary Triad Speakers, Inc. ("Triad Speakers" and together with Triad Holdings "Triad") through the purchase of all the outstanding shares of common stock of Triad for a purchase price of $9.6 million (the "Triad Purchase Agreement"), which included cash acquired of $0.3 million. In accordance with the purchase agreement, $1.4 million of the purchase price will be held for up to 18 months from the acquisition date (the "Holdback"), to cover any of the sellers' post-closing obligations, including without limitation any indemnification obligations that may arise. Due to customary net working capital adjustments, the purchase price of Triad was reduced to $9.2 million during the three months ended June 30, 2017, resulting in a reduction to the Holdback and goodwill. The Company has classified the remaining $1.1 million Holdback in other current liabilities.

Total consideration transferred for the Triad acquisition was allocated to tangible and identifiable intangible assets acquired and liabilities assumed based on their fair values at the acquisition date as set forth below. Management estimated the fair values of tangible and intangible assets and liabilities in accordance with the applicable accounting guidance for business combinations. The preliminary amount of consideration transferred is subject to potential adjustments due to tax-related matters that could have a material impact on the condensed consolidated financial statements. Due to new information obtained related to net working capital and based on facts that existed at the acquisition date, the Company recorded measurement period adjustments to cash, goodwill, accounts payable and other liabilities. The Company expects the allocation of the consideration transferred to be final within the measurement period (up to one year from the acquisition date).

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The following reflects the Company's preliminary allocation of consideration transferred for the Triad acquisition (in thousands):

	Triad Acquisition
Cash	$ 269
Accounts receivable	516
Inventory	1,078
Other assets acquired	430
Intangible assets	6,271
Goodwill	4,785
Total assets acquired	13,349
Accounts payable	878
Deferred tax liability	2,415
Warranty liability	237
Other liabilities assumed	601
Total net assets acquired	$ 9,218

Identifiable Intangible Assets

The Company acquired intangible assets that consisted of customer relationships, trademarks/trade names, and developed technology, which had estimated fair values of $2.5 million, $2.4 million, and $1.4 million, respectively. The intangible assets were measured at fair value reflecting the highest and best use of nonfinancial assets in combination with other assets and liabilities. The customer relationships and trademarks/trade names were valued using an income approach that discounts expected future cash flows to present value. The estimated net cash flows were discounted using discount rates between 15% and 16%, based on the estimated internal rate of return for the acquisition and represent the rates that market participants might use to value the intangible assets based on the risk profile of the asset. The projected cash flows were determined using key assumptions such as: estimates of revenues and operating profits; capital expense investments; royalty rates; and tax savings. The acquired technology was valued using a cost savings approach that calculates the asset's reproduction cost by estimating all the costs associated with creating the technology. The Company will amortize the intangible assets on a straight-line basis over their estimated useful lives of 10 years for the customer relationships, 12 years for the trademark/trade name, and 12 years for the developed technology. The amortization of these intangible assets is not deductible for income tax purposes.

Goodwill

Goodwill of $4.8 million represents the excess of consideration transferred over the fair value of assets acquired and liabilities assumed and is attributable to Triad's assembled workforce, synergies and the projected profits from new products and dealers. This goodwill is not deductible for income tax purposes.

The Company determined the Triad acquisition was not a significant acquisition under Rule 3-05 of Regulation S X.

Australia Expansion

On April 1, 2016, the Company began working directly with home automation integrators in Australia to better serve and support customers in that country. As part of the shift from its distribution model in Australia, Control4, through its wholly owned subsidiary, Control4 Australia Holdings Pty., Ltd, acquired customer lists and inventory from the Company's Australian distributor for $0.7 million.

The Company determined this acquisition was not a significant acquisition under Rule 3-05 of Regulation S-X.

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Acquisition of Pakedge Device and Software Inc.

On January 29, 2016, the Company entered into a definitive agreement to acquire Pakedge Device and Software Inc. (“Pakedge”) through the purchase of all of the outstanding shares of common stock of Pakedge for a price of $33.0 million, which included cash acquired of $0.8 million. In accordance with the purchase agreement, $5.0 million was deposited in escrow and held until August 2017 to cover the sellers’ post-closing obligations.

5. Goodwill and Intangible Assets

Goodwill

Changes in the carrying amount of goodwill consisted of the following (in thousands):

	Amount
Balance at December 31, 2016	$ 16,809
Current period acquisitions	4,785
Foreign currency translation adjustment	261
Balance at September 30, 2017	$ 21,855

Goodwill represents the excess of consideration transferred over the fair value of assets acquired and liabilities assumed.

Amortizable Intangible Assets

The Company’s intangible assets and related accumulated amortization consisted of the following as of September 30, 2017, and December 31, 2016 (in thousands):

	September 30, 2017		
	Gross Carrying Amount	Accumulated Amortization	Net

Developed technology	$ 18,187	$ (8,122)	$ 10,065
Customer relationships	11,720	(2,197)	9,523
Trademark/trade name	6,776	(728)	6,048
Non-competition agreements	295	(256)	39
Total intangible assets	$ 36,978	$ (11,303)	$ 25,675