

MARKETAXESS HOLDINGS INC

Form 10-Q

July 27, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2017

or

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

For the transition period from _____ to _____

Commission File Number 001-34091

MARKETAXESS HOLDINGS INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

52-2230784
(IRS Employer
Identification No.)

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299 Park Avenue, 10th Floor New York, New York 10171
(Address of principal executive offices) (Zip Code)

(212) 813-6000

(Registrant's telephone number, including area code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an "emerging growth company". See definition of "large accelerated filer," "accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
Emerging growth company

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

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

As of July 26, 2017, the number of shares of the Registrant's voting common stock outstanding was 37,537,075.

MARKETAXESS HOLDINGS INC.

FORM 10-Q FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2017

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PART I — Financial Information

Item 1. Financial Statements

MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

(Unaudited)

	As of	
	June 30, 2017	December 31, 2016
	(In thousands, except share and per share amounts)	
ASSETS		
Cash and cash equivalents	\$ 128,143	\$ 168,243
Investments, at fair value	237,361	194,404
Accounts receivable, net of allowance of \$84 and \$82 as of		
June 30, 2017 and December 31, 2016, respectively	55,215	50,668
Goodwill and intangible assets, net of accumulated amortization	63,251	63,443
Furniture, equipment, leasehold improvements and capitalized		
software, net of accumulated depreciation and amortization	34,643	31,104
Prepaid expenses and other assets	21,058	11,618
Deferred tax assets, net	7,370	8,562
Total assets	\$ 547,041	\$ 528,042
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities		
Accrued employee compensation	\$ 23,080	\$ 34,783
Income and other tax liabilities	4,686	7,582
Deferred revenue	3,076	2,515
Accounts payable, accrued expenses and other liabilities	14,971	15,149
Total liabilities	45,813	60,029
Commitments and Contingencies (Note 10)	—	—
Stockholders' equity		
Preferred stock, \$0.001 par value, 4,855,000 shares authorized,		
no shares issued and outstanding as of June 30, 2017 and		
December 31, 2016	—	—

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Series A Preferred Stock, \$0.001 par value, 110,000 shares authorized, no shares issued and outstanding as of June 30, 2017 and December 31, 2016	—	—
Common stock voting, \$0.003 par value, 110,000,000 shares authorized, 40,242,102 shares and 40,106,360 shares issued and 37,554,123 shares and 37,543,775 shares outstanding as of June 30, 2017 and December 31, 2016, respectively	121	120
Common stock non-voting, \$0.003 par value, 10,000,000 shares authorized, no shares issued and outstanding as of June 30, 2017 and December 31, 2016	—	—
Additional paid-in capital	343,085	342,311
Treasury stock - Common stock voting, at cost, 2,687,979 and 2,562,585 shares as of June 30, 2017 and December 31, 2016, respectively	(141,477)	(117,330)
Retained earnings	310,777	255,140
Accumulated other comprehensive loss	(11,278)	(12,228)
Total stockholders' equity	501,228	468,013
Total liabilities and stockholders' equity	\$ 547,041	\$ 528,042

The accompanying notes are an integral part of these consolidated financial statements.

MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(In thousands, except share and per share amounts)			
Revenues				
Commissions	\$87,015	\$86,239	\$181,037	\$165,332
Information and post-trade services	8,272	8,586	16,088	16,365
Investment income	840	517	1,587	935
Other	1,187	1,297	2,493	2,580
Total revenues	97,314	96,639	201,205	185,212
Expenses				
Employee compensation and benefits	25,421	25,815	52,822	50,342
Depreciation and amortization	4,790	4,540	9,483	9,221
Technology and communications	4,822	4,277	9,407	8,581
Professional and consulting fees	4,086	4,245	8,365	8,107
Occupancy	1,422	1,225	2,826	2,386
Marketing and advertising	2,782	1,824	4,668	3,602
Clearing costs	1,517	1,953	2,844	3,719
General and administrative	2,901	2,209	5,610	4,333
Total expenses	47,741	46,088	96,025	90,291
Income before income taxes	49,573	50,551	105,180	94,921
Provision for income taxes	11,550	17,425	24,694	32,832
Net income	\$38,023	\$33,126	\$80,486	\$62,089
Net income per common share				
Basic	\$1.03	\$0.90	\$2.18	\$1.69
Diluted	\$1.00	\$0.88	\$2.11	\$1.65
Cash dividends declared per common share	\$0.33	\$0.26	\$0.66	\$0.52
Weighted average shares outstanding				
Basic	36,853	36,876	36,852	36,826
Diluted	38,077	37,748	38,095	37,710

The accompanying notes are an integral part of these consolidated financial statements.

MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
	(In thousands)			
Net income	\$38,023	\$33,126	\$80,486	\$62,089
Net cumulative translation adjustment and foreign currency exchange hedge, net of tax of \$(1,106), \$2,089, \$(1,634) and \$4,101, respectively	1,325	(1,804)	960	(4,041)
Net unrealized (loss) gain on securities available-for-sale, net of tax of \$(20), \$21, \$(6) and \$136, respectively	(33)	34	(10)	221
Comprehensive Income	\$39,315	\$31,356	\$81,436	\$58,269

The accompanying notes are an integral part of these consolidated financial statements.

MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(Unaudited)

	Common Stock Voting (In thousands)	Additional Paid-In Capital	Treasury Stock - Common Voting	Retained Earnings	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance at December 31, 2016	\$ 120	\$ 342,311	\$(117,330)	\$ 255,140	\$ (12,228)	\$ 468,013
Net income	—	—	—	80,486	—	80,486
Cumulative translation adjustment and foreign currency exchange hedge, net of tax	—	—	—	—	960	960
Unrealized net loss on securities available-for-sale, net of tax	—	—	—	—	(10)	(10)
Stock-based compensation	—	7,468	—	—	—	7,468
Exercise of stock options	1	1,337	—	—	—	1,338
Withholding tax payments on restricted stock vesting and stock option exercises	—	(8,111)	—	—	—	(8,111)
Repurchases of common stock	—	—	(24,147)	—	—	(24,147)
Cumulative effect of change in accounting for employee share-based payments	—	80	—	(51)	—	29
Cash dividend on common stock	—	—	—	(24,798)	—	(24,798)
Balance at June 30, 2017	\$ 121	\$ 343,085	\$(141,477)	\$ 310,777	\$ (11,278)	\$ 501,228

The accompanying notes are an integral part of these consolidated financial statements.

MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Six Months Ended June 30,	
	2017	2016
	(in thousands)	
Cash flows from operating activities		
Net income	\$80,486	\$62,089
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,483	9,221
Stock-based compensation expense	7,468	6,937
Deferred taxes	1,399	307
Other	740	9,219
Changes in operating assets and liabilities:		
(Increase) in accounts receivable	(4,669)	(22,677)
(Increase) in prepaid expenses and other assets	(9,407)	(3,574)
(Increase) in corporate debt trading investments	(111)	(72,396)
(Increase) in mutual funds held in rabbi trust	(1,620)	(1,284)
(Decrease) in accrued employee compensation	(11,703)	(9,084)
(Decrease) in income and other tax liabilities	(3,068)	(1,856)
Increase in deferred revenue	561	294
(Decrease) increase in accounts payable, accrued expenses and other liabilities	(441)	2,708
Net cash provided by (used in) operating activities	69,118	(20,096)
Cash flows from investing activities		
Available-for-sale investments		
Proceeds from maturities and sales	101,354	20,000
Purchases	(143,214)	(8,065)
Purchases of furniture, equipment and leasehold improvements	(5,777)	(3,904)
Capitalization of software development costs	(6,667)	(6,142)
Other	(33)	99
Net cash (used in) provided by investing activities	(54,337)	1,988
Cash flows from financing activities		
Cash dividend on common stock	(24,535)	(19,313)
Exercise of stock options	1,338	2,138
Withholding tax payments on restricted stock vesting and stock option exercises	(8,111)	(5,585)
Repurchases of common stock	(24,147)	(5,400)
Net cash (used in) financing activities	(55,455)	(28,160)
Effect of exchange rate changes on cash and cash equivalents	574	(185)
Cash and cash equivalents		
Net (decrease) for the period	(40,100)	(46,453)
Beginning of period	168,243	199,728

End of period

\$128,143 \$153,275

The accompanying notes are an integral part of these consolidated financial statements.

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Organization and Principal Business Activity

MarketAxess Holdings Inc. (the “Company” or “MarketAxess”) was incorporated in the State of Delaware on April 11, 2000. Through its subsidiaries, MarketAxess operates a leading electronic trading platform that enables fixed-income market participants to efficiently trade corporate bonds and other types of fixed-income instruments using MarketAxess' patented trading technology. Over 1,200 institutional investor and broker-dealer firms are active users of the MarketAxess trading platform, accessing global liquidity in U.S. high-grade corporate bonds, emerging markets and high-yield bonds, European bonds, U.S. agency bonds, municipal bonds, credit default swaps and other fixed-income securities. Through its Open Trading™ protocols, MarketAxess executes certain bond transactions between and among institutional investor and broker-dealer clients on a matched principal basis by serving as counterparty to both the buyer and the seller in trades which then settle through a third-party clearing broker. MarketAxess also offers a number of trading-related products and services, including: market data to assist clients with trading decisions; connectivity solutions that facilitate straight-through processing; technology services to optimize trading environments; and execution services for exchange-traded fund managers and other clients. Through its Trax® division, MarketAxess also offers a range of pre- and post-trade services, including trade matching, regulatory transaction reporting and market and reference data, across a range of fixed-income and other products.

2. Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of the Company and its subsidiaries. All intercompany transactions and balances have been eliminated. These consolidated financial statements are unaudited and should be read in conjunction with the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2016. The consolidated financial information as of December 31, 2016 has been derived from audited financial statements not included herein. These unaudited consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) and the rules and regulations of the U.S. Securities and Exchange Commission (“SEC”) with respect to Form 10-Q and reflect all adjustments that, in the opinion of management, are normal and recurring, and that are necessary for a fair statement of the results for the interim periods presented. In accordance with such rules and regulations, certain disclosures that are normally included in annual financial statements have been omitted. Interim period operating results may not be indicative of the operating results for a full year.

Accounting Pronouncements, Recently Adopted

Effective January 1, 2017, the Company adopted ASU 2016-09, “Improvements to Employee Share-Based Payment Accounting” (“ASU 2016-09”). ASU 2016-09 simplifies several aspects related to the accounting for share-based

payment transactions, including the accounting for income taxes, statutory tax withholding requirements and classification on the statement of cash flows. Beginning January 1, 2017, the tax effects related to share-based payments are recorded through the income tax provision and the Company has elected to account for forfeitures as they occur. The adoption of ASU 2016-09 will cause volatility in the Company's net income, effective tax rate and diluted earnings per share. The volatility in future periods will depend on the Company's stock price at the vest date for restricted stock awards or exercise date for stock options and the number of awards that vest or are exercised in each period. Under the new guidance, excess tax benefits from share-based compensation are included as an operating activity in the Company's Consolidated Statements of Cash Flows. Prior period cash flows have been adjusted to conform to the new presentation.

Accounting Pronouncements, Not Yet Adopted

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09") requiring an entity to recognize revenue for the transfer of goods or services equal to the amount that it expects to be entitled to receive for those goods or services. The standard can be implemented using either a retrospective or a modified retrospective method. In August 2015, the FASB deferred the effective date of the new revenue standard for periods beginning after December 15, 2016 to December 15, 2017, with early adoption permitted but not earlier than the original effective date. The ASU will be effective for the Company beginning January 1, 2018. The Company's implementation efforts include the identification of revenue streams within the scope of the guidance, the evaluation of certain revenue contracts underlying the revenue streams, discussions with our advisory consultants, and periodic discussions with our audit committee. The Company's evaluation of the impact of this accounting guidance is ongoing though we do not expect this guidance to have a material effect on the Company's Consolidated Financial Statements or disclosures.

In February 2016, the FASB issued ASU 2016-02, "Leases" ("ASU 2016-02") requiring lessees to recognize lease assets and lease liabilities on the balance sheet for those leases previously classified as operating leases. ASU 2016-02 will be effective for the Company beginning January 1, 2019 and early adoption is permitted and should be applied prospectively. The Company is currently evaluating the potential adoption impact and expects to recognize lease assets and lease liabilities in its Consolidated Statements of Financial Condition. The Company does not expect material changes to the recognition of operating lease expense in its Consolidated Statements of Operations.

In January 2017, the FASB issued ASU 2017-04, "Intangibles-Goodwill and Other" ("ASU 2017-04"). ASU 2017-04 simplifies the testing for goodwill impairment. The guidance will be effective for the Company beginning January 1, 2020 and early adoption is permitted and should be applied prospectively. The Company is currently in the process of assessing the impact of ASU 2017-04 on the Company's Consolidated Financial Statements.

Cash and Cash Equivalents

Cash and cash equivalents includes cash and money market instruments that are primarily maintained at one major global bank. Given this concentration, the Company is exposed to certain credit risk in relation to its deposits at this bank. The Company defines cash equivalents as short-term interest-bearing investments with maturities at the time of purchase of three months or less.

Investments

The Company determines the appropriate classification of securities at the time of purchase which are recorded in the Consolidated Statements of Financial Condition on the trade date. Securities are classified as available-for-sale or trading. The Company's available-for-sale investments are comprised of municipal bonds and investment grade corporate debt securities. Available-for-sale investments are carried at fair value with the unrealized gains or losses reported in accumulated other comprehensive loss in the Consolidated Statements of Financial Condition. Trading investments primarily include investment grade corporate debt securities and are carried at fair value, with realized and unrealized gains or losses included in other income in the Consolidated Statements of Operations.

The Company assesses whether an other-than-temporary impairment loss on the available-for-sale investments has occurred due to declines in fair value or other market conditions. The portion of an other-than-temporary impairment related to credit loss is recorded as a charge in the Consolidated Statements of Operations. The remainder is recognized in accumulated other comprehensive loss if the Company does not intend to sell the security and it is more likely than not that the Company will not be required to sell the security prior to recovery. No charges for other-than-temporary losses were recorded during the six months ended June 30, 2017 and 2016.

Fair Value Financial Instruments

Fair value is defined as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." A three-tiered hierarchy for determining fair value has been established that prioritizes inputs to valuation techniques used in fair value calculations. The three levels of inputs are defined as Level 1 (unadjusted quoted prices for identical assets or liabilities in active markets), Level 2 (inputs that are observable in the marketplace other than those inputs classified in Level 1) and Level 3 (inputs that are unobservable in the marketplace). The Company's financial assets and liabilities measured at fair value on a recurring basis consist of its money market funds, securities available-for-sale, trading securities and foreign currency forward contracts. All other financial instruments are short-term in nature and the carrying amount is reported on the Consolidated Statements of Financial Condition at approximate fair value.

Allowance for Doubtful Accounts

All accounts receivable have contractual maturities of less than one year and are derived from trading-related fees and commissions and revenues from products and services. The Company continually monitors collections and payments from its customers and maintains an allowance for doubtful accounts. The allowance for doubtful accounts is based upon the historical collection experience and specific collection issues that have been identified. Additions to the allowance for doubtful accounts are charged to bad debt expense, which is included in general and administrative expense in the Company's Consolidated Statements of Operations.

Depreciation and Amortization

Fixed assets are carried at cost less accumulated depreciation. The Company uses the straight-line method of depreciation over three to seven years. The Company amortizes leasehold improvements on a straight-line basis over the lesser of the life of the improvement or the remaining term of the lease.

Software Development Costs

The Company capitalizes certain costs associated with the development of internal use software, including among other items, employee compensation and related benefits and third party consulting costs at the point at which the conceptual formulation, design and testing of possible software project alternatives have been completed. Once the product is ready for its intended use, such costs are amortized on a straight-line basis over three years. The Company reviews the amounts capitalized for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable.

Cash Provided as Collateral

Cash is provided as collateral for broker-dealer clearing accounts. Cash provided as collateral is included in prepaid expenses and other assets in the Consolidated Statements of Financial Condition.

Foreign Currency Translation and Forward Contracts

Assets and liabilities denominated in foreign currencies are translated using exchange rates at the end of the period; revenues and expenses are translated at average monthly rates. Gains and losses on foreign currency translation are a component of accumulated other comprehensive loss in the Consolidated Statements of Financial Condition. Transaction gains and losses are recorded in general and administrative expense in the Consolidated Statements of Operations.

The Company enters into foreign currency forward contracts to hedge its net investment in its U.K. subsidiaries. Gains and losses on these transactions are included in accumulated other comprehensive loss in the Consolidated Statements of Financial Condition.

Revenue Recognition

The majority of the Company's revenues are derived from commissions for trades executed on its platform and distribution fees that are billed to its broker-dealer clients on a monthly basis. The Company also derives revenues from information and post-trade services, technology products and services, investment income and other income.

Commission revenue. Commissions are generally calculated as a percentage of the notional dollar volume of bonds traded on the platform and vary based on the type, size, yield and maturity of the bond traded. Under the Company's transaction fee plans, bonds that are more actively traded or that have shorter maturities are generally charged lower commissions, while bonds that are less actively traded or that have longer maturities generally command higher commissions. For trades that the Company executes between and among institutional investor and broker-dealer clients on a matched principal basis by serving as counterparty to both the buyer and the seller, the Company earns the commission through the difference in price between the two matched principal trades. Fee programs for certain products include distribution fees which are recognized monthly.

Information and post-trade services. The Company generates revenue from information services provided to our broker-dealer clients, institutional investor clients and data-only subscribers. Information services are invoiced

monthly, quarterly or annually. When billed in advance, revenues are deferred and recognized monthly on a straight-line basis. The Company also generates revenue from regulatory transaction reporting and trade matching services. Revenue is recognized in the period the services are provided.

Technology products and services. The Company generates revenues from professional consulting services, technology software licenses and maintenance and support services. Revenue from professional consulting services is recognized as services are performed and software license subscription revenue and maintenance and support services are recognized ratably over the contract period. Technology products and services revenue is reported in other income in the Consolidated Statements of Operations.

Stock-Based Compensation

The Company measures and recognizes compensation expense for all share-based payment awards based on their estimated fair values measured as of the grant date. These costs are recognized as an expense in the Consolidated Statements of Operations over the requisite service period, which is typically the vesting period, with an offsetting increase to additional paid-in capital. Effective upon the Company's adoption of ASU 2016-09, the Company accounts for forfeitures as they occur. Prior to the adoption of ASU 2016-09, expected forfeitures were included in determining share-based compensation expense.

Income Taxes

Income taxes are accounted for using the asset and liability method. Deferred income taxes reflect the net tax effects of temporary differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when such differences are expected to reverse. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is recognized against deferred tax assets if it is more likely than not that such assets will not be realized in future years. The Company recognizes interest and penalties related to unrecognized tax benefits in general and administrative expenses in the Consolidated Statements of Operations. Effective upon the Company's adoption of ASU 2016-09, all tax effects related to share-based payments are recorded through tax expense in the periods during which the awards are exercised or vest.

Business Combinations, Goodwill and Intangible Assets

Business combinations are accounted for under the purchase method of accounting. The total cost of an acquisition is allocated to the underlying net assets based on their respective estimated fair values. The excess of the purchase price over the estimated fair values of the net assets acquired is recorded as goodwill. Determining the fair value of certain assets acquired and liabilities assumed is judgmental in nature and often involves the use of significant estimates and assumptions, including assumptions with respect to future cash flows, discount rates, growth rates and asset lives.

The Company operates as a single reporting unit. Subsequent to an acquisition, goodwill no longer retains its identification with a particular acquisition, but instead becomes identifiable with the entire reporting unit. As a result, all of the fair value of the Company is available to support the value of goodwill. An impairment review of goodwill is performed on an annual basis, at year-end, or more frequently if circumstances change. Intangible assets with definite lives, including purchased technologies, customer relationships and other intangible assets, are amortized on a straight-line basis over their estimated useful lives, ranging from three to 15 years. Intangible assets are assessed for impairment when events or circumstances indicate the existence of a possible impairment.

Earnings Per Share

Basic earnings per share is computed by dividing the net income attributable to common stock by the weighted-average number of shares of common stock outstanding during the period. For purposes of computing diluted earnings per share, the weighted-average shares outstanding of common stock reflects the dilutive effect that could occur if convertible securities or other contracts to issue common stock were converted into or exercised for common stock.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities

at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Out-of-Period Adjustments

During the first quarter of 2016, the Company determined that it had incorrectly recorded deferred taxes for the cumulative translation adjustment (“CTA”) that arises from converting the local currency financial statements into U.S. dollars. Upon making a permanent reinvestment assertion on unremitted earnings from foreign subsidiaries effective January 1, 2013, the Company should have eliminated any deferred tax balances derived from the CTA balance. The Company also determined that gains and losses on the foreign currency forward contracts used to hedge the net investment in certain foreign subsidiaries were not appropriately considered as taxable income or expense in the consolidated tax returns. The Company assessed these errors and determined that they were not material to previous reporting periods. Therefore, the Company recorded these items as out-of-period adjustments in the three months ended March 31, 2016 by decreasing deferred tax assets by \$3.1 million, decreasing other comprehensive income by \$2.1 million and increasing prepaid expenses and other assets by \$1.0 million in the Consolidated Statements of Financial Condition.

Reclassifications

Certain reclassifications have been made to the prior period's Consolidated Financial Statements in order to conform to the current year presentation. Such reclassifications had no effect on previously reported net income.

3. Net Capital Requirements

Certain U.S. subsidiaries of the Company are registered as a broker-dealer or swap execution facility and therefore are subject to the applicable rules and regulations of the SEC and the Commodity Futures Trading Commission. These rules contain minimum net capital requirements, as defined in the applicable regulations, and also may require a significant part of the registrants' assets be kept in relatively liquid form. Certain of the Company's foreign subsidiaries are regulated by the Financial Conduct Authority in the U.K. or Ontario Securities Commission in Canada and must maintain financial resources, as defined in the applicable regulations, in excess of the applicable financial resources requirement. As of June 30, 2017, each of the Company's subsidiaries that are subject to these regulations had net capital or financial resources in excess of their minimum requirements. As of June 30, 2017, the Company's subsidiaries maintained aggregate net capital and financial resources that was \$136.0 million in excess of the required levels of \$10.5 million.

Each of the Company's U.S. and foreign regulated subsidiaries are subject to local regulations which generally prohibit repayment of borrowings from the Company or affiliates, paying cash dividends, making loans to the Company or affiliates or otherwise entering into transactions that result in a significant reduction in regulatory net capital or financial resources without prior notification to or approval from such regulated entity's principal regulator.

4. Fair Value Measurements

The following table summarizes the valuation of the Company's assets and liabilities measured at fair value as categorized based on the hierarchy described in Note 2.

	Level 1	Level 2	Level 3	Total
	(In thousands)			
As of June 30, 2017				
Money market funds	\$11,087	\$—	\$ —	\$11,087
Securities available-for-sale				
Corporate debt	—	160,080	—	160,080
Trading securities				
Corporate debt	—	74,332	—	74,332
Mutual funds held in rabbi trust	—	2,949	—	2,949
Foreign currency forward position	—	(2,346)	—	(2,346)
Total	\$11,087	\$235,015	\$ —	\$246,102
As of December 31, 2016				
Money market funds	\$58,573	\$—	\$ —	\$58,573

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Securities available-for-sale				
Corporate debt	—	118,870	—	118,870
Trading securities				
Corporate debt	—	74,207	—	74,207
Mutual funds held in rabbi trust	—	1,327	—	1,327
Foreign currency forward position	—	(266)	—	(266)
Total	\$58,573	\$194,138	\$ —	\$252,711

Securities classified within Level 2 were valued using a market approach utilizing prices and other relevant information generated by market transactions involving comparable assets. The foreign currency forward contracts are classified within Level 2 as the valuation inputs are based on quoted market prices. The mutual funds held in a rabbi trust represent investments associated with the deferred cash incentive plan (see Note 14). There were no financial assets classified within Level 3 during the six months ended June 30, 2017 and 2016.

The Company enters into foreign currency forward contracts to hedge the net investment in the Company's U.K. subsidiaries. The Company designates each foreign currency forward contract as a hedge and assesses the risk management objective and strategy, including identification of the hedging instrument, the hedged item and the risk exposure and how effectiveness is to be assessed prospectively and retrospectively. These hedges are for a one-month period and are used to limit exposure to foreign currency exchange rate fluctuations. The fair value of the asset is included in prepaid expenses and other assets and the fair value of the liability is included in accounts payable, accrued expenses and other liabilities in the Consolidated Statements of Financial Condition. Gains or losses on foreign currency forward contracts designated as hedges are included in accumulated other comprehensive loss in the Consolidated Statements of Financial Condition. A summary of the Company's foreign currency forward position is as follows:

	As of	
	June 30,	December 31,
	2017	2016
	(In thousands)	
Notional value	\$77,079	\$ 66,972
Fair value of notional	79,425	67,238
Fair value of the liability	\$(2,346)	\$ (266)

The following is a summary of the Company's investments:

	Gross	Gross
	unrealized	unrealized
Amortized cost	gains	losses