CUBIC CORP /DE/
Form 10-Q
August 03, 2017
Table of Contents

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT

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

For the Quarter Ended June 30, 2017

001-08931

Commission File Number

CUBIC CORPORATION

Exact Name of Registrant as Specified in its Charter

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

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

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

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

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

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

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

As of July 22, 2017, registrant had only one class of common stock of which there were 27,126,974 shares outstanding (after deducting 8,945,300 shares held as treasury stock).

Table of Contents

CUBIC CORPORATION

QUARTERLY REPORT ON FORM 10-Q

For the Quarter Ended June 30, 2017

TABLE OF CONTENTS

Table of Contents

PART I - FINANCIAL INFORMATION

ITEM 1 - FINANCIAL STATEMENTS

CUBIC CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF INCOME (LOSS) (UNAUDITED)

(amounts in thousands, except per share data)

	Nine Months Ended June 30, 2017	2016	Three Months Ended June 30, 2017	2016
Net sales:				
Products	$ 466,071	$ 451,329	$ 167,143	$ 170,566
Services	574,184	603,748	194,726	204,674
	1,040,255	1,055,077	361,869	375,240
Costs and expenses:				
Products	334,590	328,422	120,575	108,785
Services	464,505	478,647	157,781	164,053
Selling, general and administrative expenses	183,208	206,897	60,094	68,632
Research and development	38,779	18,146	16,901	8,521
Amortization of purchased intangibles	25,093	24,620	7,865	9,666
Restructuring costs	1,950	1,615	350	1,690
	1,048,125	1,058,347	363,566	361,347
Operating income (loss)	(7,870)	(3,270)	(1,697)	13,893
Other income (expenses):				
Interest and dividend income	719	1,152	249	415
Interest expense	(12,202)	(7,403)	(4,357)	(3,486)
Other income (expense), net	722	(1,532)	1,667	(1,930)
Income (loss) before income taxes	(18,631)	(11,053)	(4,138)	8,892
Income tax provision (benefit)	5,733	(20,281)	17,819	4,394
Net income (loss)	$ (24,364)	$ 9,228	$ (21,957)	$ 4,498
Net income (loss) per share:				
Basic	$ (0.90)	$ 0.34	$ (0.81)	$ 0.17
Diluted	$ (0.90)	$ 0.34	$ (0.81)	$ 0.17

Dividends per common share	$ 0.14	$ 0.14	$ —	$ —
Weighted average shares used in per share calculations:				
Basic	27,100	26,971	27,110	26,977
Diluted	27,100	27,010	27,110	27,058

See accompanying notes.

Table of Contents

CUBIC CORPORATION

CONDENSED CONSOLIDATED

STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

(in thousands)

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Net income (loss)	$ (24,364)	$ 9,228	$ (21,957)	$ 4,498
Other comprehensive income (loss):				
Foreign currency translation	(2,111)	(39,571)	11,193	(21,950)
Change in unrealized gains/losses from cash flow hedges:				
Change in fair value of cash flow hedges, net of tax	(39)	273	930	620
Adjustment for net gains/losses realized and included in net income, net of tax	(1,204)	(868)	(1,204)	(294)
Total change in unrealized gains/losses realized from cash flow hedges, net of tax	(1,243)	(595)	(274)	326
Total other comprehensive income (loss)	(3,354)	(40,166)	10,919	(21,624)
Total comprehensive loss	$ (27,718)	$ (30,938)	$ (11,038)	$ (17,126)

See accompanying notes.

4

Table of Contents

CUBIC CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(in thousands)

	June 30, 2017	September 30, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	$ 67,064	$ 197,127
Restricted cash	4,564	75,648
Marketable securities	13,060	12,996
Accounts receivable - net	361,843	382,581
Recoverable income taxes	4,951	9,706
Inventories - net	103,438	66,362
Other current assets	33,614	38,231
Total current assets	588,534	782,651
Long-term contract receivables	21,301	20,926
Long-term capitalized contract costs	58,694	65,382
Property, plant and equipment, net	107,910	96,316
Deferred income taxes	2,149	2,194
Goodwill	410,902	406,946
Purchased intangibles, net	103,623	123,403
Other assets	9,800	6,590
Total assets	$ 1,302,913	$ 1,504,408
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Current liabilities:		
Short-term borrowings	$ 104,000	$ 240,000
Trade accounts payable	62,002	81,172
Customer advances	56,277	49,481
Accrued compensation and other current liabilities	120,304	147,690
Income taxes payable	957	1,450
Current portion of long-term debt	452	450
Total current liabilities	343,992	520,243
Long-term debt	199,978	200,291
Other long-term liabilities	97,455	93,978

Shareholders’ equity:		
Common stock	35,745	32,756
Retained earnings	784,992	813,035
Accumulated other comprehensive loss	(123,171)	(119,817)
Treasury stock at cost	(36,078)	(36,078)
Total shareholders’ equity	661,488	689,896
Total liabilities and shareholders’ equity	$ 1,302,913	$ 1,504,408

See accompanying notes.

Table of Contents

CUBIC CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(in thousands)

	Nine Months Ended June 30, 2017	Nine Months Ended June 30, 2016	Three Months Ended June 30, 2017	Three Months Ended June 30, 2016
Operating Activities:				
Net income (loss)	$ (24,364)	$ 9,228	$ (21,957)	$ 4,498
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:				
Depreciation and amortization	38,154	31,943	12,418	12,966
Share-based compensation expense	3,826	6,916	469	2,828
Change in fair value of contingent consideration	(4,713)	(2,756)	(2,519)	(1,050)
Changes in operating assets and liabilities, net of effects from acquisitions	(29,417)	(39,892)	(16,731)	23,892
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	(16,514)	5,439	(28,320)	43,134
Investing Activities:				
Acquisition of businesses, net of cash acquired	(12,924)	(243,483)	—	—
Purchases of property, plant and equipment	(25,490)	(25,883)	(10,321)	(4,508)
Purchases of marketable securities	(18,944)	(21,802)	(189)	(7,116)
Proceeds from sales or maturities of marketable securities	18,944	36,923	6,441	7,053
Proceeds from sale of fixed assets	1,233	—	—	—
Purchase of non-marketable debt and equity securities	(2,200)	—	—	—
NET CASH USED IN INVESTING ACTIVITIES	(39,381)	(254,245)	(4,069)	(4,571)
Financing Activities:				
Proceeds from short-term borrowings	93,080	263,300	23,800	10,000
Principal payments on short-term borrowings	(229,080)	(93,300)	(169,800)	(20,000)
Proceeds from long-term borrowings	—	75,000	—	—
Principal payments on long-term debt	(320)	(378)	(104)	(124)
Purchase of common stock	(2,449)	(1,658)	(94)	—
Proceeds in connection with the Company's employee stock purchase plan	1,712	—	279	—
Dividends paid	(3,679)	(3,641)	—	—
Contingent consideration payments related to acquisitions of businesses	(1,988)	(1,679)	—	—
Net change in restricted cash	71,084	(4,116)	72,597	(602)

NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	(71,640)	233,528	(73,322)	(10,726)
Effect of exchange rates on cash	(2,528)	(29,759)	4,958	(13,206)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(130,063)	(45,037)	(100,753)	14,631
Cash and cash equivalents at the beginning of the period	197,127	218,476	167,817	158,808
CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	$ 67,064	$ 173,439	$ 67,064	$ 173,439
Supplemental disclosure of non-cash investing and financing activities:				
Liability incurred to acquire Vocality, net	$ 1,035	$ —	$ —	$ —
Liability incurred to acquire GATR, net	$ —	$ 7,651	$ —	$ —
Liability incurred to acquire TeraLogics, net	$ —	$ 4,998	$ —	$ —
Liability incurred to acquire H4 Global, net	$ —	$ 952	$ —	$ —

See accompanying notes.

Table of Contents

CUBIC CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

June 30, 2017

Note 1 — Basis for Presentation

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

In our opinion, the accompanying financial statements reflect all adjustments, consisting of normal recurring adjustments, considered necessary for a fair presentation of the results for the interim periods presented. Operating results for the three- and nine-month periods ended June 30, 2017 are not necessarily indicative of the results that may be expected for the year ending September 30, 2017. For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended September 30, 2016.

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

Significant Accounting Policies

There have been no material changes to our significant accounting policies as compared with the policies described in our Annual Report on Form 10-K for the year ended September 30, 2016.

Recent Accounting Pronouncements – Not Yet Adopted

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. ASU 2014-09 outlines a comprehensive revenue recognition model and supersedes most current revenue recognition guidance. The new guidance will require revenue to be recognized when promised goods or services are transferred to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. Adoption of the new rules could affect the timing of revenue recognition for certain transactions. Adoption of ASU 2014-09 will be required for us beginning in the first quarter of fiscal 2019 and we have determined that we will not adopt ASU 2014-09 earlier than required. ASU 2014-09 allows for two methods of adoption: (a) “full retrospective” adoption, meaning the standard is applied to all periods presented, or (b) “modified retrospective” adoption, meaning the cumulative effect of applying ASU 2014-09 is recognized as an adjustment to the opening retained earnings balance in the year of adoption. We have not yet determined which method of adoption we will select.

We have assigned a task force within management to lead our implementation efforts and we have engaged outside advisors to assist. We are currently in the process of analyzing the impact of the adoption of the new standard on our various revenue streams. Under ASU 2014-09, revenue is recognized as control transfers to the customer. As such, revenue for our fixed-price development and production contracts will generally be recognized over time as costs are incurred, which is consistent with the revenue recognition model we currently use for the majority of these contracts. For certain of our fixed-price production contracts where we currently recognize revenue as units are delivered, in most cases the accounting for those contracts will change under ASU 2014-09 such that we will recognize revenue as costs are incurred. This change will generally result in an acceleration of revenue as compared with our current revenue recognition method for those contracts. Approximately 13% of our net sales used the units-of-delivery method to recognize revenue in fiscal 2016. We continue to analyze the impact of the new standard on our remaining revenue streams and, as the standard will supersede substantially all existing revenue guidance affecting us under GAAP, we expect that it will impact revenue and cost recognition on a significant number of our contracts across our business segments, in addition to our business processes and our information technology systems. As a result, our evaluation of the effect of the new standard will continue to extend over several future periods.

In January 2016, the FASB issued Accounting Standards Update ASU 2016-01, Financial Instruments – Overall (Subtopic 825-10) which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01 will be effective for us beginning October 1, 2018 and, with the exception of a specific portion of the amendment, early adoption is not permitted. We are currently evaluating the impact this guidance will have on our financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02, Leases. Under the new guidance, leasees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (a) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (b) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. The ASU will be effective for us beginning October 1, 2019 with early adoption permitted. ASU 2016-02 will be adopted on a modified retrospective transition basis for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In March 2016, the FASB issued ASU 2016-09, Compensation-Stock Compensation. The new guidance simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The amendments in this standard are effective for our annual year and first fiscal quarter beginning on October 1, 2017 with early adoption permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements. We do not intend to adopt the new guidance early.

In August 2016, the FASB issued ASU 2016-15, Classification of Certain Cash Receipts and Cash Payments, which provides clarifying guidance on how entities should classify certain cash receipts and cash payments on the statement of cash flows. The guidance also clarifies how the predominance principle should be applied when cash receipts and cash payments have aspects of more than one class of cash flows. The guidance will be effective for us in our fiscal year beginning October 1, 2018, and early adoption is permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In October 2016, the FASB issued ASU 2016-16, Intra-Entity Transfers of Assets Other Than Inventory, which requires an entity to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. The guidance will be effective for us in our fiscal year beginning October 1, 2018, and early adoption is permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In November 2016, the FASB issued ASU 2016-18, Restricted Cash, which requires amounts generally described as restricted cash and restricted cash equivalents be included with cash and cash equivalents when reconciling the total beginning and ending amounts for the periods shown on the statement of cash flows. The guidance will be effective for us in our fiscal year beginning October 1, 2018, and early adoption is permitted. The adoption of this standard is anticipated to affect our presentation of restricted cash within our statement of cash flows. We are currently evaluating whether to adopt the new guidance early.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805) Clarifying the Definition of a Business. This ASU clarifies the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The definition of a business affects many areas of accounting including acquisitions, disposals, goodwill, and consolidation. The guidance will be effective for us in our fiscal year beginning October 1, 2018 and early adoption is allowed for certain transactions. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment. This standard removes the second step of the goodwill impairment test, where a determination of the fair value of individual assets and liabilities of a reporting unit was needed to measure the goodwill impairment. Under this updated standard, goodwill impairment will now be the amount by which a reporting unit’s carrying value exceeds its fair value, not to exceed the

Table of Contents

carrying amount of goodwill. The guidance will be effective for us in our fiscal year beginning October 1, 2020 with early adoption permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In March 2017, the FASB issued ASU 2017-07, Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The update requires employers to present the service cost component of the net periodic benefit cost in the same income statement line item as other employee compensation costs arising from services rendered during the period. The other components of net benefit cost, including interest cost, expected return on plan assets, amortization of prior service cost/credit and actuarial gain/loss, and settlement and curtailment effects, are to be presented outside of any subtotal of operating income. Employers will have to disclose the line(s) used to present the other components of net periodic benefit cost, if the components are not presented separately in the income statement. ASU 2017-07 will be effective for us beginning October 1, 2018, and early adoption is permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

Note 2 — Acquisitions

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

Vocality

On November 30, 2016, we acquired all of the outstanding capital stock of Vocality International (Vocality), based in Shackleford, United Kingdom, a provider of embedded technology which unifies communications platforms, enhances voice quality, increases video performance and optimizes data throughput. Vocality contributes to our Command, Control, Communications, Computers, Intelligence, Surveillance and Reconnaissance (C4ISR) portfolio of products for our Cubic Global Defense Systems (CGD Systems) segment and expands our defense customer base. Vocality also sells its technology in the broadcast, oil and gas, mining, and maritime markets.

Vocality’s sales and results of operations included in our operating results for the quarter and nine-months ended June 30, 2017 and 2016 were as follows (in millions):

	Nine Months Ended	Three Months Ended

	June 30, 2017	2016	June 30, 2017	2016
Sales	$ 1.2	$ —	$ 0.4	$ —
Operating loss	(2.3)	—	(0.7)	—
Net loss after taxes	(2.1)	—	(0.6)	—

Vocality's operating results above included the following amounts for the quarter and nine-month periods (in millions):

	Nine Months Ended June 30, 2017	2016	Three Months Ended June 30, 2017	2016
Amortization	$ 0.4	$ —	$ 0.2	$ —
Acquisition-related expenses	1.5	—	0.3	—

Prior to our acquisition of Vocality, Vocality had a number of share-based payment awards in place to its employees. Due to the structure of some of these share-based payment awards and the acceleration of vesting of certain of these awards in connection with our acquisition of Vocality, we were required to recognize compensation expense, rather than purchase consideration, for the portion of our purchase price that we paid to the seller that was distributed to the recipients of these awards. Consequently, we recognized $0.4 million of compensation expense within general and administrative expenses during the quarter ended December 31, 2016 related to this matter. This compensation is reflected in Vocality's acquisition-related expenses and results of operations above for the nine months ended June 30, 2017.

Table of Contents

The estimated acquisition date fair value of consideration is $9.6 million, which was comprised of cash paid of $8.9 million plus additional held back consideration to be paid in the future estimated at $1.1 million, less the $0.4 million of cash paid to the seller recorded as compensation expense described above.

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

Customer relationships	$ 2.1
Technology	2.4
Trade name	0.4
Inventory	1.7
Accounts payable and accrued expenses	(0.4)
Other net assets acquired (liabilities assumed)	(0.2)
Net identifiable assets acquired	6.0
Goodwill	3.6
Net assets acquired	$ 9.6

The preliminary estimated fair values of assets acquired and liabilities assumed, including purchased intangibles, inventory and deferred revenue are preliminary estimates pending the finalization of our valuation analyses. The preliminary estimated fair values of purchased intangibles were determined using the valuation methodology deemed to be the most appropriate for each type of asset being valued. The customer relationships valuation used the excess earnings approach, and the technology and trade name asset valuations used the relief from royalty approach.

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

The goodwill resulting from the acquisition consists primarily of the synergies expected from combining the operations of Vocality with our existing CGD Systems business, including the synergies expected from combining its communication unification technologies with our C4ISR products and other products in our CGD Systems portfolio. The goodwill also includes the value of the assembled workforce that became our employees following the close of the acquisition. The amount recorded as goodwill is allocated to our CGD Systems segment and is generally not expected to be deductible for tax purposes.

The estimated amortization expense related to the intangible assets recorded in connection with our acquisition of Vocality for fiscal years 2017 through 2021 and thereafter is as follows (in millions):

Year Ended September 30,	
2017	$ 0.6
2018	0.8
2019	0.7
2020	0.6
2021	0.5
Thereafter	1.7

GATR

On February 2, 2016, we acquired all of the outstanding capital stock of GATR Technologies, LLC (GATR), a defense systems business based in Huntsville, Alabama which manufactures deployable satellite communication terminal solutions. GATR expands our satellite communications and networking applications technologies for our CGD Systems segment and expands our customer base.

Table of Contents

GATR’s sales and results of operations included in our operating results for the quarter and nine-months ended June 30, 2017 and 2016 were as follows (in millions):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Sales	$ 51.4	$ 18.6	$ 24.0	$ 9.3
Operating income (loss)	(2.6)	(24.5)	2.7	(3.8)
Net income (loss) after taxes	(1.6)	(20.6)	1.6	(2.3)

GATR’s operating results above included the following amounts for the quarter and nine-month periods (in millions):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Amortization	$ 9.7	$ 6.0	$ 3.1	$ 3.6
Gains (losses) for changes in fair value of contingent consideration	3.2	(0.7)	1.5	(0.6)
Acquisition-related expenses	1.3	20.2	0.5	0.8

GATR’s operating results for the nine months ended June 30, 2016 were significantly impacted by the GAAP accounting requirements regarding business combinations. Prior to our acquisition of GATR, GATR had a number of share-based payment awards in place to its employees. Due to the structure of certain of these share-based payment awards and the acceleration of vesting of certain of these awards in connection with our acquisition of GATR, we were required to recognize compensation expense, rather than purchase consideration, for the portion of our purchase price that we paid to the seller that was distributed to the recipients of these awards. Consequently, we recognized $18.5 million of compensation expense within general and administrative expenses during the quarter ended March 31, 2016 related to this matter. This compensation expense is reflected in GATR’s acquisition-related expenses and the results of GATR’s operations above. Of this $18.5 million amount, $15.4 million is not deductible for tax purposes.

The estimated acquisition-date fair value of consideration is $220.5 million, which is comprised of cash paid of $236.1 million plus the estimated fair value of contingent consideration of $2.5 million, less $18.1 million of cash paid to the seller that was recognized as expense in fiscal 2016. Under the purchase agreement, we will pay the sellers up to $7.5 million of contingent consideration if GATR meets certain gross profit goals for the 12 month periods ended February 28, 2017 and 2018. The contingent consideration liability will be re-measured to fair value at each reporting date until the contingencies are resolved and any changes in fair value are recognized in earnings.

The acquisition of GATR was paid for predominantly with the proceeds of borrowings on our revolving credit agreement, described below, in the second quarter of fiscal 2016. The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date (in millions):

Customer relationships	$ 51.7
Backlog	3.4
Technology	10.7
Non-compete agreements	1.2
Trade name	4.7
Accounts receivable	10.6
Inventory	3.4
Income tax receivable	5.1
Accounts payable and accrued expenses	(2.4)
Deferred tax liabilities	(23.8)
Net identifiable assets acquired	64.6
Goodwill	155.9
Net assets acquired	$ 220.5

Table of Contents

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

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

The goodwill resulting from the acquisition consists primarily of the synergies expected from combining the operations of GATR with our existing CGD Systems business, including the synergies expected from combining its satellite communications and networking applications technologies with our C4ISR products and other products in our CGD Systems portfolio. The goodwill also includes the value of the assembled workforce that became our employees following the close of the acquisition. The amount recorded as goodwill is allocated to our CGD Systems segment and is not expected to be deductible for tax purposes.

The estimated amortization expense related to the intangible assets recorded in connection with our acquisition of GATR for fiscal years 2017 through 2021 and thereafter is as follows (in millions):

Year Ended September 30,	
2017	$ 12.7
2018	11.1
2019	9.8
2020	8.3
2021	6.9
Thereafter	13.2

TeraLogics

On December 21, 2015, we acquired all of the assets of TeraLogics, LLC, an Ashburn, Virginia-based provider of real-time full motion video processing, exploitation and dissemination for the Department of Defense, the intelligence community and commercial customers. TeraLogics' ability to develop real-time video analysis and delivery software for full motion video complements the existing tactical communications portfolio of our CGD Systems segment and expands our customer base.

Teralogic's sales and results of operations included in our operating results for the quarter and nine-months ended June 30, 2017 and 2016 were as follows (in millions):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Sales	$ 14.0	$ 8.0	$ 3.0	$ 4.2
Operating loss	(1.1)	(2.4)	(0.9)	(0.4)
Net loss after taxes	(0.7)	(1.4)	(0.6)	(0.2)

Teralogic's operating results above included the following amounts for the quarter and nine-month periods (in millions):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Amortization	$ 2.7	$ 2.0	$ 0.9	$ 1.0
Gains (losses) for changes in fair value of contingent consideration	(0.2)	(0.1)	—	(0.2)
Acquisition-related expenses	0.2	2.3	0.1	0.1

Table of Contents

During the quarter ended December 31, 2015 we incurred a $1.3 million charge for compensation expense incurred related to amounts paid to TeraLogics employees upon the close of the acquisition. This compensation expense is reflected in Teralogic's acquisition-related expenses and the results of Teralogic's operations above.

The estimated acquisition-date fair value of consideration is $33.9 million, which is comprised of cash paid of $28.9 million plus the estimated acquisition-date fair value of contingent consideration of $5.0 million. Under the purchase agreement, we will pay the sellers up to $9.0 million of contingent consideration. Of this amount, up to $6.0 million will be paid if TeraLogics meets certain revenue thresholds in fiscal years 2016, 2017 and 2018; and up to $3.0 million will be paid if specific contract extensions are exercised by TeraLogics customers through fiscal 2018. The contingent consideration liability will be re-measured to fair value at each reporting date until the contingencies are resolved and any changes in fair value are recognized in earnings.

Through June 30, 2017 we have paid $32.4 million to the seller. At June 30, 2017 we have recorded a liability of $3.2 million as an estimate of the additional cash consideration that will be due to the seller in the future.

The acquisition of TeraLogics is being paid for with a combination of funds from our existing cash resources and borrowings on our revolving credit facility. The following table summarizes the fair values of the assets acquired and liabilities assumed at the acquisition date (in millions):

Customer relationships	$	6.7
Backlog		5.6
Software		2.5
Non-compete agreements		0.1
Accounts receivable		1.4
Accounts payable and accrued expenses		(0.5)
Other net assets acquired (liabilities assumed)		(0.1)
Net identifiable assets acquired		15.7
Goodwill		18.2
Net assets acquired	$	33.9

The fair values of purchased intangibles were determined using the valuation methodology deemed to be the most appropriate for each type of asset being valued. The customer relationships and backlog valuation used the excess earnings approach, the non-compete agreements used the with-and-without approach, and the software used the replacement cost new less cost decrements for obsolescence approach.

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

The goodwill resulting from the acquisition consists primarily of the synergies expected from combining the operations of TeraLogics with our existing CGD Systems business, including the synergies expected from combining TeraLogics real-time video capabilities with our existing tactical communications product portfolio. The goodwill also includes the value of the assembled workforce who became our employees following the close of the acquisition. The amount recorded as goodwill is allocated to our CGD Systems segment and is expected to be deductible for tax purposes.

The estimated amortization expense amounts related to the intangible assets recorded in connection with our acquisition of TeraLogics for fiscal years 2017 through 2021 and thereafter is as follows (in millions):

Year Ended September 30,	
2017	$ 3.5
2018	2.8
2019	2.1
2020	1.4
2021	0.8
Thereafter	1.4

Table of Contents

H4 Global

On November 4, 2015, we acquired all of the assets of H4 Global, a U.K.-based provider of simulation-based training solutions which complements our CGD Systems segment training portfolio.

H4 Global’s sales and results of operations included in our operating results for the quarter and nine months ended June 30, 2017 and 2016 were as follows (in millions):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Sales	$ 2.6	$ 1.4	$ 1.0	$ 0.8
Operating income (loss)	(0.5)	0.1	(0.2)	0.1
Net income (loss) after taxes	(0.4)	0.1	(0.2)	0.1

H4 Global’s operating results above included the following amounts for the quarter and nine-month periods (in millions):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Amortization	$ 0.1	$ —	$ —	$ —
Gains (losses) for changes in fair value of contingent consideration	—	0.2	(0.1)	—
Acquisition-related expenses	—	0.1	—	—

The acquisition-date fair value of consideration is $1.9 million, which is comprised of cash paid of $0.9 million plus the fair value of contingent consideration of $1.0 million. Under the purchase agreement, we will pay the sellers up to $4.1 million of contingent consideration, based upon the value of contracts entered over the five-year period beginning on the acquisition date. The contingent consideration liability will be re-measured to fair value at each reporting date until the contingencies are resolved and any changes in fair value will be recognized in earnings.

The fair value of the net assets acquired and liabilities assumed was not material. Consequently, virtually the entire purchase price of $1.9 million was recorded as goodwill, which is comprised of expected synergies and assembled workforce. The amount recorded as goodwill is allocated to our CGD Systems segment and is not expected to be deductible for tax purposes.

Pro forma information

The following unaudited pro forma information presents our consolidated results of operations as if Vocality, GATR, TeraLogics and H4 Global had been included in our consolidated results since October 1, 2015 (in millions):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Net sales	$ 1,040.5	$ 1,079.4	$ 361.9	$ 376.2
Net income (loss)	$ (24.6)	$ 8.0	$ (22.0)	$ 4.2

The pro forma information includes adjustments to give effect to pro forma events that are directly attributable to the acquisitions and have a continuing impact on operations including the amortization of purchased intangibles and the elimination of interest expense for the repayment of debt. No adjustments were made for transaction expenses, other adjustments that do not reflect ongoing operations or for operating efficiencies or synergies. The pro forma financial information is not necessarily indicative of what the consolidated financial results of our operations would have been had the acquisitions been completed on October 1, 2015, and it does not purport to project our future operating results.

Table of Contents

Goodwill

Changes in goodwill for the nine months ended June 30, 2017 were as follows (in millions):

	Transportation Systems	Cubic Global Defense Systems	Cubic Global Defense Services	Total
Net balances at September 30, 2016	$ 49,630	$ 262,966	$ 94,350	$ 406,946
Acquisitions	—	3,642	—	3,642
Foreign currency exchange rate changes	148	166	—	314
Net balances at June 30, 2017	$ 49,778	$ 266,774	$ 94,350	$ 410,902

Goodwill represents the purchase price paid in excess of the fair value of net tangible and intangible assets acquired. Goodwill is not amortized but is subject to an impairment test on an annual basis and when circumstances indicate that an impairment is more-likely-than-not. Such circumstances include a significant adverse change in the business climate for one of our reporting units or a decision to dispose of a reporting unit or a significant portion of a reporting unit. The test for goodwill impairment is a two-step process. The first step of the test is performed by comparing the fair value of each reporting unit to its carrying value, including recorded goodwill. If the carrying value of a reporting unit exceeds its fair value, the second step is performed to measure the amount of the impairment, if any, by comparing the implied fair value of goodwill to its carrying value. Any resulting impairment determined would be recorded in the current period.

Our most recent annual goodwill impairment test was our 2016 annual impairment test completed as of July 1, 2016. Subsequent to the effective date of that test, we do not believe that circumstances have occurred that indicate that an impairment is more-likely-than-not. As such, no subsequent interim impairment test has been performed. The results of our 2016 annual impairment test indicated that the estimated fair values for our CGD Services and Transportation Systems reporting units each exceeded their carrying values by over 20%, while the estimated value of our CGD Systems reporting unit exceeded its carrying value by over 15%.

Significant management judgment is required in the forecast of future operating results that are used in our impairment analysis. The estimates we used are consistent with the plans and estimates that we use to manage our business. For our CGD Services reporting unit, significant assumptions utilized in our discounted cash flow approach included growth rates for sales and margins at greater levels than we have achieved in the past six years, but at levels that are less than the average annual growth we achieved over the period from fiscal 2000 through fiscal 2010. Assumptions used in our discounted cash flow approach for our CGD Services reporting unit also included growth rates for sales and margins at greater levels than we have achieved in recent years due to our expectation that businesses recently acquired by this reporting unit will achieve growth at higher rates than the unit’s legacy operations.

While our interim assessment of our reporting units did not indicate that impairment was more-likely-than-not for any reporting unit, we believe that, based on the results achieved by our CGD Services reporting unit to date in fiscal 2017, there is a heightened risk that a step two impairment test could be required in the future.

Unforeseen negative changes in future business or other market conditions for any of our reporting units including margin compression or loss of business, could cause recorded goodwill to be impaired in the future. Also, changes in estimates and assumptions we make in conducting our goodwill assessment could affect the estimated fair value of our reporting units and could result in a goodwill impairment charge in a future period.

Subsequent event - acquisition of Deltenna Ltd

In July 2017, we acquired all of the outstanding capital stock of Deltenna Ltd (Deltenna), a defense systems business based in Chippenham, England which specializes in LTE wireless communication solutions for non-stationary and on-the-move defense applications. The purchase price is $4.0 million adjusted for the difference between net working capital acquired and a targeted working capital amount plus up to $7.0 million of contingent consideration.

Note 3 — Net Income (Loss) Per Share

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

Table of Contents

In periods with a net income, diluted EPS is computed by dividing the net income for the period by the weighted average number of common and common equivalent shares outstanding during the period. Common equivalent shares consist of dilutive restricted stock units. Dilutive restricted stock units are calculated based on the average share price for each fiscal period using the treasury stock method. For RSUs with performance-based vesting, no common equivalent shares are included in the computation of diluted EPS until the related performance criteria have been met. In periods with a net loss, common equivalent shares are not included in the computation of diluted EPS, because to do so would be anti-dilutive. For the quarter and nine months ended June 30, 2017, the effect of 1.0 million shares of restricted stock were excluded from diluted loss per share that would have been included if we had been in a net income position. There were no anti-dilutive securities for the three and nine months ended June 30, 2017 or for the three and nine months ended June 30, 2016.

Basic and diluted EPS are computed as follows (amounts in thousands, except per share data).

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Net income (loss)	$ (24,364)	$ 9,228	$ (21,957)	$ 4,498
Weighted average shares - basic	27,100	26,971	27,110	26,977
Effect of dilutive securities	—	39	—	81
Weighted average shares - diluted	27,100	27,010	27,110	27,058
Net income (loss) per share, basic	$ (0.90)	$ 0.34	$ (0.81)	$ 0.17
Effect of dilutive securities	—	—	—	—
Net income (loss) per share, diluted	$ (0.90)	$ 0.34	$ (0.81)	$ 0.17

Note 4 — Balance Sheet Details

Marketable Securities

Marketable securities consist of fixed time deposits with short-term maturities. Marketable securities are classified and accounted for as available-for-sale. These investments are recorded at fair value in the accompanying Condensed Consolidated Balance Sheets and the change in fair value is recorded, net of taxes, as a component of other comprehensive loss. There have been no significant realized or unrealized gains or losses on these marketable securities to date. Marketable securities have been classified as current assets in the accompanying Condensed Consolidated Balance Sheets based upon the nature of the securities and availability for use in current operations.

Accounts Receivable

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

	June 30, 2017	September 30, 2016
Trade and other receivables	$ 11,357	$ 15,488
Long-term contracts:		
Billed	163,174	146,619
Unbilled	209,014	241,726
Allowance for doubtful accounts	(401)	(326)
Total accounts receivable	383,144	403,507
Less estimated amounts not currently due	(21,301)	(20,926)
Current accounts receivable	$ 361,843	$ 382,581

Table of Contents

The amount classified as not currently due is an estimate of the amount of long-term contract accounts receivable that will not be collected within one year from June 30, 2017 under transportation systems contracts in the U.S. and Australia, and under a CGD Systems contract in Italy based upon the payment terms in the contracts. The non-current balance at September 30, 2016 represented non-current amounts due from these same customers.

Inventories

Inventories consist of the following (in thousands):

	June 30, 2017	September 30, 2016
Finished products	$ 7,223	$ 10,018
Work in process and inventoried costs under long-term contracts	100,945	62,570
Materials and purchased parts	9,798	12,102
Customer advances	(14,528)	(18,328)
Net inventories	$ 103,438	$ 66,362

Pursuant to contract provisions, agencies of the U.S. government and certain other customers have title to, or security interest in, inventories related to such contracts as a result of advances, performance-based payments, and progress payments. Contract advances, performance-based payments and progress payments received are recorded as an offset against the related inventory balances for contracts that are accounted for on a percentage-of-completion basis using units-of-delivery as the basis to measure progress toward completing the contract. This determination is performed on a contract by contract basis. Any amount of payments received in excess of the cumulative amount of accounts receivable and inventoried costs for a contract is classified as customer advances, which is classified as a liability on the balance sheet.

At June 30, 2017, work in process and inventoried costs under long-term contracts includes approximately $3.3 million in costs incurred outside the scope of work or in advance of a contract award compared to $0.7 million at September 30, 2016. We believe it is probable that we will recover the costs inventoried at June 30, 2017, plus a profit margin, under contract change orders or awards within the next year.

Long-term Capitalized Costs

Long-term capitalized contract costs include costs incurred on contracts to develop and manufacture transportation systems for customers for which revenue recognition does not begin until the customers begin operating the systems. These capitalized costs are being recognized in cost of sales based upon the ratio of revenue recorded during a period compared to the revenue expected to be recognized over the term of the contracts. Long-term capitalized costs that were recognized as cost of sales totaled $2.2 million and $7.0 million for the quarter and nine-month periods ended June 30, 2017, respectively, and $2.2 million and $6.5 million for the quarter and nine-month periods ended June 30, 2016, respectively.

Capitalized Software

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

As a part of our efforts to upgrade our current information systems, early in fiscal 2015 we purchased new enterprise resource planning (ERP) software and began the process of designing and configuring this software and other software applications to manage our operations. Certain components of our ERP system became ready for their intended use and were placed into service on April 1, 2016 and on October 1, 2016 at which time the capitalized costs of developing those components were transferred into completed software and we began amortizing these costs over the seven year estimated useful life of these software components.

Table of Contents

We continue to capitalize costs associated with the development of other ERP components that are not yet ready for their intended use. We capitalized costs related to ERP components in development totaling $5.2 million and $11.7 million for the quarter and nine-month periods ended June 30, 2017, respectively, and $4.3 million and $19.0 million for the quarter and nine-month periods ended June 30, 2016, respectively.

In addition to software costs that were capitalized, during the quarter and nine-month periods ended June 30, 2017 we recognized expense related to the development and implementation of our ERP system of $5.6 million and $15.6 million, respectively, compared to $5.1 million and $17.1 million during the quarter and nine-month periods ended June 30, 2016, respectively, for costs that did not meet the requirements for capitalization. Amounts that were expensed in connection with the development and implementation of these systems are classified within selling, general and administrative expenses in the Condensed Consolidated Statements of Income (Loss).

Deferred Compensation Plan

We have a non-qualified deferred compensation plan offered to a select group of highly compensated employees. The plan provides participants with the opportunity to defer a portion of their compensation in a given plan year. The liabilities associated with the non-qualified deferred compensation plan are included in other long-term liabilities in our Condensed Consolidated Balance Sheets and totaled $10.9 million and $10.6 million at June 30, 2017 and September 30, 2016, respectively.

In fiscal 2015, we began making contributions to a rabbi trust to provide a source of funds for satisfying a portion of these deferred compensation liabilities. The total carrying values of assets set aside to fund deferred compensation liabilities as of June 30, 2017 and September 30, 2016 were $5.1 million and $3.6 million, respectively, which were comprised entirely of life insurance contracts. The carrying value of the life insurance contracts is based on the cash surrender value of the policies. Changes in the carrying value of the deferred compensation liability, and changes in the carrying value of the assets held in the rabbi trust are reflected in our Condensed Consolidated Statements of Income (Loss).

Note 5 — Fair Value of Financial Instruments

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

- Level 1 - Quoted prices for identical instruments in active markets.

- Level 2 - Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.
- Level 3 - Significant inputs to the valuation model are unobservable.

The fair value of certain of our cash equivalents are based upon quoted prices for identical instruments in active markets. The fair value of our other cash equivalents and our available for sale marketable securities is based upon a discounted cash flow model and approximate cost. Derivative financial instruments are measured at fair value, the material portions of which are based on active or inactive markets for identical or similar instruments or model-derived valuations whose inputs are observable. Where model-derived valuations are appropriate, we use the applicable credit spread as the discount rate. Credit risk related to derivative financial instruments is considered minimal and is managed by requiring high credit standards for counterparties and through periodic settlements of positions.

The fair value of our contingent consideration liabilities to the sellers of businesses that we have acquired are revalued to their fair value each period and any increase or decrease is recorded into selling, general and administrative expense. Any changes in the assumed timing and amount of the probability of payment scenarios could impact the fair value.

The fair value of contingent consideration liabilities that are based upon revenue targets or gross margin targets are based upon a real option approach. The contingent consideration liabilities that are valued using this real option approach include a portion of the TeraLogics contingent consideration, the DTECH contingent consideration, and the GATR contingent consideration. Under this real option approach, each payment was modeled using long digital options written on the underlying revenue or gross margin metric. The strike price for each option is the respective revenue or

Table of Contents

gross margin as specified in the related agreement, and the spot price is calibrated to the revenue or gross margin forecast by calculating the present value of the corresponding projected revenues or gross margins using a risk-adjusted discount rate. The volatility for the underlying revenue metrics was based upon analysis of comparable guideline public companies and the volatility factor used in the June 30, 2017 valuations was 15% for TeraLogics, 19% for DTECH and 15% for GATR. The volatility factor used in the September 30, 2016 valuation was 17% for TeraLogics, 18% for DTECH and 17% for GATR. The risk-free rate was selected based on the quoted yields for U.S. Treasury securities with terms matching the earn-out payment period.

The fair value of the portion of the TeraLogics contingent consideration that is based on customer execution of contract extensions was estimated using a probability weighted approach. Subject to the terms and conditions of the TeraLogics Purchase Agreement, contingent consideration will be paid over a period commencing on the closing date and ending on December 21, 2018. The fair value of the contingent consideration was determined by applying probabilities of achieving the periodic payment to each period’s potential payment, and summing the present value of any future payments.

The fair value of the H4 Global contingent consideration was estimated using a probability weighted approach. Subject to the terms and conditions of the H4 Global Purchase Agreement, contingent consideration will be paid over a five year term that commenced on October 1, 2015 and ends on September 30, 2020. The payments will be calculated based on the award of certain contracts during the specified period. The fair value of the contingent consideration was determined by applying probabilities to different scenarios, and summing the present value of any future payments.

The inputs to each of the contingent consideration fair value models include significant unobservable inputs and therefore represent Level 3 measurements within the fair value hierarchy. Significant judgment is employed in determining the appropriateness of these assumptions as of the acquisition dates and each subsequent period. Accordingly, changes in the assumptions described above can materially impact the amount of contingent consideration expense we record in any period.

As of June 30, 2017, the following table summarizes the change in fair value of our Level 3 contingent consideration liability (in thousands):

	DTECH	H4	TeraLogics (Contract Extensions)	TeraLogics (Revenue Targets)	GATR	Total
Balance as of September 30, 2016	$ 2,000	$ 567	$ 1,400	$ 4,100	$ 3,200	$ 11,267
Cash paid to seller	—	—	—	(2,500)	—	(2,500)
	(1,700)	(13)	300	(100)	(3,200)	(4,713)

Total remeasurement (gain) loss recognized in earnings						
Balance as of June 30, 2017	$ 300	$ 554	$ 1,700	$ 1,500	$ —	$ 4,054

The total remeasurement (gain) loss recognized in earnings totaled gain of $2.5 million and $4.7 million for the three and nine-month periods ended June 30, 2017, respectively, compared to losses of $1.1 million and $2.8 million, respectively, for the three and nine-month periods ended June 30, 2016.

We hold certain non-marketable debt and equity securities which consist primarily of convertible notes and warrants issued by private companies. The fair value of non-marketable debt and equity securities are included within other assets.

The fair value of non-marketable debt securities is estimated using (i) discounted cash flow approach in which the contractual payments of the note principal and interest are present-valued using a discount rate adjusted for the credit risk of the note issuer, and (ii) option approach in which the value of the equity conversion feature is estimated using an option-pricing model such as Black-Scholes. The fair value of non-marketable equity securities is estimated using the Black-Scholes model.

The inputs to each of the fair value models described above include significant unobservable inputs such as the credit-risk adjusted discount rate of the issuer, the value of the stock of the issuer and its expected return volatility, and therefore represent Level 3 measurements within the fair value hierarchy.

Table of Contents

As of June 30, 2017, the following table summarizes the changes in fair value of our Level 3 non-marketable debt and equity security assets (in thousands):

	Total non-marketable debt and equity securities
Balance as of September 30, 2016	$ —
Purchases	2,200
Balance as of June 30, 2017	$ 2,200

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

	June 30, 2017				September 30, 2016			
	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets								
Cash equivalents	$ 79	$ —	$ —	$ 79	$ 57,455	$ —	$ —	$ 57,455
Marketable securities	—	13,060	—	13,060	—	12,996	—	12,996
Current derivative assets	—	2,459	—	2,459	—	14,770	—	14,770
Noncurrent derivative assets	—	846	—	846	—	1,201	—	1,201
Marketable securities in rabbi trust	17	—	—	17	4	—	—	4
Non-marketable debt and equity securities	—	—	2,200	2,200	—	—	—	—
Total assets measured at fair value	$ 96	$ 16,365	$ 2,200	$ 18,661	$ 57,459	$ 28,967	$ —	$ 86,426
Liabilities								
Current derivative liabilities	—	3,096	—	3,096	—	13,752	—	13,752
Noncurrent derivative	—	846	—	846	—	1,334	—	1,334

liabilities								
Contingent consideration to seller of GATR	—	—	—	—	—	—	3,200	3,200
Contingent consideration to seller of TeraLogics - contract extensions	—	—	1,700	1,700	—	—	1,400	1,400
Contingent consideration to seller of TeraLogics - revenue targets	—	—	1,500	1,500	—	—	4,100	4,100
Contingent consideration to seller of H4 Global	—	—	554	554	—	—	567	567
Contingent consideration to seller of DTECH	—	—	300	300	—	—	2,000	2,000
Total liabilities measured at fair value	$ —	$ 3,942	$ 4,054	$ 7,996	$ —	$ 15,086	$ 11,267	$ 26,353

We carry certain financial instruments, including accounts receivable, short-term borrowings, accounts payable and accrued liabilities at cost, which we believe approximates fair value because of the short-term maturity of these instruments.

Table of Contents

The fair value of long-term debt is calculated by discounting the value of the note based on market interest rates for similar debt instruments, which is a Level 2 technique. The following table presents the estimated fair value and carrying value of our long-term debt (in millions):

	June 30, 2017	September 30, 2016
Fair value	$ 204.9	$ 210.0
Carrying value	$ 200.7	$ 201.0

Note 6 — Financing Arrangements

In March 2013, we entered into a note purchase and private shelf agreement pursuant to which we issued $100.0 million of senior unsecured notes, bearing interest at a rate of 3.35% and maturing on March 12, 2025. In addition, pursuant to the agreement, on July 17, 2015, we issued an additional $25.0 million of senior unsecured notes bearing interest at a rate of 3.70% and maturing on March 12, 2025. Interest payments on the notes issued in 2013 and 2015 are due semi-annually and principal payments are due from 2021 through 2025. The agreement pertaining to the aforementioned notes also contained a provision that the coupon rate would increase by a further 0.50% should the company’s leverage ratio exceed a certain level. On February 2, 2016, we revised the note purchase agreement and we issued an additional $75.0 million of senior unsecured notes bearing interest at 3.93% and maturing on March 12, 2026. Interest payments on these notes are due semi-annually and principal payments are due from 2020 through 2026. At the time of the issuance of this last series of notes, certain terms and conditions of the note purchase and private shelf agreement were revised in coordination with the revision and expansion of the revolving credit agreement as discussed below in order to increase our leverage capacity.

We have a committed revolving credit agreement with a group of financial institutions in the amount of $400.0 million which expires in August 2021 (Revolving Credit Agreement). At June 30, 2017, the weighted average interest rate on outstanding borrowings under the Revolving Credit Agreement was 3.48%. Debt issuance and modification costs of $2.3 million and $1.3 million were incurred in connection with February 2, 2016 and August 11, 2016 amendments to the Revolving Credit Agreement, respectively. Costs incurred in connection with establishment of and amendments to this credit agreement are recorded in prepaid expenses and other current assets on our Condensed Consolidated Balance Sheets, and are being amortized as interest expense using the effective interest method over the stated term of the Revolving Credit Agreement. At June 30, 2017, the Company’s total debt issuance costs have an unamortized balance of $2.7 million. The available line of credit is reduced by any letters of credit issued under the Revolving Credit Agreement. As of June 30, 2017, there were borrowings totaling $104.0 million under this agreement and there were letters of credit outstanding totaling $78.7 million, which reduce the available line of credit to $217.3 million.

Until June 2017, we had a secured letter of credit facility agreement with a bank in the U.K. At September 30, 2016, there were letters of credit outstanding under this agreement of $62.7 million. Restricted cash at September 30, 2016 of $69.4 million was held on deposit in the U.K. as collateral in support of this facility. In June 2017, this agreement was terminated and the associated letters of credit were transferred to the Revolving Credit Agreement described above. The cash that formerly collateralized the secured credit facility was used to make principal payments to reduce our outstanding short-term borrowings.

Our revolving credit agreement and note purchase and private shelf agreement each contain a number of customary covenants, including requirements for us to maintain certain interest coverage and leverage ratios and restrictions on our and certain of our subsidiaries' abilities to, among other things, incur additional debt, create liens, consolidate or merge with any other entity, or transfer or sell substantially all of their assets, in each case subject to certain exceptions and limitations. The occurrence of any event of default under these agreements may result in all of the indebtedness then outstanding becoming immediately due and payable. At March 31, 2017 we did not maintain the required leverage ratio. Therefore in May 2017 certain terms and conditions of the revolving credit agreement and note purchase and private shelf agreement were further revised to allow us to maintain a higher level of leverage as of March 31, 2017 and for the remainder of the 2017 fiscal year. This revision also contains a provision that the coupon rate may increase on all of the term notes discussed above by up to 0.75% should our leverage ratio exceed certain levels. In connection with this revision, we incurred $0.4 million of costs, primarily for amounts charged by our lenders in connection with these modifications. These costs were recorded in May 2017 as a reduction in the carrying value of the related debt liability and which will be amortized into additional interest expense over the life of the related debt.

Table of Contents

We maintain a cash account with a bank in the United Kingdom for which the funds are restricted as to use. The account is required to secure the customer's interest in cash deposited in the account to fund our activities related to our performance under a fare collection services contract in the United Kingdom. The balance in the account as of June 30, 2017 was $4.6 million and is classified as restricted cash in our Condensed Consolidated Balance Sheets.

As of June 30, 2017, we had letters of credit under the Revolving Credit Agreement and bank guarantees outstanding totaling $74.7 million that guarantee either our performance or customer advances under certain contracts. In addition, we had financial letters of credit outstanding totaling $16.9 million as of June 30, 2017, which primarily guarantee our payment of certain self-insured liabilities. We have never had a drawing on a letter of credit instrument, nor are any anticipated; therefore, we estimate the fair value of these instruments to be zero.

We maintain a short-term borrowing arrangement in New Zealand totaling $0.5 million New Zealand dollars (equivalent to approximately $0.4 million) to help meet the short-term working capital requirements of our subsidiary. At June 30, 2017, no amounts were outstanding under this borrowing arrangement.

The terms of certain of our lending and credit agreements include provisions that require and/or limit, among other financial ratios and measurements, the permitted levels of debt, coverage of cash interest expense, and under certain circumstances, payments of dividends or other distributions to shareholders. As of June 30, 2017, these agreements restrict such distributions to shareholders to a maximum of $39.4 million in fiscal year 2017.

Our self-insurance arrangements are limited to certain workers' compensation plans, automobile liability and product liability claims. Under these arrangements, we self-insure only up to the amount of a specified deductible for each claim. Self-insurance liabilities included in other current liabilities on the balance sheet amounted to $7.6 million and $8.2 million as of June 30, 2017 and September 30, 2016, respectively.

Note 7 — Pension Plans

The components of net periodic pension cost (benefit) are as follows (in thousands):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016

Service cost	$ 457	$ 457	$ 155	$ 147
Interest cost	5,293	6,787	1,775	2,247
Expected return on plan assets	(9,634)	(10,028)	(3,234)	(3,253)
Amortization of actuarial loss	2,748	1,401	926	489
Administrative expenses	142	131	48	45
Net pension benefit	$ (994)	$ (1,252)	$ (330)	$ (325)

Note 8 - Stockholders' Equity

Long-Term Equity Incentive Plan

In 2013, the Executive Compensation Committee of our Board of Directors (Compensation Committee) approved a long-term equity incentive award program. Through June 30, 2017, the Compensation Committee has granted 917,802 RSUs with time-based vesting and 993,298 RSUs with performance-based vesting under this program.

Each RSU represents a contingent right to receive one share of our common stock. Dividend equivalent rights accrue with respect to the RSUs when and as dividends are paid on our common stock and vest proportionately with the RSUs to which they relate. Vested shares are delivered to the recipient following each vesting date.

The RSUs granted with time-based vesting generally vest in four equal installments on each of the four October 1 dates following the grant date, subject to the recipient's continued service through such vesting date.

The performance-based RSUs granted to participants vest over three-year performance periods based on Cubic's achievement of performance goals established by the Compensation Committee over the performance periods, subject to the recipient's continued service through the end of the respective performance periods. For the performance-based

Table of Contents

RSUs granted to date, the vesting will be contingent upon Cubic meeting one of three types of vesting criteria over the performance period. These three categories of vesting criteria consist of revenue growth targets, earnings growth targets, and return on equity targets. The level at which Cubic performs against scalable targets over the performance periods will determine the percentage of the RSUs that will ultimately vest.

Through June 30, 2017, Cubic has granted 1,911,100 RSUs of which 449,902 have vested. The grant date fair value of each RSU is the fair market value of one share of our common stock at the grant date. At June 30, 2017, the total number of unvested RSUs that are ultimately expected to vest, after consideration of expected forfeitures and estimated vesting of performance-based RSUs, is 440,045.

The following table summarizes our RSU activity:

	Unvested Restricted Stock Units		
	Number of Shares	Weighted-Average Grant-Date Fair Value	
Unvested at September 30, 2016	889,129	$	45.98
Granted	465,457		46.18
Vested	(156,537)		46.17
Forfeited	(78,777)		48.41
Unvested at June 30, 2017	1,119,272	$	45.86

Note 9 - Stock-Based Compensation

We recorded non-cash compensation expense related to stock-based awards for the three- and nine-month periods ended June 30, 2017 and 2016 as follows (in thousands):

Nine Months Ended

			Three Months Ended	
	June 30,		June 30,	
	2017	2016	2017	2016
Cost of sales	$ 412	$ 856	$ 129	$ 312
Selling, general and administrative	3,414	6,060	340	2,516
	$ 3,826	$ 6,916	$ 469	$ 2,828

As of June 30, 2017, there was $40.5 million of unrecognized compensation cost related to unvested RSUs. Based upon the expected forfeitures and the expected vesting of performance based RSUs, the aggregate fair value of RSUs expected to ultimately vest is $20.0 million. This amount is expected to be recognized over a weighted-average period of 1.7 years.

We are required to estimate forfeitures at the time of grant and revise those estimates in subsequent periods on a cumulative basis in the period the estimated forfeiture rate changes for all stock-based awards when significant events occur. We consider our historical experience with employee turnover as the basis to arrive at our estimated forfeiture rate. The forfeiture rate was estimated to be 12.5% per year as of June 30, 2017. To the extent the actual forfeiture rate is different from what we have estimated, stock-based compensation related to these awards will be different from our expectations.

Note 10 – Income Taxes

During interim periods, the Company generally utilizes the estimated annual effective tax rate method which involves the use of forecasted information. Under this method, the provision is calculated by applying an estimate of the annual effective tax rate for the full fiscal year to “ordinary” income or loss (pretax income or loss excluding unusual or infrequently occurring discrete items) for the reporting period. Although the Company believes the use of the annual effective tax rate method to be appropriate for prior interim reporting periods, for the fiscal three-month and nine-month periods ended June 30, 2017, the Company believes it is more appropriate to use a blend of the discrete effective tax rate method and the estimated annual effective tax rate method to calculate income tax expense for the period. The Company determined that since small changes in estimated “ordinary” income for U.S. operations would result in significant changes in the worldwide estimated annual effective tax rate, the discrete tax rate method should be utilized to determine a more reliable estimate of U.S. income tax expense for the period.

Table of Contents

Income tax expense recognized on pre-tax losses for the three and nine months ended June 30, 2017 resulted in effective tax rates of (430%) and (31%), respectively. The most significant items contributing to the difference between the statutory U.S. federal income tax rate of 35% and the Company's effective tax rate for the three-month and nine-month periods ending June 30, 2017 was the $20.1 million impact of recording the U.S. provision utilizing a discrete vs. annual effective rate tax rate method partially offset by the tax benefit related to the reversal of certain tax contingencies due to the lapse of the statute of limitations.

The amount of net unrecognized tax benefits was $5.9 million as of June 30, 2017 and $10.2 million as of September 30, 2016, exclusive of interest and penalties. The decrease in net unrecognized tax benefits was primarily related to a lapse of the statute of limitations on tax positions taken in previous years. At June 30, 2017, the amount of net unrecognized tax benefits from permanent tax adjustments that, if recognized, would favorably impact the effective rate was $3.2 million. During the next 12 months, it is reasonably possible that resolution of reviews by taxing authorities, both domestic and international, could be reached with respect to approximately $3.0 million of the net unrecognized tax benefits depending on the timing of examinations and expiration of statute of limitations, either because our tax positions are sustained or because we agree to their disallowance and pay the related income tax.

We are subject to ongoing audits from various taxing authorities in the jurisdictions in which we do business. As of June 30, 2017, the years open under the statute of limitations in significant jurisdictions include fiscal years 2012-2016 in the U.S. We believe we have adequately provided for uncertain tax issues that have not yet been resolved with federal, state and foreign tax authorities.

During the three month period ended March 31, 2017, in order to maintain the required leverage ratio in our revolving credit agreement and note purchase and private shelf agreements, we decided to access cash resources in our foreign subsidiaries to provide increased assurance of compliance with our loan covenants in the future. As a result, we are no longer able to assert that accumulated or current earnings in our foreign subsidiaries are indefinitely reinvested. Our intent is to repatriate a total of approximately $194.2 million of earnings from the U.K. during fiscal 2017, and we have provided for the associated incremental U.S. taxes. As of June 30, 2017, we have recorded a deferred tax liability in the amount of $17.8 million for the estimated U.S. taxes that would be due if we were to repatriate the remainder of the accumulated or current earnings in foreign subsidiaries. We do not have plans to repatriate any additional amounts at this time, however, we may do so if circumstances change or we determine it is in the company's best interests to do so.

We evaluated our net deferred income taxes, which included an assessment of the cumulative income or loss over the prior-three year period and future periods, to determine if a valuation allowance is required. After considering our recent history of U.S. losses, we recorded a valuation allowance during fiscal year 2015 on net U.S. deferred tax assets, with a corresponding charge to its income tax provision of $35.8 million. As of June 30, 2017, we maintained a valuation allowance against U.S. deferred tax assets as realization of such assets does not meet the more-likely-than-not threshold required under accounting guidelines. We will continue to assess the need for a valuation allowance on deferred tax assets by evaluating positive and negative evidence that may exist. Through June

30, 2017, a total valuation allowance of $45.6 million has been established for U.S. net deferred tax assets, certain foreign operating losses and other foreign assets.

If sufficient positive evidence arises in the future, such as a sustained return to profitability in the U.S., any existing valuation allowance could be reversed as appropriate, decreasing income tax expense in the period that such conclusion is reached. Until we re-establish a pattern of continuing profitability in the U.S. tax jurisdiction, in accordance with the applicable accounting guidance, U.S. income tax expense or benefit related to the recognition of deferred tax assets in the condensed consolidated statement of operations for future periods will be offset by decreases or increases in the valuation allowance with no net effect on the Consolidated Condensed Statements of Income (Loss).

Note 11 — Derivative Instruments and Hedging Activities

In order to manage our exposure to fluctuations in interest and foreign currency exchange rates we utilize derivative financial instruments such as forward starting swaps and foreign currency forwards for periods typically up to three years. We do not use any derivative financial instruments for trading or other speculative purposes.

Table of Contents

All derivatives are recorded at fair value, however, the classification of gains and losses resulting from changes in the fair values of derivatives are dependent on the intended use of the derivative and its resulting designation. If a derivative is designated as a fair value hedge, then a change in the fair value of the derivative is offset against the change in the fair value of the underlying hedged item and only the ineffective portion of the hedge, if any, is recognized in earnings. If a derivative is designated as a cash flow hedge, then the effective portion of a change in the fair value of the derivative is recognized as a component of accumulated other comprehensive loss until the underlying hedged item is recognized in earnings, or the forecasted transaction is no longer probable of occurring. If a derivative does not qualify as a highly effective hedge, any change in fair value is immediately recognized in earnings. We formally document all hedging relationships for all derivative hedges and the underlying hedged items, as well as the risk management objectives and strategies for undertaking the hedge transactions. We classify the fair value of all derivative contracts as current or non-current assets or liabilities, depending on the realized and unrealized gain or loss position of the hedged contract at the balance sheet date, and the timing of future cash flows. The cash flows from derivatives treated as hedges are classified in the Condensed Consolidated Statements of Cash Flows in the same category as the item being hedged.

The following table shows the notional principal amounts of our outstanding derivative instruments as of June 30, 2017 and September 30, 2016 (in thousands):

	Notional Principal	
	June 30, 2017	September 30, 2016
Instruments designated as accounting hedges:		
Foreign currency forwards	$ 158,771	$ 158,664
Instruments not designated as accounting hedges:		
Foreign currency forwards	$ 70,461	$ 115,070

Included in the amounts not designated as accounting hedges above at June 30, 2017 and September 30, 2016 are foreign currency forwards with notional principal amounts of $47.5 million and $78.4 million, respectively, that have been designed to manage exposure to foreign currency exchange risks, and for which the gains or losses of the changes in fair value of the forwards has approximately offset an equal and opposite amount of gains or losses related to the foreign currency exposure. Unrealized gains of $10.2 million and $8.2 million were recognized in other income (expense), net for the three and nine months ended June 30, 2017, respectively, and an unrealized gain and unrealized loss of $1.1 million and $8.5 million were recognized in other income (expense), net for the three and nine months ended June 30, 2016, respectively, related to foreign currency forwards not designated as accounting hedges.

The notional principal amounts for outstanding derivative instruments provide one measure of the transaction volume outstanding and do not represent the amount of the Company’s exposure to credit or market loss. Credit risk represents the Company’s gross exposure to potential accounting loss on derivative instruments that are outstanding or unsettled if all counterparties failed to perform according to the terms of the contract, based on then-current interest or currency exchange rates at each respective date. The Company’s exposure to credit loss and market risk will vary over time as a function of interest and currency exchange rates. The amount of credit risk from derivative instruments and hedging activities was not material for the periods ended June 30, 2017 and September 30, 2016. Although the table above reflects the notional principal amounts of the Company’s foreign exchange instruments, it does not reflect the gains or losses associated with the exposures and transactions that the foreign exchange instruments are intended to hedge. The amounts ultimately realized upon settlement of these financial instruments, together with the gains and losses on the underlying exposures, will depend on actual market conditions during the remaining life of the instruments.

We generally enter into master netting arrangements, which reduce credit risk by permitting net settlement of transactions with the same counterparty. We presents our derivative assets and derivative liabilities at their gross fair values. We did not have any derivative instruments with credit-risk related contingent features that would require us to post collateral as of June 30, 2017 or September 30, 2016.

Table of Contents

The table below presents the fair value of our derivative financial instruments that qualify for hedge accounting as well as their classification in the Condensed Consolidated Balance Sheets as of June 30, 2017 and September 30, 2016 (in thousands):

	Balance Sheet Location	Fair Value June 30, 2017	September 30, 2016
Asset derivatives:			
Foreign currency forwards	Other current assets	$ 2,459	$ 14,769
Foreign currency forwards	Other noncurrent assets	846	1,201
		$ 3,305	$ 15,970
Liability derivatives:			
Foreign currency forwards	Other current liabilities	$ 3,096	$ 13,752
Foreign currency forwards	Other noncurrent liabilities	846	1,333
Total		$ 3,942	$ 15,085

The tables below present gains and losses recognized in other comprehensive loss for the three and nine months ended June 30, 2017 and 2016 related to derivative financial instruments designated as cash flow hedges, as well as the amount of gains and losses reclassified into earnings during those periods (in thousands):

	Nine Months Ended June 30, 2017		June 30, 2016	
Derivative Type	Gains (losses) recognized in OCI	Gains (losses) reclassified into earnings - Effective Portion	Gains (losses) recognized in OCI	Gains (losses) reclassified into earnings - Effective Portion
Foreign currency forwards	$ (1,912)	$ 1,853	$ 917	$ 1,336

	Three Months Ended June 30, 2017		June 30, 2016	
Derivative Type	Gains (losses) recognized in OCI	Gains (losses) reclassified into earnings - Effective Portion	Gains (losses) recognized in OCI	Gains (losses) reclassified into earnings - Effective Portion
Foreign currency forwards	$ (281)	$ (355)	$ 500	$ 453

The amount of gains and losses from derivative instruments and hedging activities classified as not highly effective did not have a material impact on the results of operations for the three and nine months ended June 30, 2017 and 2016. The amount of estimated unrealized net losses from cash flow hedges which are expected to be reclassified to earnings in the next twelve months is $0.4 million, net of income taxes.

Table of Contents

Note 12 — Segment Information

Our company is aligned in three operating segments, which are also our reportable segments: Cubic Transportation Systems (CTS), Cubic Global Defense Systems (CGD Systems), and Cubic Global Defense Services (CGD Services). We define our operating segments and reportable segments based on the way our chief executive officer manages the operations of the Company for purposes of allocating resources and assessing performance and we continually reassess our operating segment and reportable segment designation based upon these criteria. In 2016 we formalized the structure of our Cubic Mission Solutions (CMS) business unit within our CGD Systems operating segment. CMS combines and integrates our command, control, communications, computers, intelligence, surveillance and reconnaissance (C4ISR) and secure communications operations. Following the formalization of the structure of our CMS business, our chief executive officer began receiving reports of our business activities in multiple different formats and began to use the results of the CMS business activities for certain aspects of resource allocation decisions and performance assessments. However, based upon our June 30, 2017 assessment of our operating segments and reportable segments we have concluded based upon factors such as the nature of the business activities and customers, and the nature of information presented to our Board of Directors that CMS is not an operating segment. As our CMS business unit continues to grow and mature, additional aspects of resource allocation and performance assessment may be made at the CMS level and it is possible that CMS could become an operating segment in the future.

Business segment financial data is as follows (in millions):

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
Sales:				
Cubic Transportation Systems	$ 407.9	$ 430.5	$ 136.4	$ 156.0
Cubic Global Defense Systems	350.7	331.3	129.8	119.0
Cubic Global Defense Services	281.7	293.3	95.7	100.2
Total sales	$ 1,040.3	$ 1,055.1	$ 361.9	$ 375.2
Operating income (loss):				
Cubic Transportation Systems	$ 16.6	$ 43.9	$ (0.9)	$ 20.5
Cubic Global Defense Systems	4.0	(23.7)	8.9	0.9
Cubic Global Defense Services	4.8	9.3	3.2	4.8
Unallocated corporate expenses	(33.3)	(32.8)	(12.9)	(12.3)
Total operating income (loss)	$ (7.9)	$ (3.3)	$ (1.7)	$ 13.9
Depreciation and amortization:				
Cubic Transportation Systems	$ 6.8	$ 5.4	$ 2.4	$ 1.2
Cubic Global Defense Systems	24.2	19.7	7.7	8.7
Cubic Global Defense Services	2.4	4.8	0.7	1.8

Corporate	4.8	2.0	1.7	1.3
Total depreciation and amortization	$ 38.2	$ 31.9	$ 12.5	$ 13.0

Unallocated corporate costs in the third quarter of 2017 include costs of strategic and IT system resource planning as part of our One Cubic Initiatives, which totaled $8.9 million compared to $8.5 million in the third quarter of last year. Unallocated corporate costs included $23.6 million of costs incurred in the first nine months of 2017 for strategic and IT system resource planning compared to $24.4 million in the first nine months of last year.

Changes in estimates on contracts for which revenue is recognized using the cost-to-cost-percentage-of-completion method increased operating income by $6.1 million and decreased operating income by $1.2 million for the three and nine months ended June 30, 2017, respectively, and increased operating income by $0.2 million and decreased operating income by $3.1 million for the three and nine months ended June 30, 2016, respectively.

These adjustments decreased our net loss by $3.2 million ($0.12 per share) and increased our net loss by $1.0 million ($0.04 per share) for the three and nine months ended June 30, 2017, respectively, and increased net income by $0.1

million (no impact to diluted shares) and decreased net income by $1.8 million ($0.07 per share) for the three and nine months ended June 30, 2016, respectively.

In June 2017, funding was approved on an $8.0 million equitable contract adjustment for our littoral combat ship virtual training contract with the U.S. Navy. As such, we recognized $8.0 million in sales and operating profit related to such contract adjustment during the quarter ended June 30, 2017 within our CGD Systems segment.

Note 13 — Legal Matters

In October 2014, a lawsuit was filed in the United States District Court, Northern District of Illinois against us and one of our transit customers alleging infringement of various patents held by the plaintiff, seeking judgment that we have infringed on plaintiff's patents; regular and treble damages; requiring an accounting of sales, profits, royalties and damages owed plaintiffs; pre and post judgment interest; an award of costs, fees and expenses, an injunction prohibiting the continuing infringement of the patents; and any other relief the court deems just and equitable. We are vigorously defending the lawsuit. We are also undertaking defense of our customer in this matter pursuant to our contractual obligations to that customer. The court made several rulings in our favor concerning the validity of the plaintiff's patents at issue. Plaintiff has appealed those rulings and they are now on appeal. We await the appellate court's ruling on those issues. Due to the uncertain status of this case, we cannot estimate the probability of loss or any range of estimate of possible loss.

We are not a party to any other material pending proceedings and we consider all other matters to be ordinary proceedings incidental to our business. We believe the outcome of these other proceedings will not have a materially adverse effect on our financial position, results of operations, or cash flows.

Table of Contents

CUBIC CORPORATION

ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL

CONDITION AND RESULTS OF OPERATIONS

June 30, 2017

We are a global provider of cost-effective systems and solutions that address the global transportation and defense markets' most pressing and demanding requirements. We are engaged in the design, development, manufacture, integration, and sustainment of advanced technology systems and products. We also provide a broad range of engineering, training, technical, logistic, and information technology services. We serve the needs of various federal and regional government agencies in the U.S. and other allied nations around the world with products and services that have both defense and civil applications. Our main areas of focus are in transportation payment and information systems, defense, intelligence, homeland security, and information technology, including cyber security.

We operate in three reportable business segments: Cubic Transportation Systems (CTS), Cubic Global Defense Systems (CGD Systems), and Cubic Global Defense Services (CGD Services). All of our business segments share a common mission of providing situational awareness to create enhanced value for our customers worldwide. Our defense customers benefit from increased readiness and robust connectivity, while our transportation customers benefit from enhanced efficiency and reduced congestion. We organize our business segments based on the nature of the products and services offered.

CTS is a systems integrator of payment and information technology and services for intelligent travel solutions. We deliver integrated systems for transportation and traffic management, delivering tools for travelers to choose the smartest and easiest way to travel and pay for their journeys, and enabling transportation authorities and agencies to manage demand across the entire transportation network — all in real time. We offer fare collection and revenue management devices, software, systems and multiagency, multimodal integration technologies, as well as a full suite of operational services that help agencies and operators efficiently collect fares and revenue, manage operations, reduce revenue leakage and make transportation more convenient. Through our NextBus and Intelligent Transport Management Solutions (ITMS) businesses, respectively, we also deliver real-time passenger information systems for tracking and predicting vehicle arrival times and we are a leading provider of urban and inter-urban intelligent transportation and enforcement solutions and technology and infrastructure maintenance services to U.K. and other international city, regional and national road and transportation agencies. Through our Urban Insights business we use big data and predictive analytics technology and a consulting model to help the transportation industry improve operations, reduce costs and better serve travelers.

CGD Systems is focused on two primary lines of business: training systems and secure communications products. CGD Systems is a diversified supplier of live and virtual military training systems, and secure communication systems and products to the U.S. Department of Defense, other U.S. government agencies and allied nations. Our training systems business manufactures instrumented range systems for fighter aircraft, armored vehicles and infantry force-on-force live training weapons effects simulations, laser-based tactical and communication systems, and precision gunnery solutions. Our secure communications products are aimed at intelligence, surveillance, ground combat, and search and rescue markets. In 2016 we formalized the structure of our Cubic Mission Solutions (CMS) business unit which combines and integrates our command, control, communications, computers, intelligence, surveillance and reconnaissance (C4ISR) and secure communications operations. CMS' C4ISR solutions provide information capture, assessment, exploitation and dissemination in a secure network-centric environment.

CGD Services is a leading provider of highly specialized military, security force and intelligence support services to the U.S. government and allied nations. Services provided include live, virtual and constructive training, real-world mission rehearsal exercises, professional military education, intelligence support, information technology, information assurance and related cyber support, development of military doctrine, consequence management, infrastructure protection and force protection, as well as support to field operations, and logistics.

Consolidated Overview

Sales for the quarter ended June 30, 2017 decreased 4% to $361.9 million from $375.2 million in the third quarter of last year. Sales from CTS and CGD Services decreased by 13% and 4%, respectively, for the quarter while sales from CGD Systems increased by 9% for the quarter. For the first nine months of the fiscal year, consolidated sales decreased by 1% to $1.040 billion compared to $1.055 billion last year. CTS and CGD Services sales decreased 5% and 4%, respectively,

Table of Contents

for the first nine months of fiscal 2017, partially offset by increases in CGD Systems sales of 6%. The average exchange rates between the prevailing currency in our foreign operations and the U.S. dollar had a negative impact on sales of $5.4 million for the third quarter and $20.3 million for the nine-month period compared to the same periods last year. Sales generated by businesses we acquired during 2017 and 2016 totaled $28.4 million and $69.2 million for the three- and nine-month periods ended June 30, 2017, respectively, compared to $14.3 million and $28.0 million for the three- and nine-month periods ended June 30, 2016, respectively. See the segment discussions following for further analysis of segment sales.

Our consolidated operating loss was $1.7 million in the third quarter of fiscal 2017 compared to operating income of $13.9 million in the third quarter of last year. CTS had an operating loss of $0.9 million in the third quarter of fiscal 2017 compared to operating income of $20.5 million in the third quarter last year. For the third quarter of fiscal 2017, CGD Services operating income decreased 33% compared to same period last year. CGD Systems had operating income of $8.9 million for the third quarter of fiscal 2017 compared to $0.9 million for the third quarter last year. Unallocated corporate and other costs for the third quarter of 2017 were $12.9 million compared to $12.3 million in 2016. The increase in unallocated corporate costs includes an increase in costs incurred in the third quarter of 2017 for strategic and IT system resource planning as part of our One Cubic Initiatives, which totaled $8.9 million in the third quarter of fiscal 2017 compared to $8.5 million in the third quarter of last year. The average exchange rates between the prevailing currency in our foreign operations and the U.S. had no significant impact on our quarterly operating results. See the segment discussions following for further analysis of segment operating income (loss).

For the nine months ended June 30, 2017, CTS and CGD Services operating income decreased 62% and 48%, respectively, compared to the first nine months of last fiscal year. CGD Systems had operating income of $4.0 million for the nine months ended June 30, 2017 compared to an operating loss of $23.7 million for the nine months ended June 30, 2016. In the first nine months of fiscal 2016, CGD Systems operating results were significantly affected by the impact of accounting for businesses acquired. Businesses we acquired in 2017 and 2016, which were all within our CGD Systems segment, generated an operating loss of $6.5 million for the nine months ended June 30, 2017 compared to an operating loss of $26.8 million for the nine months ended June 30, 2016. Included in the operating loss for the first nine months of fiscal year 2016 are business acquisition transaction costs of $27.0 million. These operating losses for acquired businesses include acquisition transaction costs and other acquisition-related charges, including an $18.5 million charge incurred for the GATR acquisition in the second quarter of fiscal 2016 described in the CGD Systems segment section below. Unallocated corporate and other costs for the nine-month period of 2017 were $33.0 million compared to $32.8 million in 2016. Unallocated corporate costs included $23.6 million of costs incurred in the first nine months of 2017 for strategic and IT system resource planning compared to $24.4 million in the first nine months of last year. The average exchange rates between the prevailing currency in our foreign operations and the U.S. dollar resulted in a decrease in operating income of $2.1 million for the nine-month period compared to the same period last year.

Our net loss for the third quarter of fiscal 2017 was $22.0 million, or 81 cents per share, compared to net income of $4.5 million, or 17 cents per share last year. This decrease in net income was primarily caused by change in the effective tax rate between quarters. Income tax expense recognized on pre-tax losses for the three and nine months ended June 30, 2017 resulted in effective tax rates of (430%) and (31%), respectively. The most significant items contributing to the difference between the statutory U.S. federal income tax rate of 35% and the Company’s effective tax rate for the three-month and nine-month periods ending June 30, 2017 were the impact of recording the U.S.

provision utilizing a discrete vs. annualized effective tax rate method partially offset by the tax benefit related to the reversal of certain tax contingencies due to the lapse of the statute of limitations. After considering the impact of the U.S. valuation allowance, we have determined that a reliable estimate of the annual effective tax rate for fiscal year 2017 cannot be made, since relatively small changes in our projected income produce a significant variation in our effective tax rate. Interest expense for the third quarter of fiscal 2017 increased to $4.4 million, compared to $3.5 million in the third quarter of last year. The increased interest expense was primarily caused by our higher average outstanding debt.

For the first nine months of fiscal 2017, our net loss was $24.4 million, or 90 cents per share, compared to net income of $9.2 million, or 34 cents per share last year. The change for the nine-month period was primarily due to the impact of the tax matters described above. Interest expense increased to $12.2 million for the first nine months of fiscal 2017 from $7.4 million for same period last year primarily due to the increase in outstanding debt.

Our gross margin percentage on product sales decreased to 28% in the third quarter of 2017 from 36% in the third quarter last year, and increased to 28% for the first nine months of fiscal 2017 compared to 27% for the first nine months of last year. Our gross margin percentage on product sales in the third quarter of fiscal 2016 was higher than our historical average primarily due to operating income recognized on a contract in Sydney. In the third quarter of fiscal

Table of Contents

2016, we had finalized negotiations regarding scope and pricing with a customer in Sydney for system development work that the customer directed us to begin in the second quarter of fiscal 2015. We had inventoried costs and deferred revenue on this development work until such negotiations were complete. As a result of the finalization of the scoping and pricing, we realized increased sales and operating profits in the third quarter of fiscal 2016. For the first nine months of fiscal 2016, these high margins in the third quarter of fiscal 2016 were partially offset by cost growth on sales of ground combat training systems in the Far East that we experienced in the first nine months of fiscal 2016.

Our gross margin percentage on service sales was 19% in the third quarter of 2017 compared to 20% in the third quarter of fiscal 2016. The decrease in gross margins on service sales was primarily in our CTS segment. Our gross margin percentage on service sales was 19% in the first nine months of 2017 compared to 21% in the first nine months of fiscal 2016. For two CTS fare system service contracts in North America, gross margins in the first half of fiscal 2016 were higher than in the first half of 2017 due to gains recognized in the second quarter of fiscal 2016 upon clarification of certain service level requirements in the contracts. Revenue had been deferred for these two contracts until these contractual clarifications were finalized in the second quarter of fiscal 2016.

Selling, general and administrative (SG&A) expenses decreased in the third quarter of 2017 to $60.1 million compared to $68.6 million in 2016. For the nine-month period, SG&A expenses decreased to $183.2 million compared to $206.9 million last year. As a percentage of sales, SG&A expenses were 17% for the third quarter and 18% for the nine-month period ended June 30, 2017, compared to 18% for the third quarter and 20% for the nine-month period ended June 30, 2016. The decrease in SG&A expenses for the quarter is primarily due to decreases in costs for strategic and IT system resource planning. The decrease in SG&A expenses for the first nine months of the fiscal year is primarily due to significant SG&A expenses incurred in the first nine months of fiscal 2016 in connection with business acquisitions, including the $18.5 million of expense noted above that was recognized in the second quarter of fiscal 2016 in connection with the GATR acquisition.

Company funded research and development (R&D) expenditures, which relate to new defense and transportation technologies under development, increased to $16.9 million for the third quarter compared to $8.5 million last year, and increased to $38.8 million for the nine-month period this year compared to $18.1 million last year. For the third quarter and first nine months of fiscal 2016, R&D expenditures increased for both CTS and CGD Systems; the rate of acceleration of R&D expenditures compared to last year was higher for CTS than for CGD Systems. In the third quarter and first nine months of fiscal 2017, CTS R&D costs included $3.0 million and $6.4 million, respectively, for the development of technologies that will be used on a major transportation contract that is expected to be awarded later in fiscal 2017. CTS also accelerated R&D activities on mobile device and next generation NextBus technologies. CGD accelerated the development of innovative ground live and virtual training technologies.

Amortization of purchased intangibles for the third quarter of 2017 decreased to $7.9 million from $9.7 million in 2017 due to reduction in amortization for intangible assets that are amortized using accelerated methods. Amortization of purchased intangibles for the first nine months of 2017 increased to $25.1 million from $24.6 million in 2016. Intangibles related to businesses acquired in early fiscal 2016 were amortized for the full nine months in the first half of fiscal 2017; however, these intangible assets were only amortized for the period subsequent to the acquisition of the related business in fiscal 2016.

Cubic Transportation Systems Segment (CTS)

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
	(in millions)			
Transportation Systems Segment Sales	$ 407.9	$ 430.5	$ 136.4	$ 156.0
Transportation Systems Segment Operating Income (Loss)	$ 16.6	$ 43.9	$ (0.9)	$ 20.5

CTS sales decreased 13% in the third quarter of fiscal 2017 to $136.4 million compared to $156.0 million in the third quarter of last year, and decreased 5% for the first nine months of fiscal 2017 to $407.9 million from $430.5 million last year. Sales for the third quarter and first nine months of fiscal 2017 decreased for North America and the U.K. as

Table of Contents

compared to the corresponding periods in fiscal 2016. Sales were lower in Australia for the third quarter of fiscal 2017 compared to the third quarter of last year, but were higher for the first nine months of this year compared to the first nine months of 2016.

Foreign currency exchange rates had a significant impact on the comparability of CTS sales between the periods. The average exchange rates between the prevailing currency in our foreign operations and the U.S. dollar resulted in a decrease in sales of $5.7 million for the third quarter of fiscal 2017 and $21.6 million for the first nine months of fiscal 2017 compared to the same periods last year, primarily due to the weakening of the British Pound against the U.S. dollar. Absent the impact of exchange rates, sales were relatively flat in the U.K. for the third quarter and first nine months of fiscal 2017. Sales in North America decreased for the third quarter and first nine months of fiscal 2017 due primarily to the reduction of development work on our contract in Vancouver between 2016 and 2017. Development work on this contract is scheduled to decrease over time as the contract progresses. Sales in Australia decreased for the third quarter of fiscal 2017 compared to the third quarter of last fiscal year. In the third quarter of fiscal 2016, we had finalized negotiations regarding scope and pricing with a customer in Sydney for system development work that the customer directed us to begin in the second quarter of fiscal 2015. We had inventoried costs and deferred revenue on this development work until such negotiations were complete. As a result of the finalization of the scoping and pricing, we realized increased sales and operating profits in the third quarter of fiscal 2016. Sales for Australia for the first nine months of fiscal 2017 were higher than for the first nine months of fiscal 2016 primarily due to an increase of work in this region as well as the formalization and recognition of additional system development and services work for our Sydney customer noted above in the first and second quarters of fiscal 2017.

CTS had an operating loss of $0.9 million in the third quarter of fiscal 2017 compared to operating income of $20.5 million in the third quarter of last year. Operating income decreased 62% for the first nine months of fiscal 2017 to $16.6 million from $43.9 million for the first nine months of last year. Operating income for the third quarter and first nine months of fiscal 2017 decreased for North America and the U.K. as compared to the corresponding periods in fiscal 2016. Australian operating income decreased for the third quarter of fiscal 2017 but increased for the first nine months of fiscal 2017 as compared to the corresponding periods last year.

The average exchange rates between the prevailing currency in our foreign operations and the U.S. dollar resulted in a decrease in operating income of $0.2 million for the third quarter and $2.7 million for the nine-month period compared to the same periods last year. Operating income for the third quarter and first nine months of fiscal 2017 decreased for the U.K. due to cost increases on a service contract in the U.K. and decreased on a lower volume of system development work in fiscal 2017 as compared to the amount of work performed in fiscal 2016. Operating income for the third quarter and first nine months of fiscal 2017 decreased for North American contracts primarily due to an increase in estimated costs on a toll contract.

The decrease in the Australian operating income for the third quarter of fiscal 2017 compared to the third quarter of last fiscal year and the increase in Australian operating income for the first nine months of fiscal 2017 compared to the first nine months of last year are primarily due to the matter noted above regarding the finalization of scoping and pricing of work in the third quarter of fiscal 2016 and the matter noted above regarding the formalization of agreements with our Sydney customer in the first two quarters of fiscal 2017 and resulting recognition of incremental sales and operating income.

In addition, CTS operating income decreased due to increases in R&D expenditures related primarily to the development of next generation fare collection, mobile and NextBus technologies. The increases in R&D expenditures totaled $5.6 million and $12.4 million for the third quarter of fiscal 2017 and the first nine months of fiscal 2017, respectively, compared to corresponding periods in fiscal 2016. In the third quarter and first nine months of fiscal 2017 CTS incurred $3.0 million and $6.4 million, respectively, of R&D costs for the development of technologies that will be used on a major transportation contract that is expected to be awarded later in fiscal 2017.

Table of Contents

Cubic Global Defense Systems Segment (CGD Systems)

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
	(in millions)			
Cubic Global Defense Systems Segment Sales	$ 350.7	$ 331.3	$ 129.8	$ 119.0
Cubic Global Defense Systems Segment Operating Income (Loss)	$ 4.0	$ (23.7)	$ 8.9	$ 0.9

CGD Systems sales increased 9% in the third quarter to $129.8 million compared to $119.0 million last year, and sales increased 6% for the first nine months of fiscal 2017 to $350.7 million from $331.3 million last year due primarily to sales from acquired businesses. Revenues from businesses we acquired in fiscal years 2017 and 2016, all within our CGD Systems operating segment, were $28.4 million and $69.2 million for the three- and nine-month periods ended June 30, 2017, respectively, compared to $14.3 million and $28.0 million for the three- and nine-month periods ended June 30, 2016, respectively.

In June 2017, funding was approved on an $8.0 million equitable contract adjustment for our littoral combat ship virtual training contract with the U.S. Navy. As such, we recognized $8.0 million in sales and operating profit related to such contract adjustment during the quarter ended June 30, 2017. Sales were higher for the third quarter and first nine months of fiscal 2017 for secure communications products, but were lower for immersive training systems. Sales of ground combat training systems were relatively flat for the third quarter and first nine months of fiscal 2017. Sales of air combat training systems were lower for the third quarter of fiscal 2017 compared to the third quarter of last year, but were higher for the first nine months of the year.

The average exchange rates between the prevailing currency in our foreign operations and the U.S. dollar resulted in an increase in sales of $0.2 million for the third quarter of 2017 and $1.2 million for the nine-month period ended June 30, 2017 compared to the same periods last year.

CGD Systems operating income was $8.9 million in the third quarter of fiscal 2017 compared to operating income of $0.9 million last year. As noted above, CGD Systems recognized a gain of $8.0 million due to the approval of a contract adjustment with the U.S. Navy in the third quarter of fiscal 2017.

The change in CGD Systems operating results were also significantly influenced by the impacts of accounting for business acquisitions in fiscal 2016 and 2017. Including the impacts of business acquisition accounting and amortization expense, the businesses we acquired in fiscal years 2017 and 2016 had operating income of $0.9 million for the third quarter of fiscal 2017 compared to operating losses of $4.1 million in the third quarter of fiscal 2016. Acquired businesses incurred operating losses of $6.5 million in the first nine months of 2017 compared to $26.8 million in the first nine months of 2016. Included in the operating loss for the first nine months of fiscal year 2016 are business acquisition transaction costs of $27.0 million. Business acquisition transaction costs consist of expenses incurred for retention bonus expenses, due diligence and consulting costs incurred in connection with the acquisitions, expenses recognized related to the change in the fair value of contingent consideration for acquisitions, and, most significantly, expenses recognized in connection with our acquisition of GATR. GATR’s operating income for the nine months ended June 30, 2016 was significantly impacted by the GAAP accounting requirements regarding business combinations. Prior to our acquisition of GATR, GATR had a number of share-based payment awards in place to its employees. Due to the structure of certain of these share-based payment awards, we were required to recognize compensation expense, rather than purchase consideration, for the portion of our purchase price that we paid to the seller that was distributed to the recipients of these awards. Consequently, we recognized $18.5 million of compensation expense during the quarter ended March 31, 2016 related to this matter upon completing this acquisition. Expense related to the amortization of CGD Systems intangible assets totaled $5.9 million in the third quarter of 2017 compared to $7.0 million in the third quarter last year, and totaled $18.6 million in the first nine months of fiscal 2017 compared to $15.4 million in the first nine months of 2016. In addition, CGD Systems increased R&D expenditures related primarily to the development of innovative ground live and virtual training technologies of $2.7 million and $8.3 million for the third quarter of fiscal 2017 and the first nine months of fiscal 2017, respectively, compared to corresponding periods in fiscal 2016.

In addition to the impacts of acquired businesses described above, operating income for the third quarter and first nine months of fiscal 2017 were increased by improved operating results on higher sales of secure communications products.

Table of Contents

Operating income on ground combat training sales was relatively consistent between the third quarter of fiscal 2017 and the third quarter of fiscal 2016. However, operating income on ground combat training systems was significantly higher in the first nine months of fiscal 2017 compared to the first nine months of last year. The operating income from ground combat training systems in the first nine months of fiscal 2016 was negatively impacted by cost growth that was recognized in the second quarter of fiscal 2016 on a ground combat training system that we were developing in the Far East. Operating income was lower in the third quarter of fiscal 2017 than the third quarter of fiscal 2016 due to lower sales during the period, but operating income for the first nine months of fiscal 2017 were higher than the first nine months of fiscal 2016 due to strong sales in the first half of fiscal 2017.

The average exchange rates between the prevailing currency in our foreign operations and the U.S. dollar resulted in an increase in operating income of $0.2 million for the third quarter of fiscal 2017 and $0.5 million for the nine-month period ended June 30, 2017 compared to the same periods last year.

Cubic Global Defense Services Segment (CGD Services)

	Nine Months Ended June 30,		Three Months Ended June 30,	
	2017	2016	2017	2016
	(in millions)			
Cubic Global Defense Services Segment Sales	$ 281.7	$ 293.3	$ 95.7	$ 100.2
Cubic Global Defense Services Segment Operating Income	$ 4.8	$ 9.3	$ 3.2	$ 4.8

CGD Services sales decreased 4% in the third quarter of fiscal 2017 to $95.7 million compared to $100.2 million last year, and 4% for the first nine months of fiscal 2017 to $281.7 million compared to $293.3 million last year. Sales for the third quarter and first nine months of fiscal 2017 were lower primarily because of decreased activity on U.S. Army contracts and special forces training work, other than our contract with the Joint Readiness Training Center (JRTC). JRTC sales were flat for the third quarter but increased 5% for the first nine months of fiscal 2017 compared to the corresponding period in fiscal 2016 due to increase in the number of training exercises.

CGD Services operating income was $3.2 million in the third quarter of fiscal 2017 compared to $4.8 million last year, and $4.8 million for the nine-month period compared to $9.3 million last year. The decrease in operating income was primarily driven by the decreased activity on the U.S. Army and Special Operations Forces training contracts noted above. In addition, certain contracts that we retained after recompete were won in the first quarter of fiscal 2017 at reduced pricing due to an extremely competitive bid environment. These reductions in operating profit were partially offset by a decrease in the amortization expense on purchased intangible assets which are amortized based upon accelerated methods.

Table of Contents

Backlog

	June 30, 2017	September 30, 2016
	(in millions)	
Total backlog		
Transportation Systems	$ 1,693.8	$ 1,793.3
Cubic Global Defense Systems	479.8	576.8
Cubic Global Defense Services	458.3	570.3
Total	$ 2,631.9	$ 2,940.4
Funded backlog		
Transportation Systems	$ 1,693.8	$ 1,793.3
Cubic Global Defense Systems	479.8	576.8
Cubic Global Defense Services	112.5	139.2
Total	$ 2,286.1	$ 2,509.3

Total backlog decreased by $308.5 million from September 30, 2016 to June 30, 2017 as sales outpaced new business orders for all three business segments in the third quarter of fiscal 2017. Backlog for CTS in particular can be subject to significant variations over time due to the significant size of larger customer procurements and the inconsistent frequency of such large contract opportunities. Changes in exchange rates between the prevailing currency in our foreign operations and the U.S. dollar as of the end of the quarter increased backlog by $4.2 million compared to September 30, 2016.

The difference between total backlog and funded backlog represents options under multiyear CGD Services contracts. Funding for these contracts comes from annual operating budgets of the U.S. government and the options are normally exercised annually. Funded backlog includes unfilled firm orders for our products and services for which funding has been both authorized and appropriated by the customer (Congress, in the case of U.S. government agencies). Options for the purchase of additional systems or equipment are not included in backlog until exercised. In addition to the amounts identified above, we have been selected as a participant in or, in some cases, the sole contractor for several substantial indefinite delivery/indefinite quantity (ID/IQ) contracts. ID/IQ contracts are not included in backlog until an order is received. In the past, many of the contracts we were awarded in CGD Services were long-term in nature, spanning periods of five to ten years. The U.S. Department of Defense now awards shorter-term contracts for the services we provide and increasingly relies upon ID/IQ contracts which can result in a lower backlog and/or lower funded backlog due to the shorter-term nature of Task Orders issued under these ID/IQ awards. We also have several service contracts in our transportation business that include contingent revenue provisions tied to meeting certain performance criteria. These variable revenues are also not included in the amounts identified above.

Liquidity and Capital Resources

Operating activities used cash of $16.5 million for the nine-month period ended June 30, 2017.

As a part of our efforts to upgrade our current information systems, early in fiscal 2015 we began the process of designing and implementing new enterprise resource planning (ERP) software and other software applications to manage our operations. Certain costs incurred in the development of internal-use software and software applications, including external direct costs of materials and services and applicable compensation costs of employees devoted to specific software development, are capitalized as computer software costs. Costs incurred outside of the application development stage, or that do not meet the capitalization requirements, are expensed as incurred. Cash used in connection with ERP design and development totaled $27.3 million in the first nine months of fiscal 2017. Of this amount, $15.6 million was recognized as expense and is reflected in cash flows used in operations, while $11.7 million was capitalized and is included in purchases of property, plant and equipment in investing cash flows. Investing activities for the nine-month period also included $12.9 million of cash paid related to the acquisition of businesses in our CGD Systems segment.

Financing activities for the nine-month period consisted primarily of the principal repayments of $136.0 million on short-term borrowings. We also used $0.7 million for the repurchase of common stock in connection with our stock-based compensation plan and paid dividends to shareholders of $3.7 million.

Table of Contents

A change in exchange rates between foreign currencies, primarily between the Australian dollar and the U.S. dollar and between the British Pound and the U.S. dollar, resulted in a decrease of $2.5 million to our cash balance as of June 30, 2017 compared to September 30, 2016.

In March 2013, we entered into a note purchase and private shelf agreement pursuant to which we issued $100.0 million of senior unsecured notes, bearing interest at a rate of 3.35% and maturing on March 12, 2025. In addition, pursuant to the agreement, on July 17, 2015, we issued an additional $25.0 million of senior unsecured notes bearing interest at a rate of 3.70% and maturing on March 12, 2025. Interest payments on the notes issued in 2013 and 2015 are due semi-annually and principal payments are due from 2021 through 2025. The agreement pertaining to the aforementioned notes also contained a provision that the coupon rate would increase by a further 0.50% should the company's leverage ratio exceed a certain level. On February 2, 2016, we revised the note purchase agreement and we issued an additional $75.0 million of senior unsecured notes bearing interest at 3.93% and maturing on March 12, 2026. Interest payments on these notes are due semi-annually and principal payments are due from 2020 through 2026. At the time of the issuance of this last series of notes, certain terms and conditions of the note purchase and private shelf agreement were revised in coordination with the revision and expansion of the revolving credit agreement as discussed below in order to increase our leverage capacity.

We have a committed revolving credit agreement with a group of financial institutions in the amount of $400.0 million which expires in August 2021 (Revolving Credit Agreement). At June 30, 2017, the weighted average interest rate on outstanding borrowings under the Revolving Credit Agreement was 3.48%. The available line of credit is reduced by any letters of credit issued under the Revolving Credit Agreement. As of June 30, 2017, there were borrowings totaling $104.0 million under this agreement and there were letters of credit outstanding totaling $78.7 million, which reduce the available line of credit to $217.3 million.

Until June 2017, we had a secured letter of credit facility agreement with a bank. At September 30, 2016, there were letters of credit outstanding under this agreement of $62.7 million. Restricted cash at September 30, 2016 of $69.4 million was held on deposit in the U.K. as collateral in support of this facility. In June of 2017 this agreement was terminated and the associated letters of credit were transferred to the Revolving Credit Agreement described above. The cash that formerly collateralized the secured credit facility was used to make principal payments to reduce our outstanding short-term borrowings.

Our revolving credit agreement and note purchase and private shelf agreement each contain a number of customary covenants, including requirements for us to maintain certain interest coverage and leverage ratios and restrictions on our and certain of our subsidiaries' abilities to, among other things, incur additional debt, create liens, consolidate or merge with any other entity, or transfer or sell substantially all of their assets, in each case subject to certain exceptions and limitations. The occurrence of any event of default under these agreements may result in all of the indebtedness then outstanding becoming immediately due and payable. At March 31, 2017 we did not maintain the required leverage ratio. Therefore in May 2017 certain terms and conditions of the revolving credit agreement and note purchase and private shelf agreement were further revised to allow us to maintain a higher level of leverage as of March 31, 2017 and for the remainder of the 2017 fiscal year. This revision also contains a provision that the coupon rate may increase on all of the term notes discussed above by up to 0.75% should our leverage ratio exceed certain levels.

We maintain a cash account with a bank in the United Kingdom for which the funds are restricted as to use. The account is required to secure the customer's interest in cash deposited in the account to fund our activities related to our performance under a fare collection services contract in the United Kingdom. The balance in the account as of June 30, 2017 was $4.6 million and is classified as restricted cash in our Condensed Consolidated Balance Sheets.

The terms of certain of our lending and credit agreements include provisions that require and/or limit, among other financial ratios and measurements, the permitted levels of debt, coverage of cash interest expense, and under certain circumstances, payments of dividends or other distributions to shareholders. As of June 30, 2017, these agreements restrict such distributions to shareholders to a maximum of $39.4 million in fiscal year 2017.

As of June 30, 2017, virtually all of the $84.7 million of our cash, cash equivalents, including restricted cash, and marketable securities was held by our foreign subsidiaries, primarily in the U.K., New Zealand and Australia. In light of our inability as of March 31, 2017 to maintain the required leverage ratio in our revolving credit agreement and note purchase and private shelf agreement using U.S. cash resources, in the second quarter of fiscal 2017 we decided to access our cash resources in these foreign jurisdictions to provide increased assurance of compliance with our loan

Table of Contents

covenants in the future. As a result, we are no longer able to assert that current or accumulated earnings in our foreign subsidiaries are indefinitely reinvested. Our intent is to repatriate a total of approximately $194.2 million of accumulated earnings from the U.K. in fiscal 2017, and we have provided for the associated U.S. taxes. As of June 30, 2017, we have recorded a deferred tax liability in the amount of $17.8 million for the estimated U.S. taxes that would be due if we were to repatriate the remainder of the current or accumulated earnings in our foreign subsidiaries. We do not have plans to repatriate any additional amounts at this time, however, we may do so if circumstances change or we determine it is in the company’s best interests to do so.

Our financial condition remains strong with working capital of $244.5 million and a current ratio of 1.7 to 1 at June 30, 2017. We expect that cash on hand, cash flows from operations, and our unused lines of credit will be adequate to meet our liquidity requirements for the foreseeable future.

Recent Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. ASU 2014-09 outlines a comprehensive revenue recognition model and supersedes most current revenue recognition guidance. The new guidance will require revenue to be recognized when promised goods or services are transferred to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. Adoption of the new rules could affect the timing of revenue recognition for certain transactions. Adoption of ASU 2014-09 will be required for us beginning in the first quarter of fiscal 2019 and we have determined that we will not adopt ASU 2014-09 earlier than required. ASU 2014-09 allows for two methods of adoption: (a) “full retrospective” adoption, meaning the standard is applied to all periods presented, or (b) “modified retrospective” adoption, meaning the cumulative effect of applying ASU 2014-09 is recognized as an adjustment to the opening retained earnings balance in the year of adoption. We have not yet determined which method of adoption we will select.

We have assigned a task force within management to lead our implementation efforts and we have engaged outside advisors to assist. We are currently in the process of analyzing the impact of the adoption of the new standard on our various revenue streams. Under ASU 2014-09, revenue is recognized as control transfers to the customer. As such, revenue for our fixed-price development and production contracts will generally be recognized over time as costs are incurred, which is consistent with the revenue recognition model we currently use for the majority of these contracts. For certain of our fixed-price production contracts where we currently recognize revenue as units are delivered, in most cases the accounting for those contracts will change under ASU 2014-09 such that we will recognize revenue as costs are incurred. This change will generally result in an acceleration of revenue as compared with our current revenue recognition method for those contracts. Approximately 13% of our net sales used the units-of-delivery method to recognize revenue in fiscal 2016. We continue to analyze the impact of the new standard on our remaining revenue streams and, as the standard will supersede substantially all existing revenue guidance affecting us under GAAP, we expect that it will impact revenue and cost recognition on a significant number of our contracts across our business segments, in addition to our business processes and our information technology systems. As a result, our evaluation of the effect of the new standard will continue to extend over several future periods.

In January 2016, the FASB issued Accounting Standards Update ASU 2016-01, Financial Instruments – Overall (Subtopic 825-10) which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01 will be effective for us beginning October 1, 2018 and, with the exception of a specific portion of the amendment, early adoption is not permitted. We are currently evaluating the impact this guidance will have on our financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02, Leases. Under the new guidance, leasees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (a) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and (b) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. The ASU will be effective for us beginning October 1, 2019 with early adoption permitted. ASU 2016-02 will be adopted on a modified retrospective transition basis for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

Table of Contents

In March 2016, the FASB issued ASU 2016-09, Compensation-Stock Compensation. The new guidance simplifies several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The amendments in this standard are effective for our annual year and first fiscal quarter beginning on October 1, 2017 with early adoption permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements. We do not intend to adopt the new guidance early.

In August 2016, the FASB issued ASU 2016-15, Classification of Certain Cash Receipts and Cash Payments, which provides clarifying guidance on how entities should classify certain cash receipts and cash payments on the statement of cash flows. The guidance also clarifies how the predominance principle should be applied when cash receipts and cash payments have aspects of more than one class of cash flows. The guidance will be effective for us in our fiscal year beginning October 1, 2018, and early adoption is permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In October 2016, the FASB issued ASU 2016-16, Intra-Entity Transfers of Assets Other Than Inventory, which requires an entity to recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. The guidance will be effective for us in our fiscal year beginning October 1, 2018, and early adoption is permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In November 2016, the FASB issued ASU 2016-18, Restricted Cash, which requires amounts generally described as restricted cash and restricted cash equivalents be included with cash and cash equivalents when reconciling the total beginning and ending amounts for the periods shown on the statement of cash flows. The guidance will be effective for us in our fiscal year beginning October 1, 2018, and early adoption is permitted. The adoption of this standard is anticipated to affect our presentation of restricted cash within our statement of cash flows. We are currently evaluating whether to adopt the new guidance early.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805) Clarifying the Definition of a Business. This ASU clarifies the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The definition of a business affects many areas of accounting including acquisitions, disposals, goodwill, and consolidation. The guidance will be effective for us in our fiscal year beginning October 1, 2018 and early adoption is allowed for certain transactions. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment. This standard removes the second step of the goodwill impairment test, where a determination of the fair value of individual assets and liabilities of a reporting unit was needed to measure the goodwill impairment. Under this updated standard, goodwill impairment will now be the amount by which a reporting unit’s carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. The guidance will be effective for us in our fiscal year beginning October 1, 2020 with early adoption permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

In March 2017, the FASB issued ASU 2017-07, Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The update requires employers to present the service cost component of the net periodic benefit cost in the same income statement line item as other employee compensation costs arising from services rendered during the period. The other components of net benefit cost, including interest cost, expected return on plan assets, amortization of prior service cost/credit and actuarial gain/loss, and settlement and curtailment effects, are to be presented outside of any subtotal of operating income. Employers will have to disclose the line(s) used to present the other components of net periodic benefit cost, if the components are not presented separately in the income statement. ASU 2017-07 will be effective for us beginning October 1, 2018, and early adoption is permitted. We are currently evaluating the impact of the application of this accounting standard update on our consolidated financial statements as well as whether to adopt the new guidance early.

Table of Contents

Critical Accounting Policies, Estimates and Judgments

Our financial statements are prepared in accordance with accounting principles that are generally accepted in the United States. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. We continually evaluate our estimates and judgments, the most critical of which are those related to revenue recognition, income taxes, valuation of goodwill, purchased intangibles, accounting for business combinations, and pension costs. We base our estimates and judgments on historical experience and other factors that we believe to be reasonable under the circumstances. Materially different results can occur as circumstances change and additional information becomes known.

Besides the estimates identified above that are considered critical, we make many other accounting estimates in preparing our financial statements and related disclosures. All estimates, whether or not deemed critical, affect reported amounts of assets, liabilities, revenues and expenses, as well as disclosures of contingent assets and liabilities. These estimates and judgments are also based on historical experience and other factors that are believed to be reasonable under the circumstances. Materially different results can occur as circumstances change and additional information becomes known, even for estimates and judgments that are not deemed critical.

For further information, refer to “Item 7 — Management’s Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Policies, Estimates and Judgments” and the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended September 30, 2016.

CAUTIONARY STATEMENT ABOUT FORWARD-LOOKING INFORMATION

This report, including the documents incorporated by reference herein, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that are subject to the safe harbor created by such Act. Any statements about our expectations, beliefs, plans, objectives, assumptions, future events or our future financial and/or operating performance are not historical and may be forward-looking. These statements are often, but not always, made through the use of words or phrases such as “may,” “will,” “anticipate,” “estimate,” “plan,” “project,” “conti “ongoing,” “expect,” “believe,” “intend,” “predict,” “potential,” “opportunity” and similar words or phrases or the negatives of words or phrases. These forward-looking statements involve risks, estimates, assumptions and uncertainties, including those discussed in “Part I - Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended September 30, 2016, and throughout this report that could cause actual results to differ materially from those expressed in these statements. Such risks, estimates, assumptions and uncertainties include, among others:

· unanticipated issues related to the restatement of our financial statements for fiscal years 2013 and 2012;

· our ability to monitor and evaluate the effectiveness of new processes and procedures we have implemented to remediate the material weaknesses that previously existed in our internal control over financial reporting;

· our dependence on U.S. and foreign government contracts;

· delays in approving U.S. and foreign government budgets and cuts in U.S. and foreign government defense expenditures;

· the ability of certain government agencies to unilaterally terminate or modify our contracts with them;

· the effect of sequestration on our contracts;

· our assumptions covering behavior by public transit authorities;

· our ability to successfully integrate new companies into our business and to properly assess the effects of such integration on our financial condition;

· the U.S. government's increased emphasis on awarding contracts to small businesses, and our ability to retain existing contracts or win new contracts under competitive bidding processes;

Table of Contents

· negative audits by the U.S. government;

· the effects of politics and economic conditions on negotiations and business dealings in the various countries in which we do business or intend to do business;

· competition and technology changes in the defense and transportation industries;

· the change in the way transit agencies pay for transit systems;

· our ability to accurately estimate the time and resources necessary to satisfy obligations under our contracts;

· the effect of adverse regulatory changes on our ability to sell products and services;

· our ability to identify, attract and retain qualified employees;

· our failure to properly implement our enterprise resource planning system;

· unforeseen problems with the implementation and maintenance of our information systems;

· business disruptions due to cyber security threats, physical threats, terrorist acts, acts of nature and public health crises;

· our involvement in litigation, including litigation related to patents, proprietary rights and employee misconduct;

· our reliance on subcontractors and on a limited number of third parties to manufacture and supply our products;

· our ability to comply with our development contracts and to successfully develop, introduce and sell new products, systems and services in current and future markets;

· defects in, or a lack of adequate coverage by insurance or indemnity for, our products and systems;

· changes in U.S. and foreign tax laws, exchange rates or our economic assumptions regarding our pension plans; and

· other factors discussed elsewhere in this report.

Because the risks, estimates, assumptions and uncertainties referred to above could cause actual results or outcomes to differ materially from those expressed in any forward-looking statements made by us or on our behalf, you should not place undue reliance on any forward-looking statements. In addition, past financial and/or operating performance is not necessarily a reliable indicator of future performance and you should not use our historical performance to anticipate results or future period trends. Further, any forward-looking statement speaks only as of the date on which it is made, and, except as required by law, we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and it is not possible for us to predict which factors will arise. In addition, we cannot assess the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our market risks at June 30, 2017 have not changed materially from those described under “Item 7A. Quantitative and Qualitative Disclosure about Market Risk” in our Annual Report on Form 10-K for the year ended September 30, 2016.

Table of Contents

ITEM 4 - CONTROLS AND PROCEDURES

We performed an evaluation of the effectiveness of our disclosure controls and procedures as of June 30, 2017. The evaluation was performed with the participation of senior management of each business segment and key corporate functions, and under the supervision of our Chief Executive Officer and our Chief Financial Officer. Based on our evaluation, we concluded that our disclosure controls and procedures were operating and effective as of that date.

Disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (Exchange Act) are designed to provide reasonable assurance that information required to be disclosed in reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission (SEC) and that such information is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

During the third quarter of fiscal 2016, we began the implementation of a new enterprise resource planning (ERP) system by transitioning our corporate operations, including corporate payroll, corporate general ledger, corporate procurement and payments, and corporate cash receipts functions. During the first quarter of fiscal 2017, this transition to our new ERP system continued with our North American manufacturing operations transitioning to a new material requirements planning (MRP) system and certain of our North American CGD Systems subsidiaries transitioning their payroll, general ledger, procurement, payment, billing and cash receipts functions to our new ERP system. We have accordingly in fiscal 2017 modified our existing internal controls infrastructure, as well as added other processes and internal controls, to adapt to our new ERP system as well as take advantage of the increased functionality of the new system. The transition of our remaining operations to our new ERP system will occur in phases in fiscal 2018. We believe that the new ERP system and related changes to processes and the design of our internal controls will enhance our internal control over financial reporting while providing us with the ability to scale our business. We believe we have taken the necessary steps to monitor and maintain appropriate internal control over financial reporting during the first nine months of fiscal 2017 and we will continue to evaluate the operating effectiveness of related key controls during subsequent periods.

There were no other changes in our internal control over financial reporting during the quarter ended June 30, 2017 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II - OTHER INFORMATION

ITEM 1 - LEGAL PROCEEDINGS

In October 2014, a lawsuit was filed in the United States District Court, Northern District of Illinois against us and one of our transit customers alleging infringement of various patents held by the plaintiff, seeking judgment that we have infringed on plaintiff's patents; regular and treble damages; requiring an accounting of sales, profits, royalties and damages owed plaintiffs; pre and post judgment interest; an award of costs, fees and expenses, an injunction prohibiting the continuing infringement of the patents; and any other relief the court deems just and equitable. We are vigorously defending the lawsuit. We are also undertaking defense of our customer in this matter pursuant to our contractual obligations to that customer. The court made several rulings in our favor concerning the validity of the plaintiff's patents at issue. Plaintiff has appealed those rulings and they are now on appeal. We await the appellate court's ruling on those issues. Due to the uncertain status of this case, we cannot estimate the probability of loss or any range of estimate of possible loss.

We are not a party to any other material pending proceedings and we consider all other matters to be ordinary proceedings incidental to our business. We believe the outcome of these other proceedings will not have a materially adverse effect on our financial position, results of operations, or cash flows.

ITEM 1A - RISK FACTORS

There have been no material changes to the risk factors disclosed in "Part I - Item 1A. Risk Factors" of our Annual Report on Form 10-K for the year ended September 30, 2016.

ITEM 6 - EXHIBITS

(a) The following exhibits are included herein:

Exhibit No.	Description
3.1	

	Amended and Restated Certificate of Incorporation. Incorporated by reference to Form 10-Q for the quarter ended June 30, 2006 file No. 001-08931, Exhibit 3.1.
3.2	Certificate of Amendment of Amended and Restated Certificate of Incorporation. Incorporated by reference to Form 10-Q for the quarter ended March 31, 2016, file No. 001-08931, Exhibit 3.2.
3.3	Amended and Restated Bylaws. Incorporated by reference to Form 8-K filed April 22, 2014, file No. 001-08931, Exhibit 3.1.
10.1*	Employment Transition Agreement, dated July 11, 2017, by and between Cubic Corporation and John D. Thomas.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350
101	Financial statements from the Cubic Corporation Quarterly Report on Form 10-Q for the quarter ended June 30, 2017, formatted in Extensible Business Reporting Language (XBRL): (i) Condensed Consolidated Statements of Income (Loss), (ii) Condensed Consolidated Statements of Comprehensive Income (Loss), (iii) Condensed Consolidated Balance Sheets, (iv) Condensed Consolidated Statements of Cash Flows, and (v) Notes to Condensed Consolidated Financial Statements.

*Indicates management contract or compensatory plan or arrangement.

Table of Contents

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.

	CUBIC CORPORATION
Date August 3, 2017	/s/ John D. Thomas John D. Thomas Executive Vice President and Chief Financial Officer (Principal Financial Officer)
Date August 3, 2017	/s/ Mark A. Harrison Mark A. Harrison Senior Vice President and Corporate Controller (Principal Accounting Officer)