UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended April 30, 2019
OR

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

HEALTHEQUITY, INC.

(Exact name of registrant as specified in its charter)

Delaware	**7389**	**52-2383166**
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

15 West Scenic Pointe Drive
Suite 100
Draper, Utah 84020
(Address of principal executive offices) (Zip code)

(801) 727-1000
(Registrant's telephone Number, including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	**Trading Symbol(s)**	**Name of each exchange on which registered**
Common stock, par value $0.0001 per share	HQY	The NASDAQ Global Select Market

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☑ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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. (Check one):

Large accelerated filer	☑	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☐
		Emerging growth Company	☐

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

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

As of May 31, 2019, there were 62,724,780 shares of the registrant's common stock outstanding.

HealthEquity, Inc. and subsidiaries
Form 10-Q quarterly report

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Part I. Financial information
Item 1. Financial statements

HealthEquity, Inc. and subsidiaries
Condensed consolidated balance sheets

(in thousands, except par value)		April 30, 2019		January 31, 2019
		(unaudited)		
Assets				
Current assets				
Cash and cash equivalents	$	329,310	$	361,475
Accounts receivable, net of allowance for doubtful accounts as of April 30, 2019 and January 31, 2019 of $111 and $125, respectively		27,022		25,668
Other current assets		8,244		7,534
Total current assets		364,576		394,677
Other investments		78,065		709
Property and equipment, net		8,481		8,223
Operating lease right-of-use assets		37,367		—
Intangible assets, net		81,437		79,666
Goodwill		4,651		4,651
Deferred tax asset		551		1,677
Other assets		21,511		20,413
Total assets	$	596,639	$	510,016
Liabilities and stockholders' equity				
Current liabilities				
Accounts payable	$	1,964	$	3,520
Accrued compensation		8,501		16,981
Accrued liabilities		9,127		8,552
Operating lease liabilities		3,786		—
Total current liabilities		23,378		29,053
Operating lease liabilities, non-current		36,243		—
Deferred tax liability		7,332		916
Other long-term liabilities		387		2,968
Total liabilities		67,340		32,937
Commitments and contingencies (see note 6)				
Stockholders' equity				
Preferred stock, $0.0001 par value, 100,000 shares authorized, no shares issued and outstanding as of April 30, 2019 and January 31, 2019, respectively		—		—
Common stock, $0.0001 par value, 900,000 shares authorized, 62,718 and 62,446 shares issued and outstanding as of April 30, 2019 and January 31, 2019, respectively		6		6
Additional paid-in capital		315,621		305,223
Accumulated earnings		213,672		171,850
Total stockholders' equity		529,299		477,079
Total liabilities and stockholders' equity	$	596,639	$	510,016

See accompanying notes to condensed consolidated financial statements.

HealthEquity, Inc. and subsidiaries
Condensed consolidated statements of operations and comprehensive income (unaudited)

	Three months ended April 30,	
(in thousands, except per share data)	**2019**	**2018**
Revenue:		
Service revenue	$ 26,808	$ 24,821
Custodial revenue	41,952	28,434
Interchange revenue	18,292	16,649
Total revenue	87,052	69,904
Cost of revenue:		
Service costs	20,649	18,047
Custodial costs	4,123	3,439
Interchange costs	4,527	4,062
Total cost of revenue	29,299	25,548
Gross profit	57,753	44,356
Operating expenses:		
Sales and marketing	8,970	6,860
Technology and development	10,905	7,979
General and administrative	8,709	7,507
Amortization of acquired intangible assets	1,491	1,470
Total operating expenses	30,075	23,816
Income from operations	27,678	20,540
Other income (expense), net	23,600	(1)
Income before income taxes	51,278	20,539
Income tax provision (benefit)	9,456	(2,038)
Net income and comprehensive income	$ 41,822	$ 22,577
Net income per share:		
Basic	$ 0.67	$ 0.37
Diluted	$ 0.65	$ 0.36
Weighted-average number of shares used in computing net income per share:		
Basic	62,326	61,170
Diluted	63,901	62,693

See accompanying notes to condensed consolidated financial statements.

HealthEquity, Inc. and subsidiaries
Condensed consolidated statements of stockholders' equity (unaudited)

	Three months ended April 30,	
(in thousands)	2019	2018
Total stockholders' equity, beginning balances (audited)	$ 477,079	$ 346,274
Common stock:		
Beginning balance	6	6
Issuance of common stock upon exercise of stock options, and for restricted stock	—	—
Ending balance	6	6
Additional paid-in capital:		
Beginning balance	305,223	261,237
Issuance of common stock upon exercise of stock options, and for restricted stock	4,370	10,964
Stock-based compensation	6,028	4,239
Ending balance	315,621	276,440
Accumulated comprehensive loss:		
Beginning balance	—	(269)
Cumulative effect from adoption of ASU 2016-01	—	269
Ending balance	—	—
Accumulated earnings:		
Beginning balance	171,850	85,300
Net income	41,822	22,577
Cumulative effect from adoption of ASC 606	—	13,007
Cumulative effect from adoption of ASU 2016-01	—	(356)
Ending balance	$ 213,672	$ 120,528
Total stockholders' equity, ending balances	$ 529,299	$ 396,974

See accompanying notes to condensed consolidated financial statements.

HealthEquity, Inc. and subsidiaries
Condensed consolidated statements of cash flows (unaudited)

	Three months ended April 30,	
(in thousands)	**2019**	**2018**
Cash flows from operating activities:		
Net income	$ 41,822	$ 22,577
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,773	4,520
Unrealized (gains) losses on marketable equity securities and other	(23,484)	140
Deferred taxes	7,542	1,989
Stock-based compensation	6,028	4,239
Changes in operating assets and liabilities:		
Accounts receivable	(1,354)	(1,420)
Other assets	(1,694)	(5,471)
Operating lease right-of-use assets	635	—
Accounts payable	(1,577)	87
Accrued compensation	(8,480)	(4,909)
Accrued liabilities and other current liabilities	1,769	881
Operating lease liabilities, non-current	(627)	—
Other long-term liabilities	(17)	71
Net cash provided by operating activities	25,336	22,704
Cash flows from investing activities:		
Purchases of intangible member assets	(1,262)	—
Purchases of marketable equity securities	(53,845)	(180)
Purchases of property and equipment	(1,126)	(1,121)
Purchases of software and capitalized software development costs	(5,497)	(2,097)
Net cash used in investing activities	(61,730)	(3,398)
Cash flows from financing activities:		
Proceeds from exercise of common stock options	4,229	10,167
Net cash provided by financing activities	4,229	10,167
Increase (decrease) in cash and cash equivalents	(32,165)	29,473
Beginning cash and cash equivalents	361,475	199,472
Ending cash and cash equivalents	$ 329,310	$ 228,945
Supplemental cash flow data:		
Interest expense paid in cash	$ 50	$ 50
Income taxes paid in cash, net of refunds received	(51)	39
Supplemental disclosures of non-cash investing and financing activities:		
Purchases of property and equipment included in accounts payable or accrued liabilities at period end	$ 21	$ 491
Purchases of software and capitalized software development costs included in accounts payable or accrued liabilities at period end	158	117
Exercise of common stock options receivable	141	797

See accompanying notes to condensed consolidated financial statements.

HealthEquity, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Note 1. Summary of business and significant accounting policies

HealthEquity, Inc. was incorporated in the state of Delaware on September 18, 2002. The Company offers a full range of innovative solutions for managing health care accounts (Health Savings Accounts, Health Reimbursement Arrangements, and Flexible Spending Accounts) for health plans, insurance companies, and third-party administrators.

Certain reclassifications have been made to prior year amounts to conform to the current year presentation.

Principles of consolidation

The condensed consolidated financial statements include the accounts of HealthEquity, Inc. and its wholly owned subsidiaries, HealthEquity Trust Company, HEQ Insurance Services, Inc., HealthEquity Advisors, LLC and HealthEquity Retirement Services, LLC (collectively referred to as the "Company").

The Company has a 4% ownership interest in a public company that is a leader in administering Consumer-Directed Benefits. The Company measures the investment at fair value, and all gains and losses on the investment, realized and unrealized, are recognized in other income (expense), net in the consolidated statements of operations and comprehensive income. The investment was valued at $77.4 million as of April 30, 2019 and is included in other investments on the accompanying condensed consolidated balance sheet.

The Company has a 22% ownership interest in a limited partnership for investment in and the management of early stage companies in the healthcare industry; this partnership interest is accounted for using the equity method of accounting. The investment was approximately $0.2 million as of April 30, 2019 and is included in other investments on the accompanying condensed consolidated balance sheet.

The Company has a 1% ownership interest in a limited partnership that engages in the development of technology-based financial healthcare products. The Company elected the measurement alternative for non-marketable equity investments to account for the investment. The investment was valued at $0.5 million as of April 30, 2019 and is included in other investments on the accompanying condensed consolidated balance sheet.

Acquisitions of businesses are accounted for as business combinations, and accordingly, the results of operations of acquired businesses are included in the condensed consolidated financial statements from the date of acquisition. All significant intercompany balances and transactions have been eliminated.

Basis of presentation

The accompanying condensed consolidated financial statements as of April 30, 2019 and for the three months ended April 30, 2019 and 2018 are unaudited and have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP") and the applicable rules and regulations of the Securities and Exchange Commission ("SEC") regarding interim financial reporting. In the opinion of management, the interim data includes all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results for the interim periods. Certain information and note disclosures normally included in annual financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Therefore, these condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the year ended January 31, 2019. The fiscal year-end condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by GAAP.

Significant accounting policies

There have been no material changes in the Company’s significant accounting policies, other than the additions of the policies described below for leases and investments in equity securities, as compared to the significant accounting policies described in the Company’s Annual Report on Form 10-K for the year ended January 31, 2019.

Leases. The Company determines if a contract contains a lease at inception or any modification of the contract. A contract contains a lease if the contract conveys the right to control the use of an identified asset for a specified period in exchange for consideration. Control over the use of the identified asset means the lessee has both (a) the right to obtain substantially all of the economic benefits from the use of the asset and (b) the right to direct the use of the asset.

HealthEquity, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Note 1. Summary of business and significant accounting policies (continued)

The Company has entered into various operating leases consisting of office space and data storage facilities with remaining lease terms of approximately 3 to 12 years, often with one or more Company options to renew. These renewal terms can extend the lease term from 3 to 10 years and are included in the lease term when it is reasonably certain that the Company will exercise the option. Leases with an expected term of 12 months or less at commencement are not accounted for on the balance sheet. All operating lease expense is recognized on a straight-line basis over the expected lease term. Certain leases also include obligations to pay for non-lease services, such as utilities and common area maintenance. The services are accounted for separately from lease components, and the Company allocates payments to the lease and other services components based on estimated stand-alone prices.

Operating lease right-of-use ("ROU") assets and liabilities are recognized based on the present value of future minimum lease payments over the expected lease term at commencement date. As the rate implicit in each lease is not readily determinable, management uses the Company's incremental borrowing rate based on the information available at commencement date in determining the present value of future payments. The Company used its incremental borrowing rate on February 1, 2019 for all leases that commenced prior to that date.

Operating leases are included in Operating lease right-of-use assets, Operating lease liabilities and Operating lease liabilities, non-current on the condensed consolidated balance sheets beginning February 1, 2019.

Investments. Marketable equity securities are strategic equity investments with readily determinable fair values and for which the Company does not have the ability to exercise significant influence are accounted for at fair value and are classified as other investments on the condensed consolidated balance sheets. All gains and losses on these investments, realized and unrealized, are recognized in other income (expense), net in the consolidated statements of operations and comprehensive income.

Non-marketable equity securities are strategic equity investments without readily determinable fair values and for which the Company does not have the ability to exercise significant influence are accounted for using the measurement alternative and are classified as other investments on the condensed consolidated balance sheets. All gains and losses on these investments, realized and unrealized, are recognized in other income (expense), net on the consolidated statements of operations and comprehensive income.

Equity method investments are equity securities in investees the Company does not control but over which the Company has the ability to exercise significant influence. Equity-method investments are included in other investments on the condensed consolidated balance sheets. The Company's share of the earnings or losses as reported by equity-method investees, amortization of basis differences, and related gains or losses, if any, are recognized in other income (expense), net on the consolidated statements of operations and comprehensive income.

The Company assesses whether an other-than-temporary impairment loss on equity method investments and an impairment loss on non-marketable equity securities has occurred due to declines in fair value or other market conditions. If any impairment is considered other than temporary for equity method investments or impairment is identified for non-marketable equity securities, the Company will write down the investment to its fair value and record the corresponding charge through other income (expense), net in the consolidated statements of operations and comprehensive income. See Note 3—Supplemental financial statement information for additional information.

Recent adopted accounting pronouncements

In February 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2016-02, *Leases (codified as "ASC 842"),* which requires the recognition of lease assets and lease liabilities by lessees for those leases classified as operating leases under previous guidance. ASC 842 requires that a lessee recognize a liability to make lease payments (the lease liability) and a ROU asset representing its right to use the underlying asset for the lease term on the balance sheet.

The Company adopted ASC 842 on February 1, 2019 using the modified retrospective transition method with the adoption date as the date of initial application. Consequently, prior period balances and disclosures have not been restated. The Company has elected the package of practical expedients, which allows the Company not to reassess (1) whether any expired or existing contracts as of the adoption date contain a lease, (2) lease classification for any

HealthEquity, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Note 1. Summary of business and significant accounting policies (continued)

expired or existing leases as of the adoption date and (3) initial direct costs for any existing leases as of the adoption date. The adoption of ASC 842 on February 1, 2019 resulted in the recognition on the Company's condensed consolidated balance sheet of both operating lease liabilities of $40.6 million and ROU assets of $38.0 million, which equals the lease liabilities net of accrued rent previously recorded on its consolidated balance sheet under previous guidance. The adoption of ASC 842 did not have an impact on the Company's condensed consolidated statement of operations, stockholders' equity and cash flows for the three-month period ended April 30, 2019.

Recent issued accounting pronouncements

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses: Measurement of Credit Losses on Financial Instruments,* which requires financial assets measured at amortized cost be presented at the net amount expected to be collected. This ASU is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted. The Company does not plan to early adopt this ASU. The Company believes the adoption of this ASU will not have a material impact on its consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, *Simplifying the Test for Goodwill Impairment,* which removes step two from the goodwill impairment test. As a result, an entity should perform its annual goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount and should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting units' fair value. This ASU is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently evaluating the timing of adoption; however, it does not believe this ASU will have a material impact on the Company's consolidated financial statements.

In August 2018, FASB issued ASU 2018-13, *Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement* ("ASU 2018-13"), which amends ASC 820, "Fair Value Measurement." ASU 2018-13 modifies the disclosure requirements for fair value measurements by removing, modifying and adding certain disclosures. This ASU is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted. As this relates to disclosure only, the Company believes the adoption of this ASU will not have a material impact on its consolidated financial statements.

In August 2018, the FASB issued ASU 2018-15, *Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract*. This ASU allows the capitalization of implementation costs incurred in a hosting arrangement. This ASU is effective for fiscal years beginning after December 15, 2019. The Company is currently evaluating the potential effect of this ASU on the consolidated financial statements.

HealthEquity, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Note 2. Net income per share

The following table sets forth the computation of basic and diluted net income per share:

(in thousands, except per share data)	Three months ended April 30, 2019	2018
Numerator (basic and diluted):		
Net income	$ 41,822	$ 22,577
Denominator (basic):		
Weighted-average common shares outstanding	62,326	61,170
Denominator (diluted):		
Weighted-average common shares outstanding	62,326	61,170
Weighted-average dilutive effect of stock options and restricted stock units	1,575	1,523
Diluted weighted-average common shares outstanding	63,901	62,693
Net income per share:		
Basic	$ 0.67	$ 0.37
Diluted	$ 0.65	$ 0.36

For the three months ended April 30, 2019 and 2018, approximately 0.2 million shares attributable to stock options and restricted stock units were excluded from the calculation of diluted earnings per share as their inclusion would have been anti-dilutive.

Note 3. Supplemental financial statement information

Selected condensed consolidated balance sheet and condensed consolidated statement of operations and comprehensive income components consist of the following:

Property and equipment

Property and equipment consisted of the following as of April 30, 2019 and January 31, 2019:

(in thousands)	April 30, 2019	January 31, 2019
Leasehold improvements	$ 3,753	$ 3,583
Furniture and fixtures	4,828	4,476
Computer equipment	9,839	9,242
Property and equipment, gross	18,420	17,301
Accumulated depreciation	(9,939)	(9,078)
Property and equipment, net	$ 8,481	$ 8,223

Depreciation expense for the three months ended April 30, 2019 and 2018 was $0.9 million and $0.8 million, respectively.

Other investments

Other investments consisted of the following equity investments as of April 30, 2019 and January 31, 2019:

(in thousands)	April 30, 2019	January 31, 2019
Marketable equity securities, at fair value	$ 77,356	$ —
Non-marketable equity securities	500	500
Equity method investments	209	209
Total equity investments	$ 78,065	$ 709

Unrealized gain recognized during the three months ended April 30, 2019 for equity investments held as of April 30, 2019 was $23.5 million, which was attributable to an increase in fair value of marketable equity securities.

HealthEquity, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Note 3. Supplemental financial statement information (continued)

Other income (expense), net

Other income (expense), net, consisted of the following:

	Three months ended April 30,	
(in thousands)	**2019**	**2018**
Interest income, net	$ 1,280	$ 191
Unrealized gain on marketable equity securities	23,511	—
Acquisition-related costs	(1,184)	(1)
Other	(7)	(191)
Total other income (expense), net	$ 23,600	$ (1)

Note 4. Leases

The Company has entered into various non-cancelable operating lease agreements for office space and data storage facilities with remaining lease terms of approximately 3 to 12 years, often with one or more Company options to renew. These renewal terms can extend the lease term from 3 to 10 years and are included in the lease term when it is reasonably certain that the Company will exercise the option.

The components of operating lease costs, lease term and discount rate are as follows:

(in thousands, except for term and percentages)	Three months ended April 30, 2019
Operating lease expense	$ 1,074
Weighted average remaining lease term	11.49 years
Weighted average discount rate	4.37%

Maturities of operating lease liabilities as of April 30, 2019 were as follows:

Fiscal year ending January 31, (in thousands)	Operating leases
Remaining 2020	$ 2,865
2021	4,105
2022	4,205
2023	4,233
2024	4,288
Thereafter	31,930
Total lease payments	51,626
Less imputed interest	(11,597)
Present value of lease liabilities	$ 40,029
Current	$ 3,786
Non-current	36,243
Total lease liabilities	$ 40,029

As of April 30, 2019, the Company had an additional operating lease for office space that has not yet commenced with undiscounted lease payments of $17.1 million. This operating lease will commence in fiscal year 2021 with a lease term of approximately 11 years.

HealthEquity, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Note 4. Leases (continued)

Supplemental cash flow information related to the Company's operating leases was as follows:

(in thousands)		Three months ended April 30, 2019
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows from operating leases	$	977
ROU assets obtained in exchange for new operating lease obligations	$	199

Note 5. Intangible assets and goodwill

During the three months ended April 30, 2019 and 2018, the Company capitalized software development costs of $3.7 million and $2.1 million, respectively, related to significant enhancements and upgrades to its proprietary system.

The gross carrying amount and associated accumulated amortization of intangible assets were as follows as of April 30, 2019 and January 31, 2019:

(in thousands)		April 30, 2019		January 31, 2019
Amortized intangible assets:				
Capitalized software development costs	$	44,328	$	40,583
Software		6,162		4,252
Other intangible assets		2,882		2,882
Acquired intangible member assets		85,110		85,110
Intangible assets, gross		138,482		132,827
Accumulated amortization		(57,045)		(53,161)
Intangible assets, net	$	81,437	$	79,666

During the three months ended April 30, 2019 and 2018, the Company expensed a total of $3.9 million and $3.2 million, respectively, in software development costs primarily related to the post-implementation and operation stages of its proprietary software.

Amortization expense for the three months ended April 30, 2019 and 2018 was $3.9 million and $3.7 million, respectively.

There were no changes to the goodwill carrying value during the three months ended April 30, 2019 and 2018.

Note 6. Commitments and contingencies

The Company’s principal commitments consist of operating lease obligations for office space and data storage facilities, a processing services agreement with a vendor, and contractual commitments related to network infrastructure, equipment, and certain maintenance agreements under long-term, non-cancelable operating leases. These commitments as of January 31, 2019 are disclosed in the Company’s consolidated financial statements included in its Annual Report on Form 10-K for the year ended January 31, 2019, and did not change materially during the three months ended April 30, 2019.

Note 7. Indebtedness

On September 30, 2015, the Company entered into a new credit facility (the "Credit Agreement") that provides for a secured revolving credit facility in the aggregate principal amount of $100.0 million for a term of five years. The proceeds of borrowings under the Credit Agreement may be used for general corporate purposes. No amounts have been drawn under the Credit Agreement as of April 30, 2019.

Borrowings under the Credit Agreement bear interest equal to, at the Company's option, a) an adjusted LIBOR rate or b) a customary base rate, in each case with an applicable spread to be determined based on the Company's

HealthEquity, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Note 7. Indebtedness (continued)

leverage ratio as of the most recent fiscal quarter. The applicable spread for borrowing under the Credit Agreement ranges from 1.50% to 2.00% with respect to adjusted LIBOR rate borrowings and 0.50% to 1.00% with respect to customary base rate borrowings. Additionally, the Company pays a commitment fee ranging from 0.20% to 0.30% on the daily amount of the unused commitments under the Credit Agreement payable in arrears at the end of each fiscal quarter.

The Company's material subsidiaries are required to guarantee the obligations of the Company under the Credit Agreement. The obligations of the Company and the guarantors under the Credit Agreement and the guarantees are secured by substantially all assets of the Company and the guarantors, subject to customary exclusions and exceptions.

The Credit Agreement requires the Company to maintain a total leverage ratio of not more than 3.00 to 1.00 as of the end of each fiscal quarter and a minimum interest coverage ratio of at least 3.00 to 1.00 as of the end of each fiscal quarter. In addition, the Credit Agreement includes customary representations and warranties, affirmative and negative covenants, and events of default. The restrictive covenants include customary restrictions on the

Company's ability to incur additional indebtedness; make investments, loans or advances; grant or incur liens on assets; engage in mergers, consolidations, liquidations or dissolutions; engage in transactions with affiliates; and make dividend payments. The Company was in compliance with these covenants as of April 30, 2019.

Note 8. Income taxes

The Company follows FASB Accounting Standards Codification 740-270, *Income Taxes - Interim Reporting*, for the computation and presentation of its interim period tax provision. Accordingly, management estimated the effective annual tax rate and applied this rate to the year-to-date pre-tax book income to determine the interim provision for income taxes. For the three months ended April 30, 2019, the Company recorded income tax expense of $9.5 million. This resulted in an effective income tax expense rate of 18.4% for the three months ended April 30, 2019, compared with an effective income tax benefit rate of 9.9% for the three months ended April 30, 2018. For the three months ended April 30, 2019 and 2018, the net impact of discrete tax items caused a 4.5 and 31.8 percentage point decrease, respectively, to the effective income tax rate primarily due to the excess tax benefit on stock-based compensation expense recognized in the provision for income taxes in the condensed consolidated statements of operations and comprehensive income. The increase in the effective income tax rate from the same period last year is primarily due to a decrease in excess tax benefits on stock-based compensation expense recognized in the provision for income taxes relative to pre-tax book income.

As of April 30, 2019 and January 31, 2019, the Company’s total gross unrecognized tax benefit was $1.9 million and $1.7 million, respectively. Certain unrecognized tax benefits have been netted against their related deferred tax assets; therefore, no unrecognized tax benefit has been recorded as of April 30, 2019 and January 31, 2019. If recognized, $1.7 million of the total gross unrecognized tax benefits would affect the Company's effective tax rate as of April 30, 2019.

The Company files income tax returns with U.S. federal and state taxing jurisdictions and is not currently under examination with any jurisdiction. The Company remains subject to examination by federal and various state taxing jurisdictions for tax years after 2003.

HealthEquity, Inc. and subsidiaries
Notes to condensed consolidated financial statements (unaudited)

Note 9. Stock-based compensation

The following table shows a summary of stock-based compensation in the Company's condensed consolidated statements of operations and comprehensive income during the periods presented:

	Three months ended April 30,	
(in thousands)	**2019**	**2018**
Cost of revenue	$ 860	$ 413
Sales and marketing	1,007	705
Technology and development	1,499	991
General and administrative	2,662	2,130
Total stock-based compensation expense	$ 6,028	$ 4,239

The following table shows stock-based compensation by award type:

	Three months ended April 30,	
(in thousands)	**2019**	**2018**
Stock options	$ 1,783	$ 1,764
Performance stock options	—	153
Restricted stock units	2,926	1,542
Performance restricted stock units	651	514
Restricted stock awards	163	55
Performance restricted stock awards	505	211
Total stock-based compensation expense	$ 6,028	$ 4,239

Stock options

The Company currently grants stock options under the 2014 Equity Incentive Plan (as amended and restated, the"Incentive Plan"), which provided for the issuance of stock options to the directors and team members of the Company to purchase up to an aggregate of 2.6 million shares of common stock.

In addition, under the Incentive Plan, the number of shares of common stock reserved for issuance under the Incentive Plan automatically increases on February 1 of each year, beginning as of February 1, 2015 and continuing through and including February 1, 2024, by 3% of the total number of shares of the Company's capital stock outstanding on January 31 of the preceding fiscal year, or a lesser number of shares determined by the board of directors.

Under the terms of the Incentive Plan, the Company has the ability to grant incentive and nonqualified stock options. Incentive stock options may be granted only to Company team members. Nonqualified stock options may be granted to Company executive officers, other team members, directors and consultants. Such options are to be exercisable at prices, as determined by the board of directors, which must be equal to no less than the fair value of the Company's common stock at the date of the grant. Stock options granted under the Incentive Plan generally expire 10 years from the date of issuance, or are forfeited 90 days after termination of employment. Shares of common stock underlying stock options that are forfeited or that expire are returned to the Incentive Plan.

Valuation assumptions. The Company has adopted the provisions of Topic 718, which requires the measurement and recognition of compensation for all stock-based awards made to team members and directors, based on estimated fair values.

Under Topic 718, the Company uses the Black-Scholes option pricing model as the method of valuation for stock options. The determination of the fair value of stock-based awards on the date of grant is affected by the fair value of the stock as well as assumptions regarding a number of complex and subjective variables. The variables include, but are not limited to, 1) the expected life of the option, 2) the expected volatility of the fair value of the Company's common stock over the term of the award estimated by averaging the Company's historical volatility in addition to published volatilities of a relative peer group, 3) risk-free interest rate, and 4) expected dividends.

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Note 9. Stock-based compensation (continued)

The key input assumptions that were utilized in the valuation of the stock options granted during the periods presented:

	Three months ended April 30, 2019	2018
Expected dividend yield	—%	—%
Expected stock price volatility	35.98% - 36.53%	37.84%
Risk-free interest rate	2.21% - 2.43%	2.52% - 2.68%
Expected life of options	4.95 - 5.09 years	5.17 - 6.25 years

The Company historically used the "simplified" method to estimate the expected life of an option as determined under Staff Accounting Bulletin No. 110 due to limited option exercise history as a public company. Commencing February 1, 2019, the Company began estimating the expected life of an option using its own historical option exercise and termination data. Expected volatility is determined using weighted average volatility of the Company's historical common stock price in addition to published volatilities of publicly traded peer companies. The risk-free interest rate is determined by using published zero coupon rates on treasury notes for each grant date given the expected term on the options. The dividend yield of zero is based on the fact that the Company expects to invest cash in operations.

A summary of stock option activity is as follows:

	Outstanding stock options				
(in thousands, except for exercise prices and term)	**Number of options**	**Range of exercise prices**	**Weighted-average exercise price**	**Weighted-average contractual term (in years)**	**Aggregate intrinsic value**
Outstanding as of January 31, 2019	2,444	$0.10 - 82.39	$ 27.37	6.74	$ 85,971
Granted	108	$63.64 - 73.61	$ 73.27		
Exercised	(178)	$0.10 - 44.53	$ 24.49		
Forfeited	(18)	$24.36 - 44.53	$ 30.92		
Outstanding as of April 30, 2019	2,356	$0.10 - 82.39	$ 29.66	6.62	$ 90,701
Vested and expected to vest as of April 30, 2019	2,356		$ 29.66	6.62	$ 90,701
Exercisable as of April 30, 2019	1,503		$ 21.82	5.91	$ 69,042

The aggregate intrinsic value in the table above represents the difference between the estimated fair value of common stock and the exercise price of outstanding, in-the-money stock options.

As of April 30, 2019, the weighted-average vesting period of non-vested awards expected to vest is approximately 1.9 years; the amount of compensation expense the Company expects to recognize for stock options vesting in future periods is approximately $12.4 million.

Restricted stock units and restricted stock awards

The Company grants restricted stock units ("RSUs") and restricted stock awards ("RSAs") to certain team members, officers, and directors under the Incentive Plan. RSUs and RSAs vest upon service-based criteria and performance-based criteria. Generally, service-based RSUs and RSAs vest over a four-year period in equal annual installments commencing upon the first anniversary of the grant date. RSUs and RSAs are valued based on the current value of the Company's closing stock price on the date of grant less the present value of future expected dividends discounted at the risk-free interest rate.

Performance restricted stock units and awards. In March 2017, the Company awarded 146,964 performance-based RSUs ("PRSUs"). Vesting of the PRSUs is dependent upon the achievement of certain financial criteria and cliff vest on January 31, 2020. The Company records stock-based compensation related to PRSUs when it is

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Note 9. Stock-based compensation (continued)

considered probable that the performance conditions will be met. Issuance of the underlying shares occurs at vesting. The Company believes it is probable that the PRSUs will vest at least in part. The vesting of the PRSUs will ultimately range from 0% to 150% of the number of shares underlying the PRSU grant based on the level of achievement of the performance goals.

In March 2018, the Company awarded 227,760 performance-based RSAs ("PRSAs"). Vesting of the PRSAs is dependent upon the achievement of certain financial criteria and cliff vest on January 31, 2021. The Company records stock-based compensation related to PRSAs when it is considered probable that the performance conditions will be met. Issuance of the underlying shares occured at the grant date. The Company believes it is probable that the PRSAs will vest at least in part. The vesting of the PRSAs will ultimately range from 0% to 200% based on the level of achievement of the performance goals. The PRSAs were issued at the 200% level of achievement. As the underlying shares were issued at grant date, they are subject to clawback based on actual Company performance.

In March 2019, the Company awarded 129,963 PRSUs. Vesting of the PRSUs is dependent upon the achievement of certain financial criteria and cliff vest on January 31, 2022. The Company records stock-based compensation related to PRSUs when it is considered probable that the performance conditions will be met. Issuance of the underlying shares occurs at vesting. The Company believes it is probable that the PRSUs will vest at least in part. The vesting of the PRSUs will ultimately range from 0% to 200% of the number of shares underlying the PRSU grant based on the level of achievement of the performance goals.

A summary of the RSU and RSA activity is as follows:

	RSUs and PRSUs		RSAs and PRSAs	
(in thousands, except weighted-average grant date fair value)	**Shares**	**Weighted-average grant date fair value**	**Shares**	**Weighted-average grant date fair value**
Outstanding as of January 31, 2019	648	$ 55.20	256	$ 61.93
Granted	421	73.02	—	—
Vested	(94)	52.35	(11)	62.75
Forfeited	(19)	54.48	(10)	61.72
Outstanding as of April 30, 2019	956	$ 63.33	235	$ 61.91

For the three months ended April 30, 2019, the aggregate intrinsic value of RSUs and RSAs vested was $6.9 million and $0.8 million, respectively. For the three months ended April 30, 2018, the aggregate intrinsic value of RSUs vested was $2.9 million.

Total unrecorded stock-based compensation expense as of April 30, 2019 associated with RSUs and PRSUs was $52.0 million, which is expected to be recognized over a weighted-average period of 2.8 years. Total unrecorded stock-based compensation expense as of April 30, 2019 associated with RSAs and PRSAs was $6.2 million, which is expected to be recognized over a weighted-average period of 2.1 years.

Note 10. Fair Value

Fair value measurements are made at a specific point in time, based on relevant market information. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. Accounting standards specify a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect data obtained from independent sources, while unobservable inputs reflect the Company’s market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1—quoted prices in active markets for identical assets or liabilities;
- Level 2—inputs, other than the quoted prices in active markets, that are observable either directly or indirectly; and
- Level 3—unobservable inputs based on the Company’s own assumptions.

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Note 10. Fair Value (continued)

Level 1 instruments are valued based on publicly available daily net asset values. Level 1 instruments consist primarily of marketable equity securities.

The following table summarizes the assets measured at fair value on a recurring basis and indicates the level within the fair value hierarchy reflecting the valuation techniques utilized to determine fair value:

			April 30, 2019
(in thousands)	Level 1	Level 2	Level 3
Other investments:			
Marketable equity securities	$ 77,356	$ —	$ —

The Company did not have any assets measured at fair value on a recurring basis as of January 31, 2019. The Company has classified cash and cash equivalents and marketable equity securities as Level 1 in the fair value hierarchy.

Item 2. Management's discussion and analysis of financial condition and results of operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q. The following discussion and analysis contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. Statements that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements are often identified by the use of words such as, but not limited to, "anticipate," "believe," "can," "continue," "could," "estimate," "expect," "intend," "may," "plan," "project," "seek," "should," "target," "will," "would" and similar expressions or variations intended to identify forward-looking statements. Such statements include, but are not limited to, statements concerning market opportunity, our future financial and operating results, investment and acquisition strategy, sales and marketing strategy, management's plans, beliefs and objectives for future operations, technology and development, economic and industry trends or trend analysis, expectations about seasonality, opportunity for portfolio purchases and other acquisitions, use of non-GAAP financial measures, operating expenses, anticipated income tax rates, capital expenditures, cash flows and liquidity. These statements are based on the beliefs and assumptions of our management based on information currently available to us. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk factors" included in our Annual Report on Form 10-K for the year ended January 31, 2019, as updated by this Quarterly Report on Form 10-Q, and in our other reports filed with the SEC. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such events.

Overview

We are a leader and an innovator in the high-growth category of technology-enabled services platforms that empower consumers to make healthcare saving and spending decisions. Our platform provides an ecosystem where consumers can access their tax-advantaged healthcare savings, compare treatment options and pricing, evaluate and pay healthcare bills, receive personalized benefit and clinical information, earn wellness incentives, and make educated investment choices to grow their tax-advantaged healthcare savings.

The core of our ecosystem is the HSA, a financial account through which consumers spend and save long-term for healthcare on a tax-advantaged basis. We are the integrated HSA platform for 141 Health Plan and Administrator Partners and over 45,000 employer clients. Our Health Plan and Administrator Partners and Employer Partners constitute our Network Partners.

Since our inception in 2002, we have been committed to developing technology solutions that empower healthcare consumers. We have a proprietary cloud-based technology platform, developed and refined during more than a decade of operations, which we believe is highly differentiated in the marketplace. Key platform differentiators include purpose-built technology that offers greater functionality and flexibility than the technologies used by our competitors, more than 3,000 data integrations with our Network Partner and other benefits provider systems, and configurability solutions with more than 1,700 uniquely tailored configurations serving our Network Partners. We work closely with our Network Partners to educate and provide personalized guidance regarding the benefits of HSAs and our other products.

We earn revenue primarily from three sources: service revenue, custodial revenue and interchange revenue. We earn service revenue by providing monthly account services on our platform, primarily through contracts with our Network Partners, and custodial agreements with individual members. We earn custodial revenue from custodial cash assets deposited with our federally-insured custodial depository partners and with our insurance company partner, and recordkeeping fees we earn in respect of mutual funds in which our members invest. We also earn interchange revenue from interchange fees that we earn on payments that our members make using our physical and virtual payment cards.

Key factors affecting our performance

We believe that our performance and future success are driven by a number of factors, including those identified below. Each of these factors presents both significant opportunities and significant risks to our future performance. See the section entitled “Risk factors” included in our Annual Report on Form 10-K, as updated by this Quarterly Report on Form 10-Q.

Structural change in U.S. private health insurance

Substantially all of our revenue is derived from healthcare-related saving and spending by consumers in the United States, which is impacted by changes affecting the broader healthcare industry in the U.S. The healthcare industry has changed significantly in recent years, and we expect that significant changes will continue to occur that will result in increased participation in high deductible healthcare plans, or HDHPs, and other consumer-centric health plans. In particular, we believe that continued growth in healthcare costs, and related factors will spur HDHP and HSA growth; however, the timing and impact of these and other developments in the healthcare industry are difficult to predict, and changes in U.S. healthcare policy could adversely affect our business.

Attracting and penetrating network partners

We created our business model to take advantage of the changing dynamics of the U.S. private health insurance market. Our model is based on a B2B2C distribution strategy, meaning that we rely on our Employer Partners and Health Plan and Administrator Partners to reach potential members to increase the number of our HSA Members. Our success depends in large part on our ability to further penetrate our existing Network Partners by adding new HSA Members from these partners and adding new Network Partners.

Our innovative technology platform

We believe that innovations incorporated in our technology that enable consumers to make healthcare saving and spending decisions differentiate us from our competitors and drive our growth in revenue, HSA Members, Network Partners and custodial assets. Similarly, these innovations underpin our ability to provide a differentiated consumer experience in a cost-effective manner. We intend to continue to invest in our technology development to enhance our platform’s capabilities and infrastructure. For example, we are currently undertaking a significant update of our proprietary platform’s architecture, which will allow us to improve our transaction processing capabilities and related platform infrastructure to support continued account and transaction growth.

Our “DEEP Purple” culture

The new healthcare consumer needs education and guidance delivered by people as well as technology. We believe that our "DEEP Purple" culture which we define as driving excellence, ethics, and process while providing remarkable service, is a significant factor in our ability to attract and retain customers and to address nimbly, opportunities in the rapidly changing healthcare sector. We make significant efforts to promote and foster DEEP

Purple within our workforce. We invest in and intend to continue to invest in human capital through technology-enabled training, career development and advancement opportunities.

Interest rates

As a non-bank custodian, we contract with federally-insured custodial depository partners and an insurance company partner to hold custodial cash assets on behalf of our members, and we earn a significant portion of our total revenue from interest rates offered to us by these partners. The contract terms range from three to five years and have either fixed or variable interest rates. As our custodial assets increase and existing agreements expire, we seek to enter into new contracts with federally-insured custodial depository partners, the terms of which are impacted by the then-prevailing interest rate environment. The diversification of deposits among partners and varied contract terms substantially reduces our exposure to short-term fluctuations in prevailing interest rates and mitigates the short-term impact of a sustained increase or decline in prevailing interest rates on our custodial revenue. A sustained decline in prevailing interest rates may negatively affect our business by reducing the size of the interest rate yield, or yield, available to us and thus the amount of the custodial revenue we can realize. Conversely, a sustained increase in prevailing interest rates without a corresponding increase in what we pay on our members' deposits can increase our yield over time. An increase in our yield would increase our custodial revenue as a percentage of total revenue. In addition, as our yield increases, we expect the spread to grow between the interest offered to us by our custodial depository partners and the interest retained by our members, thus increasing our profitability. However, we may be required to increase the interest retained by our members in a rising prevailing interest rate environment. Changes in prevailing interest rates are driven by macroeconomic trends and government policies over which we have no control.

Our competition and industry

Our direct competitors are HSA custodians. Many of these are state or federally chartered banks and other financial institutions for which we believe technology-based healthcare services are not a core business. Certain of our direct competitors have chosen to exit the market despite increased demand for these services. This has created, and we believe will continue to create, opportunities for us to leverage our technology platform and capabilities to increase our market share. However, some of our direct competitors (including well-known mutual fund companies such as Fidelity) are in a position, should they choose, to devote more resources to the development, sale and support of their products and services than we have at our disposal. In addition, numerous indirect competitors, including benefits administration technology and service providers, partner with banks and other HSA custodians to compete with us. Our Health Plan and Administrator Partners may also choose to offer technology-based healthcare services directly, as some health plans have done. Our success depends on our ability to predict and react quickly to these and other industry and competitive dynamics.

Regulatory environment

Federal law and regulations, including the Affordable Care Act, the Internal Revenue Code and IRS regulations, the Employee Retirement Income Security Act and Department of Labor regulations, and public health regulations that govern the provision of health insurance, play a pivotal role in determining our market opportunity. Privacy and data security-related laws such as the Health Insurance Portability and Accountability Act, or HIPAA, and the Gramm-Leach-Bliley Act, laws governing the provision of investment advice to consumers, such as the Investment Advisers Act of 1940, or the Advisers Act, the USA PATRIOT Act, anti-money laundry laws, and the Federal Deposit Insurance Act, all play a similar role in determining our competitive landscape. In addition, state-level regulations also have significant implications for our business in some cases. For example, our subsidiary HealthEquity Trust Company is regulated by the Wyoming Division of Banking, and several states are considering, or have already passed, new fiduciary rules that can affect our business. Our ability to predict and react quickly to relevant legal and regulatory trends and to correctly interpret their market and competitive implications is important to our success.

Our acquisition strategy

We have a successful history of acquiring complementary assets and businesses that strengthen our platform. We seek to continue this growth strategy and are regularly engaged in evaluating different opportunities. We have developed an internal capability to source, evaluate and integrate acquisitions that have created value for shareholders. We intend to continue to pursue acquisitions of complementary assets and businesses that we believe will strengthen our platform.

From February 1, 2019 to April 4, 2019, we acquired approximately 1.6 million common shares of WageWorks, Inc. ("WageWorks") in open market purchases. On April 11, 2019, we made a proposal to acquire all of the outstanding shares of WageWorks for $50.50 per share in cash, or approximately $2 billion. As further described below, during the three months ended April 30, 2019, we recognized an unrealized gain of $23.5 million (pre-tax) in connection with the WageWorks investment.

Key financial and operating metrics

Our management regularly reviews a number of key operating and financial metrics to evaluate our business, determine the allocation of our resources, make decisions regarding corporate strategies and evaluate forward-looking projections and trends affecting our business. We discuss certain of these key financial metrics, including revenue, below in the section entitled “Key components of our results of operations.” In addition, we utilize other key metrics as described below.

HSA Members

The following table sets forth our HSA Members as of and for the periods indicated:

(in millions, except percentages)	April 30, 2019	April 30, 2018	% Change	January 31, 2019
HSA Members	4,054	3,476	17 %	3,994
Average HSA Members - Year-to-date	4,026	3,444	17 %	3,608
Average HSA Members - Quarter-to-date	4,026	3,444	17 %	3,813
New HSA Members - Year-to-date	89	98	(9)%	679
New HSA Members - Quarter-to-date	89	98	(9)%	341
Active HSA Members	3,245	2,882	13 %	3,241
HSA Members with investments	177	134	32 %	163

The number of our HSA Members is a key metric because our revenue is driven by the amount we earn from our HSA Member's accounts, balances and spend. The number of our HSA Members increased by approximately 578,000, or 17%, from April 30, 2018 to April 30, 2019, primarily driven by further penetration into existing Network Partners and the addition of new Network Partners.

HSAs are individually owned portable healthcare accounts. As HSA Members transition between employers or health plans, they may no longer be enrolled in an HDHP that qualifies them to continue to make contributions to their HSA. If these HSA Members deplete their custodial balance, we may consider them no longer an Active HSA Member. We define an Active HSA Member as an HSA Member that (i) is associated with a Health Plan and Administrator Partner or an Employer Partner, in each case as of the end of the applicable period; or (ii) has held a custodial balance at any point during the previous twelve month period. Active HSA Members increased 13% from 2.9 million as of April 30, 2018 to 3.2 million as of April 30, 2019.

Custodial assets

The following table sets forth our HSA Member custodial assets as of and for the periods indicated:

(in millions, except percentages)	April 30, 2019	April 30, 2018	% Change	January 31, 2019
Custodial cash	$ 6,404	$ 5,511	16%	$ 6,428
Custodial investments	1,917	1,351	42%	1,670
Total custodial assets	$ 8,321	$ 6,862	21%	$ 8,098
Average daily custodial cash - Year-to-date	$ 6,407	$ 5,467	17%	$ 5,586
Average daily custodial cash - Quarter-to-date	$ 6,407	$ 5,467	17%	$ 5,837

Our custodial assets, which are our HSA Members' assets for which we are the custodian, consist of the following components: (i) custodial cash deposits, which are deposits with our federally-insured custodial depository partners, (ii) custodial cash deposits invested in an annuity contract with our insurance company partner, and (iii) investments in mutual funds through our custodial investment fund partner. Measuring our custodial assets is important because our custodial revenue is directly affected by average daily custodial balances.

Our total custodial assets increased by $1.5 billion, or 21%, from April 30, 2018 to April 30, 2019, primarily driven by additional custodial assets from our existing HSA Members and new custodial assets from our new HSA Members. Importantly, our custodial investment assets increased by $566 million, or 42%, from April 30, 2018 to April 30, 2019, reflecting our strategy to help our HSA Members build wealth and invest for retirement.

Adjusted EBITDA

We define Adjusted EBITDA, which is a non-GAAP financial metric, as adjusted earnings before interest, taxes, depreciation and amortization, stock-based compensation expense, unrealized gains and losses on marketable equity securities, and certain other non-operating items. We believe that Adjusted EBITDA provides useful information to investors and analysts in understanding and evaluating our operating results in the same manner as our management and our board of directors because it reflects operating profitability before consideration of non-operating expenses and non-cash expenses, and serves as a basis for comparison against other companies in our industry.

The following table presents a reconciliation of net income, the most comparable GAAP financial measure, to Adjusted EBITDA for each of the periods indicated:

	Three months ended April 30,	
(in thousands)	**2019**	**2018**
Net income	$ 41,822	$ 22,577
Interest income	(1,343)	(258)
Interest expense	63	67
Income tax provision (benefit)	9,456	(2,038)
Depreciation and amortization	3,282	3,050
Amortization of acquired intangible assets	1,491	1,470
Stock-based compensation expense	6,028	4,239
Unrealized gain on marketable equity securities	(23,511)	—
Other (1)	1,635	520
Adjusted EBITDA	$ 38,923	$ 29,627

(1) For the three months ended April 30, 2019 and 2018, Other consisted of non-income-based taxes of $13 and $104, other (income)/costs of $(6) and $88, acquisition-related costs of $1,184 and $1, and amortization of incremental costs to obtain a contract of $444 and $327, respectively.

The following table further sets forth our Adjusted EBITDA:

	Three months ended April 30,			
(in thousands, except percentages)	**2019**	**2018**	**$ Change**	**% Change**
Adjusted EBITDA	$ 38,923	$ 29,627	$ 9,296	31%
As a percentage of revenue	45%	42%		

Our Adjusted EBITDA increased by $9.3 million, or 31%, from $29.6 million for the three months ended April 30, 2018 to $38.9 million for the three months ended April 30, 2019. The increase in Adjusted EBITDA was driven by the overall growth of our business, including a $7.1 million, or 35%, increase in income from operations.

Our use of Adjusted EBITDA has limitations as an analytical tool, and it should not be considered in isolation or as a substitute for analysis of our results as reported under GAAP.

Key components of our results of operations

Revenue

We generate revenue from three primary sources: service revenue, custodial revenue, and interchange revenue.

Service revenue. We earn service revenue from the fees we charge our Network Partners, employer clients and individual members for the administration services we provide in connection with the HSAs and RAs we offer. With respect to our Network Partners, our fees are generally based on a fixed tiered structure for the duration of our agreement with the relevant Network Partner and are paid to us on a monthly basis. We recognize revenue on a monthly basis as services are rendered under our written service agreements.

Custodial revenue. We earn custodial revenue, an increasing component of our overall revenue, from our HSA Member custodial cash assets deposited with our federally-insured custodial depository partners and with our insurance company partner, Employer Partner custodial cash assets, and recordkeeping fees we earn in respect of mutual funds in which our members invest. As a non-bank custodian, we deposit our custodial cash with our various depository partners pursuant to contracts that (i) have terms up to five years, (ii) provide for a fixed or variable interest rate payable on the average daily cash balances deposited with the relevant depository partner, and (iii) have minimum and maximum required deposit balances. We earn custodial revenue on our custodial cash that is based on the interest rates offered to us by these depository partners. In addition, once a member’s HSA cash balance reaches a certain threshold, the member is able to invest his or her HSA assets in mutual funds through our custodial investment partner. We earn a recordkeeping fee, calculated as a percentage of invested assets, in respect of custodial investments.

Interchange revenue. We earn interchange revenue each time one of our members uses one of our payment cards to make a qualified purchase. This revenue is collected each time a member “swipes” our payment card to pay a healthcare-related expense. We recognize interchange revenue monthly based on reports received from third parties, namely, the card-issuing bank and the card processor.

Cost of revenue

Cost of revenue includes costs related to servicing member accounts, managing customer and partner relationships and processing reimbursement claims. Expenditures include personnel-related costs, depreciation, amortization, stock-based compensation, common expense allocations (such as office rent, supplies, and other overhead expenses), new member and participant supplies, and other operating costs related to servicing our members. Other components of cost of revenue include interest retained by members on custodial cash and interchange costs incurred in connection with processing card transactions for our members.

Service costs. Service costs include the servicing costs described above. Additionally, for new accounts, we incur on-boarding costs associated with the new accounts, such as new member welcome kits, the cost associated with issuance of new payment cards and costs of marketing materials that we produce for our Network Partners.

Custodial costs. Custodial costs are comprised of interest retained by our HSA Members and fees we pay to banking consultants whom we use to help secure agreements with our federally-insured custodial depository partners. Interest retained by HSA Members is calculated on a tiered basis. The interest rates retained by HSA Members can change based on a formula or upon required notice.

Interchange costs. Interchange costs are comprised of costs we incur in connection with processing payment transactions initiated by our members. Due to the substantiation requirement on RA-linked payment card transactions, payment card costs are higher for RA card transactions. In addition to fixed per card fees, we are assessed additional transaction costs determined by the amount of the transaction.

Gross profit and gross margin

Our gross profit is our total revenue minus our total cost of revenue, and our gross margin is our gross profit expressed as a percentage of our total revenue. Our gross margin has been and will continue to be affected by a number of factors, including interest rates, the amount we charge our partners and members, how many services we deliver per account, and payment processing costs per account. We expect our annual gross margin to increase somewhat over the near term as our custodial revenue increases as a percentage of total revenue, although our gross margin could fluctuate from period to period depending on the interplay of these factors.

Operating expenses

Sales and marketing. Sales and marketing expenses consist primarily of personnel and related expenses for our sales and marketing staff, including sales commissions for our direct sales force, external agent/broker commission expenses, marketing expenses, depreciation, amortization, stock-based compensation, and common expense allocations.

Technology and development. Technology and development expenses include personnel and related expenses for software engineering, information technology, and product development. Technology and development expenses also include software engineering services, the costs of operating our on-demand technology infrastructure, depreciation, amortization of capitalized software development costs, stock-based compensation, and common expense allocations.

General and administrative. General and administrative expenses include personnel and related expenses of, and professional fees incurred by our executive, finance, legal, compliance, and people departments. They also include depreciation, amortization, stock-based compensation and common expense allocations.

Amortization of acquired intangible assets. Amortization of acquired intangible assets results primarily from our acquisition of intangible member assets. We acquired these intangible member assets from third-party custodians. We amortize these assets over the assets’ estimated useful life of 15 years. We also acquired other intangible assets, which are 401(k) customer relationships, in connection with an acquisition of a business. We amortize these assets over the assets' estimated useful life of 10 years. We evaluate our acquired intangible assets for impairment at least each year, or at a triggering event.

Other income (expense), net

Other income (expense) primarily consists of unrealized holding gains and losses on mark-to-market investments, less interest expense associated with our credit agreement, non-income-based taxes and acquisition-related expenses, plus interest income earned on corporate cash.

Income tax provision

We are subject to federal and state income taxes in the United States based on a calendar tax year which differs from our fiscal year-end for financial reporting purposes. We use the asset and liability method to account for income taxes, under which current tax liabilities and assets are recognized for the estimated taxes payable or refundable on the tax returns for the current fiscal year. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, net operating loss carryforwards, and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted statutory tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be realized or settled. As of April 30, 2019, we recorded a net deferred tax liability in most jurisdictions except Utah and three other states for which a net deferred tax asset has been recorded. Valuation allowances are established when necessary to reduce net deferred tax assets to the amount expected to be realized. Due to the positive evidence of current taxable income coupled with forecasted profitability, no valuation allowance was required as of April 30, 2019 for most of our deferred tax assets. However, we recorded a valuation allowance of $0.1 million as of April 30, 2019 and January 31, 2019 with respect to unrealized capital losses for which we do not expect to generate taxable capital gains in order to utilize the capital losses in the future.

Comparison of the three months ended April 30, 2019 and 2018

Our net income increased 85% to $41.8 million during the three months ended April 30, 2019 from $22.6 million during the three months ended April 30, 2018, primarily due to a $17.9 million, net of tax, unrealized gain ($23.5 million pre-tax) this quarter in connection with our equity investment in WageWorks as well as a $7.1 million increase in income from operations, partially offset by a $11.5 million increase in our income tax provision.

The following table sets forth our revenue for the periods indicated:

	Three months ended April 30,			
(in thousands, except percentages)	**2019**	**2018**	**$ Change**	**% Change**
Service revenue	$ 26,808	$ 24,821	$ 1,987	8%
Custodial revenue	41,952	28,434	13,518	48%
Interchange revenue	18,292	16,649	1,643	10%
Total revenue	$ 87,052	$ 69,904	$ 17,148	25%

Service revenue

The $2.0 million, or 8%, increase in service revenue from the three months ended April 30, 2018 to the three months ended April 30, 2019 was primarily due to an increase in the number of our HSA Members, partially offset by lower service revenue per average HSA Members. The number of our HSA Members increased by approximately 578,000, or 17%, from April 30, 2018 to April 30, 2019. The growth in the number of our HSA Members was primarily due to growth from our new and existing Network Partners.

Service revenue as a percentage of our total revenue continues to decrease primarily due to the higher growth rate of custodial revenue.

Service revenue per average HSA Members decreased by approximately 8% from the three months ended April 30, 2018 to the three months ended April 30, 2019. Our service fee tiered pricing structure incentivizes our Network Partners to add HSA Members because we charge a lower rate for higher volumes of HSA Members. As Network Partners add more HSA Members, the account fee per average HSA Members will continue to decrease.

Custodial revenue

The $13.5 million, or 48%, increase in custodial revenue from the three months ended April 30, 2018 to the three months ended April 30, 2019 was primarily due to an increase in the yield on average custodial cash assets from 2.04% for the three months ended April 30, 2018 to 2.53% and an increase in average daily custodial cash assets of $940.3 million, or 17%.

Custodial revenue as a percentage of our total revenue continues to increase primarily due to new custodial depository agreements with higher interest rates payable on average cash balances deposited thereunder, and also due to average daily custodial cash asset growth.

Custodial revenue per average HSA Members increased by approximately 26% from the three months ended April 30, 2018 to the three months ended April 30, 2019 primarily due to the increase in the yield on and balances of average daily custodial cash assets.

Interchange revenue

The $1.6 million, or 10%, increase in interchange revenue from the three months ended April 30, 2018 to the three months ended April 30, 2019 was primarily due to an overall increase in the number of average HSA Members partially offset by lower card spend per average HSA Members.

Interchange revenue per average HSA Members decreased by approximately 6% from the three months ended April 30, 2018 to the three months ended April 30, 2019, primarily due to a decrease in card spend per average HSA Members.

Total revenue

Total revenue per average HSA Members increased by 7% from the three months ended April 30, 2018 to the three months ended April 30, 2019, due to the increase in custodial revenue per average HSA Members, partially offset by the decreases in service and interchange revenue per average HSA Members.

Cost of revenue

The following table sets forth our cost of revenue for the periods indicated:

	Three months ended April 30,			
(in thousands, except percentages)	**2019**	**2018**	**$ Change**	**% Change**
Service costs	$ 20,649	$ 18,047	$ 2,602	14%
Custodial costs	4,123	3,439	684	20%
Interchange costs	4,527	4,062	465	11%
Total cost of revenue	$ 29,299	$ 25,548	$ 3,751	15%

Service costs

The $2.6 million, or 14%, increase in service costs from the three months ended April 30, 2018 to the three months ended April 30, 2019 was due to the higher volume of accounts being serviced**.** The $2.6 million increase is due to increases in activation and processing costs of $1.4 million, increases of $0.7 million related to the hiring of additional personnel to implement and support our new Network Partners and HSA Members, and increases in stock-based compensation expense of $0.5 million. Service costs per average HSA Members decreased by 2% from the three months ended April 30, 2018 to the three months ended April 30, 2019 due to lower incremental expenses associated with fraud prevention measures.

Custodial costs

The $0.7 million, or 20%, increase in custodial costs from the three months ended April 30, 2018 to the three months ended April 30, 2019 was due to an increase in average daily custodial cash assets, which increased from $5.5 billion for the three months ended April 30, 2018 to $6.4 billion for the three months ended April 30, 2019. Custodial costs on average custodial cash assets decreased slightly from 0.24% for the three months ended April 30, 2018 to 0.23% for the three months ended April 30, 2019.

Interchange costs

The $0.5 million, or 11%, increase in interchange costs for the three months ended April 30, 2018 compared to the three months ended April 30, 2019 was due to an overall increase in average HSA Members, partially offset by decreased card spend per average HSA Members.

Cost of revenue

As we continue to add HSA Members, we expect that our cost of revenue will increase in dollar amount to support our Network Partners and members. Cost of revenue will continue to be affected by a number of different factors, including our ability to scale our Member Education Center, Network Partner implementation and account management functions.

Operating expenses

The following table sets forth our operating expenses for the periods indicated:

	Three months ended April 30,			
(in thousands, except percentages)	**2019**	**2018**	**$ Change**	**% Change**
Sales and marketing	$ 8,970	$ 6,860	$ 2,110	31%
Technology and development	10,905	7,979	2,926	37%
General and administrative	8,709	7,507	1,202	16%
Amortization of acquired intangible assets	1,491	1,470	21	1%
Total operating expenses	$ 30,075	$ 23,816	$ 6,259	26%

Sales and marketing

The $2.1 million, or 31%, increase in sales and marketing expense from the three months ended April 30, 2018 to the three months ended April 30, 2019 was due to increased staffing of $1.5 million, higher stock-based compensation expense of $0.3 million, and increases in other expenses of $0.3 million.

We expect our sales and marketing expenses to increase for the foreseeable future as we continue to increase the size of our sales and marketing organization and expand into new markets. On an annual basis, we expect our sales and marketing expenses to increase slightly as a percentage of our total revenue over the near term pursuant to our growth initiatives. However, our sales and marketing expenses may fluctuate as a percentage of our total revenue from period to period due to the seasonality of our total revenue and the timing and extent of our sales and marketing expenses.

Technology and development

The $2.9 million, or 37%, increase in technology and development expense from the three months ended April 30, 2018 to the three months ended April 30, 2019 was due to increased personnel-related expense of $1.7 million, increases in professional fees of $1.6 million, increases in amortization, depreciation and stock-based compensation of $0.9 million, and other increases of $0.4 million, which were partially offset by decreases in capitalized development of $1.7 million.

We expect our technology and development expenses to increase for the foreseeable future as we continue to invest in the development and security of our proprietary system. On an annual basis, we expect our technology and development expenses to increase as a percentage of our total revenue pursuant to our growth initiatives. Our technology and development expenses may fluctuate as a percentage of our total revenue from period to period due to the seasonality of our total revenue and the timing and extent of our technology and development expenses.

General and administrative

The $1.2 million, or 16%, increase in general and administrative expense from the three months ended April 30, 2018 to the three months ended April 30, 2019 was due to increased personnel-related expense of $0.6 million, increases in stock-based compensation of $0.5 million, and increases in other expenses of $0.1 million.

We expect our general and administrative expenses to increase for the foreseeable future due to the additional demands on our legal, compliance, accounting, and insurance functions that we incur as we continue to grow our business, as well as other costs associated with being a public company. On an annual basis, we expect our general and administrative expenses to remain steady as a percentage of our total revenue. Our general and administrative expenses may fluctuate as a percentage of our total revenue from period to period due to the seasonality of our total revenue and the timing and extent of our general and administrative expenses.

Other income (expense), net

The change in other income (expense), net, from the three months ended April 30, 2018 to the three months ended April 30, 2019 was primarily due to an unrealized gain of $23.5 million in connection with our equity investment in WageWorks, as well as interest income, net, on corporate cash of $1.3 million, partially offset by acquisition-related costs of $1.2 million.

Income tax provision (benefit)

Income tax provision for the three months ended April 30, 2019 was $9.5 million as compared to an income tax benefit of $2.0 million for the three months ended April 30, 2018. The increase in the tax provision for the three months ended April 30, 2019 compared to the three months ended April 30, 2018 of $11.5 million was primarily due to the unrealized gain of $23.5 million in connection with our equity investment in WageWorks coupled with a decrease in excess tax benefits from stock-based compensation.

Our effective income tax rate for the three months ended April 30, 2019 was a provision of 18.4%, compared to a benefit of 9.9% for the three months ended April 30, 2018. The change to an income tax provision from an income tax benefit for the three months ended April 30, 2019 compared to the three months ended April 30, 2018 is primarily due to a decrease in excess tax benefits related to stock-based compensation recognized in the provision for income taxes relative to pre-tax book income.

Seasonality

Seasonal concentration of our growth combined with our recurring revenue model create seasonal variation in our results of operations. A significant number of new and existing Network Partners bring us new HSA Members beginning in January of each year concurrent with the start of many employers' benefit plan years. Before we realize any revenue from these new HSA Members, we incur costs related to implementing and supporting our new Network Partners and new HSA Members. These costs of services relate to activating accounts and hiring additional staff, including seasonal help to support our member support center. These expenses begin to ramp up during our third fiscal quarter with the majority of expenses incurred in our fourth fiscal quarter.

Liquidity and capital resources

Cash and cash equivalents overview

As of April 30, 2019, our principal source of liquidity was our current cash and cash equivalents balances, collections from our service, custodial and interchange revenue activities, and availability under our credit facility. We rely on cash provided by operating activities to meet our short-term liquidity requirements, which primarily relate to the payment of corporate payroll and other operating costs, and capital expenditures.

As of April 30, 2019 and January 31, 2019, cash and cash equivalents were $329.3 million and $361.5 million, respectively.

Capital resources

We have a "shelf" registration statement on Form S-3 on file with the SEC. This shelf registration statement, which includes a base prospectus, allows us at any time to offer any combination of securities described in the prospectus in one or more offerings. Unless otherwise specified in a prospectus supplement accompanying the base prospectus, we would use the net proceeds from the sale of any securities offered pursuant to the shelf registration statement for general corporate purposes, including, but not limited to, working capital, sales and marketing activities, general and administrative matters and capital expenditures, and if opportunities arise, for the acquisition of, or investment in, assets, technologies, solutions or businesses that complement our business. Pending such uses, we may invest the net proceeds in interest-bearing securities. In addition, we may conduct concurrent or other financings at any time.

We have a secured credit facility of $100.0 million. The credit facility has a term of five years and expires on September 30, 2020. The credit facility contains covenants and events of default customary for facilities of this type. There were no borrowings under the facility as of April 30, 2019. We were in compliance with all covenants as of April 30, 2019.

Use of cash

From February 1, 2019 to April 4, 2019, we acquired approximately 1.6 million common shares of WageWorks for $53.8 million in open market purchases ahead of our April 11, 2019 proposal to acquire all of WageWorks' outstanding shares for $50.50 per share in cash, or approximately $2 billion.

Capital expenditures for the three months ended April 30, 2019 and 2018 were $6.6 million and $3.2 million, respectively. We expect our capital expenditures to increase for the remainder of the year ending January 31, 2020 as we continue to devote capital expenditures to improve the architecture and functionality of our proprietary system. Costs to improve the architecture of our proprietary system include computer hardware, personnel and related costs for software engineering and outsourced software engineering services. In addition, we plan to devote further resources to leasehold improvements and furniture and fixtures for our office space.

We believe our existing cash and cash equivalents will be sufficient to meet our operating and capital expenditure requirements for at least the next 12 months. To the extent these current and anticipated future sources of liquidity are insufficient to fund our future business activities and requirements, we may need to raise additional funds through public or private equity or debt financing. In the event that additional financing is required, we may not be able to raise it on favorable terms, if at all.

The following table shows our cash flows from operating activities, investing activities and financing activities for the stated periods:

	Three months ended April 30,	
(in thousands)	**2019**	**2018**
Net cash provided by operating activities	$ 25,336	$ 22,704
Net cash used in investing activities	(61,730)	(3,398)
Net cash provided by financing activities	4,229	10,167
Increase (decrease) in cash and cash equivalents	(32,165)	29,473
Beginning cash and cash equivalents	361,475	199,472
Ending cash and cash equivalents	$ 329,310	$ 228,945

Cash flows provided by operating activities. Net cash provided by operating activities during the three months ended April 30, 2019 resulted primarily from our net income of $41.8 million, adjusted for the following non-cash items: depreciation and amortization of $4.8 million, stock-based compensation of $6.0 million, and changes in deferred taxes of $7.5 million, operating lease right-of-use assets of $0.6 million, and accrued liabilities and other current liabilities of $1.8 million. These items were offset by unrealized gains on marketable equity securities of $23.5 million, a decrease in accrued compensation of $8.5 million resulting from the payment of bonuses and commissions subsequent to year-end, an increase in accounts receivable of $1.4 million, an increase in other assets of $1.7 million, and a decrease in other long-term liabilities, operating lease liabilities, and accounts payable of $2.1 million.

Net cash provided by operating activities during the three months ended April 30, 2018 resulted primarily from our net income of $22.6 million, adjusted for the following non-cash items: depreciation and amortization of $4.5 million, stock-based compensation of $4.2 million, and changes in deferred taxes of $2.0 million, and changes in inventories, accrued liabilities, accounts payable, other long-term liabilities, and unrealized losses on marketable securities and other totaling $1.2 million. These items were offset by an increase in other assets of $5.5 million, a decrease in accrued compensation of $4.9 million resulting from the payment of bonuses and commissions subsequent to year-end, and an increase in accounts receivable of $1.4 million.

Cash flows used in investing activities. Net cash used in investing activities for the three months ended April 30, 2019 was primarily the result of purchases of marketable equity securities of $53.8 million. We also continued development of our proprietary system and other software necessary to support our continued account growth. Purchases of software and capitalized software development costs for the three months ended April 30, 2019 were $5.5 million, compared to purchases of software and capitalized software development costs of $2.1 million for the three months ended April 30, 2018. In addition, during the three months ended April 30, 2019, purchases of intangible member assets resulted in cash outflows of $1.3 million.

Cash flows provided by financing activities. Cash flow provided by financing activities during the three months ended April 30, 2019 resulted primarily from the proceeds associated with the exercise of stock options of $4.2 million compared to $10.2 million for the three months ended April 30, 2018.

Contractual obligations

There were no material changes, outside of the ordinary course of business, in our contractual obligations from those disclosed in our Annual Report on Form 10-K for the year ended January 31, 2019.

Off-balance sheet arrangements

During the three months ended April 30, 2019 and 2018, we did not have any relationships with unconsolidated organizations or financial partnerships, such as structured finance or special purpose entities, that would have been established for the purpose of facilitating off-balance sheet arrangements.

Critical accounting policies and significant management estimates

Our management's discussion and analysis of financial condition and results of operations are based upon our unaudited condensed consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these unaudited condensed consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis, we evaluate our critical accounting policies and estimates. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable in the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions and conditions. Our significant accounting policies are more fully described in Note 1 of the accompanying unaudited condensed consolidated financial statements and in Note 1 to our audited consolidated financial statements contained in our Annual Report on Form 10-K for the year ended January 31, 2019. Other than the adoption of ASU 2016-02 and related subsequent amendments, *Leases*, and updates to our Investment policies described in Note 1 of the accompanying unaudited condensed consolidated financial statements, there have been no significant or material changes in our critical accounting policies during the three months ended April 30, 2019, as compared to those disclosed in "Management's discussion and analysis of financial condition and results of operations – Critical accounting policies and significant management estimates" in our Annual Report on Form 10-K for the year ended January 31, 2019.

Recent accounting pronouncements

See Note 1. Summary of business and significant accounting policies within the interim financial statements included in this Form 10-Q for further discussion.

Item 3. Qualitative and quantitative disclosures about market risk

Market risk

Concentration of market risk. We derive a substantial portion of our revenue from providing services to tax-advantaged healthcare account holders. A significant downturn in this market or changes in state and/or federal laws impacting the preferential tax treatment of healthcare accounts such as HSAs could have a material adverse effect on our results of operations. During the three months ended April 30, 2019, no one customer accounted for greater than 10% of our total revenue. We monitor market and regulatory changes regularly and make adjustments to our business if necessary.

Inflation. Inflationary factors may adversely affect our operating results. Although we do not believe that inflation has had a material impact on our financial position or results of operations to date, a high rate of inflation in the future may have an adverse effect on our ability to maintain current levels of expenses as a percentage of revenue if our revenue does not correspondingly increase with inflation.

Concentration of credit risk

Financial instruments, which potentially subject us to concentrations of credit risk, consist primarily of cash and cash equivalents. We maintain our cash and cash equivalents in bank and other depository accounts, which frequently may exceed federally insured limits. Our cash and cash equivalents as of April 30, 2019 were $329.3 million, of which $1 million was covered by federal depository insurance. We have not experienced any material losses in such accounts and believe we are not exposed to any significant credit risk with respect to our cash and cash equivalents. Our accounts receivable balance as of April 30, 2019 was $27.0 million. We have not experienced any significant write-offs to our accounts receivable and believe that we are not exposed to significant credit risk with respect to our accounts receivable. We continue to monitor our credit risk and place our cash, cash equivalents, and marketable securities with reputable financial institutions.

Interest rate risk

Custodial assets. As of April 30, 2019, we had custodial cash assets of approximately $6.4 billion. We have entered into depository agreements with financial institutions for our cash custodial assets. The contracted interest rates were negotiated at the time the depository agreements were executed. A significant reduction in prevailing market interest rates may make it difficult for us to continue to place custodial deposits at the current contracted rates.

Cash and cash equivalents. We consider all highly liquid investments purchased with an original maturity of three months or less to be unrestricted cash equivalents. Our unrestricted cash and cash equivalents are held in institutions in the U.S. and include deposits in a money market account that is unrestricted as to withdrawal or use.

As of April 30, 2019, we had unrestricted cash and cash equivalents of $329.3 million. Due to the short-term nature of these instruments, we believe that we do not have any material exposure to changes in the fair value of our cash and cash equivalents as a result of changes in interest rates.

Equity investment risk

Marketable equity securities. Our marketable equity securities are subject to a variety of market-related risks that could substantially reduce or increase the carrying value of our holdings. As of April 30, 2019, we had marketable equity securities of $77.4 million, comprised of investments in WageWorks, Inc. common stock. We are required to record all adjustments to the carrying value of our marketable equity securities through our condensed consolidated statements of operations and comprehensive income. As such, we anticipate volatility to our net income in future periods due to changes in fair value related to our investments in marketable equity securities.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act means controls and other procedures of a company that are designed to ensure the information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures included, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and 15d-15(d) of the Exchange Act that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Part II—Other Information

Item 1. Legal Proceedings

From time-to-time, we may be subject to various legal proceedings and claims that arise in the normal course of our business activities. As of the date of this Quarterly Report on Form 10-Q, we are not a party to any litigation whereby the outcome of such litigation, if determined adversely to us, would individually or in the aggregate be reasonably expected to have a material adverse effect on our results of operations, cash flows, financial position or brand.

Item 1A. Risk factors

The risks described in “Risk factors,” in our Annual Report on Form 10-K for the year ended January 31, 2019 could materially and adversely affect our business, financial condition and results of operations. There have been no material changes in such risks. These risk factors do not identify all risks that we face - our operations could also be affected by factors that are not presently known to us or that we currently consider to be immaterial to our operations.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) Unregistered Sale of Equity Securities

None.

(b) Use of Proceeds from Public Offering of Common Stock

On August 5, 2014, we closed our initial public offering of 10,465,000 shares of common stock sold by us. The offer and sale of all of the shares in the IPO were registered under the Securities Act pursuant to a registration statement on Form S-1 (File No. 333-196645), which was declared effective by the SEC on July 30, 2014. JP Morgan & Chase Co. and Wells Fargo acted as the lead underwriters. The public offering price of the shares sold in the offering was $14.00 per share. The total gross proceeds from the offering to us were $146.5 million. After deducting underwriting discounts and commissions of approximately $10.2 million and offering expenses payable by us of approximately $3.7 million, we received approximately $132.6 million. There has been no material change in the planned use of proceeds from our IPO as described in our final prospectus (dated July 30, 2014) filed with the SEC on August 1, 2014 pursuant to Rule 424(b) of the Securities Act. We paid a previously declared cash dividend of $50.0 million on shares of our common stock outstanding on August 4, 2014. In addition, we paid a cash dividend of $347,000 on shares of our outstanding series D-3 redeemable convertible preferred stock accrued through the date of conversion of such shares into common stock, which occurred on August 4, 2014. Other than the foregoing dividends, we made no payments directly or indirectly to (i) any of our officers or directors or their associates, (ii) any persons owning 10% or more of any class of our equity securities, or (iii) any of our affiliates.

On May 11, 2015, we closed our public offering of 972,500 shares of common stock sold by us. The offer and sale of all of the shares in the public offering were registered under the Securities Act pursuant to registration statements on Form S-1 (File Nos. 333-203190 and 333-203888), which became effective on May 5, 2015. Wells Fargo acted as the lead underwriter. The public offering price of the shares sold in the offering was $25.90 per share. Certain selling stockholders sold 3,455,000 shares of common stock in the offering, including 380,000 shares of common stock which were issued upon the exercise of outstanding options. The Company received net proceeds of approximately $23.5 million after deducting underwriting discounts and commissions of approximately $1.0 million and other offering expenses payable by the Company of approximately $688,000. The Company did not receive any proceeds from the sale of shares by the selling stockholders other than $222,000 representing the exercise price of the options that were exercised by certain selling stockholders in connection with the offering. We paid all of the expenses related to the registration and offering of the shares sold by the selling stockholders, other than underwriting discounts and commissions relating to those shares. Other than these expenses, we made no payments directly or indirectly to (i) any of our officers or directors or their associates, (ii) any persons owning 10% or more of any class of our equity securities, or (iii) any of our affiliates. There has been no material change in the planned use of proceeds from our public offering as described in our final prospectus (dated May 5, 2015) filed with the SEC on May 6, 2015 pursuant to Rule 424(b) of the Securities Act.

During the year ended January 31, 2016, the Company used funds received from the offerings to acquire the rights to be the custodian of the Bancorp and M&T Bank HSA portfolios for approximately $34.2 million and approximately $6.2 million, respectively.

During the year ended January 31, 2018, the Company used funds received from the offerings to acquire the rights to be custodian of two HSA portfolios for approximately $6.4 million and $8.0 million in cash, respectively, the assets of BenefitGuard LLC, a 401(k) provider that offers plan administrator and named fiduciary services for 401(k) employer sponsors, for approximately $2.9 million, and the rights to be the sole administrator of a portfolio of HSA Members for $3.3 million.

During the year ended January 31, 2019, the Company used funds received from the offerings to acquire the rights to be custodian of an HSA portfolio for approximately $1.2 million in cash.

The remainder of the funds received have been invested in registered money market accounts and marketable equity securities.

Item 6. Exhibits

		Incorporate by reference			
Exhibit no.	Description	Form	File No.	Exhibit	Filing Date
10.1+	First Amendment to Credit Agreement, dated March 8, 2019				
31.1+	Certification of the Principal Executive Officer Pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				
31.2+	Certification of the Principal Financial Officer Pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002				
32.1*#	Certification of the Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				
32.2*#	Certification of the Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002				
101.INS	XBRL Instance document				
101.SCH	XBRL Taxonomy schema linkbase document				
101.CAL	XBRL Taxonomy calculation linkbase document				
101.DEF	XBRL Taxonomy definition linkbase document				
101.LAB	XBRL Taxonomy labels linkbase document				
101.PRE	XBRL Taxonomy presentation linkbase document				

+ Filed herewith.

* Furnished herewith.

These certifications are not deemed filed with the Securities and Exchange Commission and are not to be incorporated by reference in any filing the registrant makes under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, irrespective of any general incorporation language in any filings.

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.

	HEALTHEQUITY, INC.	
Date: June 6, 2019	By:	/s/ Darcy Mott
	Name:	Darcy Mott
	Title:	Executive Vice President and Chief Financial Officer

EXECUTION COPY

AMENDMENT NO. 1 TO CREDIT AGREEMENT

This Amendment No. 1 to Credit Agreement, dated as of March 8, 2019 (this "Amendment") is among HealthEquity, Inc., a Delaware corporation (the "Borrower"), the financial institutions listed on the signature pages hereof as Lenders, and JPMorgan Chase Bank, N.A., as Administrative Agent (in such capacity, the "Administrative Agent"). Capitalized terms not otherwise defined herein having the definitions provided therefor in the Credit Agreement referenced below.

WHEREAS, the Borrower, the financial institutions from time to time party thereto as Lenders, and the Administrative Agent are parties to that certain Credit Agreement, dated as of September 30, 2015 (as amended, restated, supplemented or otherwise modified from time to time, the "Credit Agreement");

WHEREAS, the Borrower has requested that the Lenders and the Administrative Agent agree to certain amendments to the Credit Agreement; and

WHEREAS, the Borrower, the Lenders party hereto and the Administrative Agent have so agreed on the terms and conditions set forth herein;

NOW, THEREFORE, in consideration of the mutual agreements, provisions and covenants contained herein, the parties hereto agree as follows:

1. Amendment to the Credit Agreement. Subject to the satisfaction of the conditions precedent set forth in Section 2 below, Section 6.04(p) of the Credit Agreement is hereby amended to delete the amount "$25,000,000" set forth therein and to replace it with the amount "$65,000,000".

2. Conditions of Effectiveness. The effectiveness of this Amendment is subject to the conditions precedent that:

(a) the Administrative Agent shall have received counterparts to this Amendment duly executed by the Borrower, the Required Lenders and the Administrative Agent; and

(b) the Administrative Agent shall have received payment of the Administrative Agent's and its Affiliates' expenses (including reasonable fees and expenses of counsel for the Administrative Agent) in connection with this Amendment and the other Loan Documents.

3. Representations and Warranties of the Borrower. The Borrower hereby represents and warrants as follows:

(a) This Amendment and the Credit Agreement as amended hereby constitute legal, valid and binding obligations of the Borrower and are enforceable against the Borrower in accordance with their terms, subject to applicable bankruptcy, insolvency, reorganization, moratorium or other laws affecting creditors' rights generally and subject to general principles of equity, regardless of whether considered in a proceeding in equity or at law.

(b) As of the date hereof, after giving effect to the terms of this Amendment, (i) no Default or Event of Default has occurred and is continuing and (ii) the representations and warranties of the Borrower set forth in the Credit Agreement are true and correct in all material respects (provided that any representation and warranty that is qualified by Material Adverse Effect or other materiality qualifier is true and correct in all respects), except to the extent that such representations and warranties specifically refer to an earlier date, in which case they are true and correct in all material respects (provided that any representation and warranty that is qualified by Material Adverse Effect or other materiality qualifier is true and correct in all respects) as of such earlier date.

4. Reference to and Effect on the Credit Agreement.

(a) Upon the effectiveness hereof, each reference to the Credit Agreement in the Credit Agreement or any other Loan Document shall mean and be a reference to the Credit Agreement as amended hereby.

(b) Except as amended hereby, each Loan Document (including, without limitation, the Security Agreement) and all other documents, instruments and agreements executed and/or delivered in connection therewith shall remain in full force and effect and are hereby ratified and confirmed.

(c) Except with respect to the subject matter hereof, the execution, delivery and effectiveness of this Amendment shall not operate as a waiver of any right, power or remedy of the Administrative Agent or the Lenders, nor constitute a waiver of any provision of the Credit Agreement, the Loan Documents or any other documents, instruments and agreements executed and/or delivered in connection therewith.

(d) This Amendment is a "Loan Document" under (and as defined in) the Credit Agreement.

5. Governing Law. This Amendment shall be construed in accordance with and governed by the law of the State of New York.

6. Headings. Section headings in this Amendment are included herein for convenience of reference only are not part of this Amendment and shall not affect the construction of, or be taken into consideration in interpreting, this Amendment.

7. Counterparts. This Amendment may be executed in counterparts (and by different parties hereto on different counterparts), each of which shall constitute an original, but all of which when taken together shall constitute a single contract. Delivery of an executed counterpart of a signature page of this Amendment by telecopy, e-mailed .pdf or any other electronic means that reproduces an image of the actual executed signature page shall be effective as delivery of a manually executed counterpart of this Amendment.

[Signature Pages Follow]

IN WITNESS WHEREOF, this Amendment has been duly executed as of the day and year first above written.

HEALTHEQUITY, INC.
By:
Name:
Title:

JPMORGAN CHASE BANK, N.A., individually as a Lender and as Administrative Agent
By:____
Name:
Title:

WELLS FARGO BANK, N.A., as a Lender
By:____
Name:
Title:

SUNTRUST BANK, as a Lender
By:____
Name:
Title:

Exhibit 31.1

**Certification of Principal Executive Officer
Pursuant to
Exchange Act Rules 13a-14(a) and 15d-14(a),
as Adopted Pursuant to
Section 302 of Sarbanes-Oxley Act of 2002**

I, Jon Kessler, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of HealthEquity, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: June 6, 2019

By:	/s/ Jon Kessler
Name:	Jon Kessler
Title:	*Chief Executive Officer* *(Principal Executive Officer)*

Exhibit 31.2

Certification of Principal Financial Officer
pursuant to
Exchange Act Rules 13a-14(a) and 15d-14(a),
as adopted pursuant to
Section 302 of Sarbanes-Oxley Act of 2002

I, Darcy Mott, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of HealthEquity, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: June 6, 2019

By:	/s/ Darcy Mott
Name:	Darcy Mott
Title:	*Executive Vice President and Chief Financial Officer* *(Principal Financial Officer)*

Exhibit 32.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, Jon Kessler, the Chief Executive Officer (Principal Executive Officer) of HealthEquity, Inc. (the “Company”), hereby certify that, to my knowledge:

1. Our Quarterly Report on Form 10-Q for the quarter ended April 30, 2019 (the “Report”), of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: June 6, 2019

By:	/s/ Jon Kessler
Name:	Jon Kessler
Title:	*Chief Executive Officer* *(Principal Executive Officer)*

Exhibit 32.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, I, Darcy Mott, Executive Vice President and Chief Financial Officer (Principal Financial Officer) of HealthEquity, Inc. (the "Company"), hereby certify that, to my knowledge:

1. Our Quarterly Report on Form 10-Q for the quarter ended April 30, 2019 (the "Report"), of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: June 6, 2019

By:	/s/ Darcy Mott
Name:	Darcy Mott
Title:	*Executive Vice President and Chief Financial Officer (Principal Financial Officer)*