Manning & Napier, Inc.
Form 10-Q
November 08, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2018
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: 001-35355

MANNING & NAPIER, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	45-2609100 (I.R.S. Employer Identification No.)
290 Woodcliff Drive Fairport, New York (Address of principal executive offices)	14450 (Zip Code)

Registrant's telephone number, including area code:
(585) 325-6880

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 x 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes x 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 the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	x
		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 x

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

Class	Outstanding at November 5, 2018
Class A common stock, $0.01 par value per share	15,333,041

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In this Quarterly Report on Form 10-Q, “we”, “our”, “us”, the “Company”, “Manning & Napier” and the “Registrant” refers to Manning & Napier, Inc. and, unless the context otherwise requires, its consolidated direct and indirect subsidiaries and predecessors.

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PART I—FINANCIAL INFORMATION
Item 1. Financial Statements
Manning & Napier, Inc.
Consolidated Statements of Financial Condition
(In thousands, except share data)

	September 30, 2018 (unaudited)	December 31, 2017
Assets		
Cash and cash equivalents	$ 76,706	$ 78,262
Accounts receivable	13,276	15,337
Investment securities	69,993	70,404
Prepaid expenses and other assets	4,099	4,870
Total current assets	164,074	168,873
Property and equipment, net	5,478	5,407
Net deferred tax assets, non-current	22,275	23,298
Goodwill	4,829	4,829
Other long-term assets	3,992	2,773
Total assets	$ 200,648	$ 205,180
Liabilities		
Accounts payable	$ 1,828	$ 1,612
Accrued expenses and other liabilities	23,436	32,347
Deferred revenue	9,905	10,213
Total current liabilities	35,169	44,172
Other long-term liabilities	2,824	3,370
Amounts payable under tax receivable agreement, non-current	18,172	19,278
Total liabilities	56,165	66,820
Commitments and contingencies (Note 8)		
Shareholders' equity		
Class A common stock, $0.01 par value; 300,000,000 shares authorized; 15,333,041 and 15,039,347 shares issued and outstanding at September 30, 2018 and December 31, 2017, respectively	153	150
Additional paid-in capital	198,573	198,641
Retained deficit	(39,072)	(38,424)
Accumulated other comprehensive income (loss)	(103)	(86)
Total shareholders' equity	159,551	160,281
Noncontrolling interests	(15,068)	(21,921)
Total shareholders' equity and noncontrolling interests	144,483	138,360
Total liabilities, shareholders' equity and noncontrolling interests	$ 200,648	$ 205,180

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

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Manning & Napier, Inc.
Consolidated Statements of Operations
(In thousands, except share data)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Revenues				
Management Fees				
Separately managed accounts	$24,228	$ 27,182	$74,066	$ 84,651
Mutual funds and collective investment trusts	10,596	15,672	32,606	52,763
Distribution and shareholder servicing	2,974	3,473	9,185	9,867
Custodial services	2,021	1,925	5,838	6,282
Other revenue	729	586	2,197	2,296
Total revenue	40,548	48,838	123,892	155,859
Expenses				
Compensation and related costs	23,105	22,287	68,567	67,901
Distribution, servicing and custody expenses	4,518	6,920	13,801	21,415
Other operating costs	8,392	7,887	23,425	23,099
Total operating expenses	36,015	37,094	105,793	112,415
Operating income	4,533	11,744	18,099	43,444
Non-operating income (loss)				
Interest expense	(18)	(22)	(48)	(34)
Interest and dividend income	519	191	1,395	609
Change in liability under tax receivable agreement	113	(33)	404	(33)
Net gains (losses) on investments	105	711	(165)	2,293
Total non-operating income (loss)	719	847	1,586	2,835
Income before provision for income taxes	5,252	12,591	19,685	46,279
Provision for income taxes	274	739	1,244	3,324
Net income attributable to controlling and noncontrolling interests	4,978	11,852	18,441	42,955
Less: net income attributable to noncontrolling interests	4,198	10,331	15,681	37,852
Net income attributable to Manning & Napier, Inc.	$780	$ 1,521	$2,760	$ 5,103
Net income per share available to Class A common stock				
Basic	$0.05	$ 0.10	$0.18	$ 0.35
Diluted	$0.05	$ 0.10	$0.18	$ 0.35
Weighted average shares of Class A common stock outstanding				
Basic	14,740,541	14,249,347	14,583,570	14,135,288
Diluted	78,096,830	78,210,019	78,134,657	14,241,642
Cash dividends declared per share of Class A common stock	$0.08	$ 0.08	$0.24	$ 0.24

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

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Manning & Napier, Inc.
Consolidated Statements of Comprehensive Income
(In thousands)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
Net income attributable to controlling and noncontrolling interests	$4,978	$11,852	$18,441	$42,955
Net unrealized holding gain (loss) on investment securities, net of tax	55	(2)	(92)	(17)
Comprehensive income attributable to controlling and noncontrolling interests	$5,033	$11,850	$18,349	$42,938
Less: Comprehensive income attributable to noncontrolling interests	4,243	10,329	15,606	37,835
Comprehensive income attributable to Manning & Napier, Inc.	$790	$1,521	$2,743	$5,103

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

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Manning & Napier, Inc.
Consolidated Statements of Shareholders' Equity
(In thousands, except share data)
(Unaudited)

	Common Stock – class A		Common Stock – class B				Accumulated		
	Shares	Amount	Shares	Amount	Additional Paid in Capital	Retained Deficit	Accumulated Other Comprehensive Income (Loss)	Non Controlling Interests	Total
Balance—December 31, 2016	14,982,880	$ 150	1,000	$ —	$ 200,158	$ (37,383)	$ (13)	$ (28,434)	$ 134,478
Net income	—	—	—	—	—	5,103	—	37,852	42,955
Distributions to noncontrolling interests	—	—	—	—	—	—	—	(24,490)	(24,490)
Net changes in unrealized investment securities gains or losses	—	—	—	—	—	—	(17)	—	(17)
Common stock issued under equity compensation plan, net of forfeitures	56,467	—	—	—	—	—	—	—	—
Shares withheld to satisfy tax withholding requirements related to restricted stock units granted	—	—	—	—	(48)	—	—	(224)	(272)
Equity-based compensation	—	—	—	—	304	—	—	1,412	1,716
Dividends declared on Class A common stock - $0.24 per share	—	—	—	—	—	(3,426)	—	—	(3,426)
Impact of changes in ownership of Manning & Napier Group, LLC	—	—	—	—	(1,878)	—	—	(7,925)	(9,803)
Balance—September 30, 2017	15,039,347	$ 150	1,000	$ —	$ 198,536	$ (35,706)	$ (30)	$ (21,809)	$ 141,141
Balance—December 31, 2017	15,039,347	$ 150	—	$ —	$ 198,641	$ (38,424)	$ (86)	$ (21,921)	$ 138,360
Net income	—	—	—	—	—	2,760	—	15,681	18,441
Distributions to noncontrolling interests	—	—	—	—	—	—	—	(10,226)	(10,226)
Net changes in unrealized investment securities gains or losses	—	—	—	—	—	—	(17)	(75)	(92)
Common stock issued under equity compensation plan, net	293,694	3	—	—	(3)	—	—	—	—

of forfeitures									
Equity-based compensation	—	—	—	—	382	—	—	1,720	2,102
Dividends declared on Class A common stock - $0.24 per share	—	—	—	—	—	(3,674)	—	—	(3,674)
Cumulative effect of change in accounting principle, net of taxes (Note 3)	—	—	—	—	—	266	—	1,224	1,490
Impact of changes in ownership of Manning & Napier Group, LLC (Note 4)	—	—	—	—	(447)	—	—	(1,471)	(1,918)
Balance—September 30, 2018	15,333,041	$ 153	—	$ —	$ 198,573	$ (39,072)	$ (103)	$ (15,068)	$ 144,483

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

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Manning & Napier, Inc.
Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Nine months ended September 30, 2018	2017
Cash flows from operating activities:		
Net income attributable to controlling and noncontrolling interests	$18,441	$42,955
Adjustment to reconcile net income to net cash provided by operating activities:		
Equity-based compensation	2,102	1,716
Depreciation and amortization	1,333	1,328
Change in amounts payable under tax receivable agreement	(404)	33
Gain on sale of intangible assets	(2,575)	—
Net (gains) losses on investment securities	165	(2,293)
Deferred income taxes	954	2,342
(Increase) decrease in operating assets and increase (decrease) in operating liabilities:		
Accounts receivable	2,061	4,620
Prepaid expenses and other assets	1,203	1,907
Other long-term assets	(124)	—
Accounts payable	216	(138)
Accrued expenses and other liabilities	(9,400)	(10,599)
Deferred revenue	(308)	117
Other long-term liabilities	(687)	(671)
Net cash provided by operating activities	12,977	41,317
Cash flows from investing activities:		
Purchase of property and equipment	(1,369)	(1,057)
Sale of investments	2,533	12,871
Purchase of investments	(46,677)	(38,510)
Sale of intangible assets	2,575	—
Proceeds from maturity of investments	44,297	27,063
Acquisitions, net of cash received	—	320
Net cash provided by investing activities	1,359	687
Cash flows from financing activities:		
Distributions to noncontrolling interests	(10,226)	(24,490)
Dividends paid on Class A common stock	(3,650)	(4,802)
Payment of shares withheld to satisfy withholding requirements	—	(272)
Payment of capital lease obligations	(98)	(134)
Purchase of Class A units of Manning & Napier Group, LLC	(1,918)	(9,803)
Net cash used in financing activities	(15,892)	(39,501)
Net increase (decrease) in cash and cash equivalents	(1,556)	2,503
Cash and cash equivalents:		
Beginning of period	78,262	100,819
End of period	$76,706	$103,322

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

Manning & Napier, Inc.
Notes to Consolidated Financial Statements

Note 1—Organization and Nature of the Business

Manning & Napier, Inc. ("Manning & Napier", or the "Company") provides a broad range of investment solutions through separately managed accounts, mutual funds, and collective investment trusts, as well as a variety of consultative services that complement its investment process. Founded in 1970, the Company offers U.S. and non-U.S. equity, fixed income and a range of blended asset portfolios, such as life cycle funds and actively-managed exchange-traded fund ("ETF")-based portfolios. Headquartered in Fairport, New York, the Company serves a diversified client base of high-net-worth individuals and institutions, including 401(k) plans, pension plans, Taft-Hartley plans, endowments and foundations.

The Company is the sole managing member of Manning & Napier Group, LLC ("Manning & Napier Group"), a holding company for the investment management businesses conducted by its operating subsidiaries. The diagram below depicts the Company's organization structure as of September 30, 2018.

(1) The consolidated operating subsidiaries of Manning & Napier Group include Manning & Napier Advisors, LLC ("MNA"), Perspective Partners LLC, Manning & Napier Information Services, LLC, Manning & Napier Investor Services, Inc., Exeter Trust Company and Rainier Investment Management, LLC ("Rainier").

Note 2—Summary of Significant Accounting Policies

Critical Accounting Policies

The Company's critical accounting policies and estimates are disclosed in its Annual Report on Form 10-K for the year ended December 31, 2017. The Company believes that the disclosures herein are adequate so that the information presented is not misleading; however, these financial statements should be read in conjunction with the financial statements and the notes thereto in the Company's Annual Report on Form 10-K for the year ended December 31, 2017. The financial data for the interim periods may not necessarily be indicative of results for future interim periods or for the full year.

Changes to the Company's accounting policies as a result of adopting ASU 2014-09, Revenue from Contracts with Customers (Topic 606) are discussed under "Revenue", "Costs to Obtain a Contract" and "Reclassifications" below.

Revenue

Investment Management: Investment management fees are computed as a percentage of assets under management ("AUM"). The Company's performance obligation is a series of services that form part of a single obligation satisfied over time.

Separately managed accounts are paid in advance, typically for a semi-annual or quarterly period, or in arrears, typically for a monthly or quarterly period. When investment management fees are paid in advance, the Company defers the revenue as a contract liability and recognizes it over the applicable period. When investment management fees are paid in arrears, the Company estimates revenue and records a contract asset (accrued accounts receivable) based on AUM as of the most recent month end date.

Manning & Napier, Inc.
Notes to Consolidated Financial Statements (Continued)

Mutual funds and collective investment trust investment management revenue is calculated and earned daily based on AUM. Revenue is presented net of cash rebates and fees waived pursuant to contractual expense limitations of the funds. The Company also has agreements with third parties who provide recordkeeping and administrative services for employee benefit plans participating in the collective investment trusts. The Company is acting as an agent on behalf of the employee benefit plan sponsors, therefore, investment management revenue is recorded net of fees paid to third party service providers.

Distribution and shareholder servicing: The Company receives distribution and servicing fees for providing services to its affiliated mutual funds. Revenue is computed and earned daily based on a percentage of AUM. The performance obligation is a series of services that form part of a single performance obligation satisfied over time. The Company has agreements with third parties who provide distribution and administrative services for its mutual funds. The agreements are evaluated to determine whether revenue should be reported gross or net of payments to third-party service providers. The Company controls the services provided and acts as a principal in the relationship. Therefore, distribution and shareholder servicing revenue is recorded gross of fees paid to third parties.

Custodial services: Custodial service fees are calculated as a percentage of the client’s market value with additional fees charged for certain transactions. For the safeguarding and administrative services that are subject to a percentage of market value fee, the Company's performance obligation is a series of services that form part of a single obligation satisfied over time. Revenue for transactions assigned a stand-alone selling price is recognized in the period which the transaction is executed. Custodial service fees are billed monthly in arrears. The Company has agreements with third parties who provide safeguarding, recordkeeping and administrative services for their clients. The Company controls the services provided and acts as a principal in the relationship. Therefore, custodial service revenue is recorded gross of fees paid to third parties.

Costs to Obtain a Contract

Incremental first year commissions directly associated with new separate account and collective investment trust contracts are capitalized and amortized straight-line over the estimated customer contract period of 7 years for separate accounts and 3 years for collective investment trust contracts. Refer to Note 3 for further discussion.

Basis of Presentation

The accompanying unaudited consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) and related rules and regulations of the U.S. Securities and Exchange Commission (“SEC”) for interim financial reporting and include all adjustments, consisting only of normal recurring adjustments which are, in the opinion of management, necessary for a fair statement of the results for the interim period.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates or assumptions that affect the reported amounts and disclosures in the consolidated financial statements. Actual results could differ from these estimates or assumptions.

Reclassifications

The Company changed the presentation of revenue within its consolidated statements of operations for the three and nine months ended September 30, 2018. Revenue, previously reported as a single line item, has been disaggregated to present revenue by the various services the Company provides. Amounts for the comparative prior periods have been reclassified to conform to the current period presentation. These reclassifications had no impact on previously reported net income or financial position and do not represent a restatement of any previously published financial results.

For periods prior to and including December 31, 2017, the Company presented "Accounts receivable - affiliated mutual funds" on its consolidated statements of financial condition. Further disclosure regarding accounts receivable from affiliated mutual funds and the components of accounts receivable as of September 30, 2018 is included in "Accounts Receivable" in Note 3 of the notes to the consolidated financial statements. Amounts for the comparative prior fiscal year periods have been reclassified to conform to the current period presentation. These reclassifications had no impact on previously reported net income and do not represent a restatement of any previously published financial results.

Principles of Consolidation

The Company consolidates all majority-owned subsidiaries. In addition, as of September 30, 2018, Manning & Napier holds an economic interest of approximately 18.2% in Manning & Napier Group but, as managing member, controls all of the business and affairs of Manning & Napier Group. As a result, the Company consolidates the financial results of Manning & Napier Group and records a noncontrolling interest on its consolidated statements of financial condition with respect to the remaining economic interest in Manning & Napier Group held by Manning & Napier Group Holdings, LLC ("M&N Group Holdings") and Manning & Napier Capital Company, LLC ("MNCC").

All material intercompany transactions have been eliminated in consolidation.

In accordance with Accounting Standards Update ("ASU") 2015-02, Consolidation (Topic 810) – Amendments to the Consolidation Analysis, the determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design, a company's ability to direct the activities of the entity that most significantly impact the entity's economic performance, and whether a company is obligated to absorb losses or receive benefits that could potentially be significant to the entity. The standard also requires ongoing assessments of whether a company is the primary beneficiary of a variable interest entity ("VIE"). When utilizing the voting interest entity ("VOE") model, controlling financial interest is generally defined as majority ownership of voting interests.

The Company provides seed capital to its investment teams to develop new products and services for its clients. The original seed investment may be held in a separately managed account, comprised solely of the Company's investments, or within a mutual fund, where the Company's investments may represent all or only a portion of the total equity investment in the mutual fund. Pursuant to U.S. GAAP, the Company evaluates its investments in mutual funds on a regular basis and consolidates such mutual funds for which it holds a controlling financial interest. When no longer deemed to hold a controlling financial interest, the Company would deconsolidate the fund and classify the remaining investment as either an equity method investment or as trading securities, as applicable.

The Company serves as the investment adviser for Manning & Napier Fund, Inc. series of mutual funds (the "Fund"), Exeter Trust Company Collective Investment Trusts ("CIT") and Rainier Multiple Investment Trust. The Fund, CIT and Rainier Multiple Investment Trust are legal entities, the business and affairs of which are managed by their respective boards of directors. As a result, each of these entities is a VOE. The Company holds, in limited cases, direct investments in a mutual fund (which are made on the same terms as are available to other investors) and consolidates each of these entities where it has a controlling financial interest or a majority voting interest. The Company's investments in the Fund amounted to approximately $1.4 million as of September 30, 2018 and $2.6 million as of December 31, 2017. As of December 31, 2017, the Company maintained significant influence in one mutual fund, Manning & Napier Fund, Inc. Quality Equity Series, but did not maintain a controlling financial interest in the mutual fund, which was accounted for as an equity method investment. During the first quarter of 2018, the Manning & Napier Fund, Inc. Quality Equity Series liquidated and closed.

Cash and Cash Equivalents

The Company generally considers all highly liquid investments with original maturities of three months or less to be cash equivalents. Cash and cash equivalents are primarily held in operating accounts at major financial institutions and also in money market securities. Cash equivalents are stated at cost, which approximates market value due to the short-term maturity of these investments. The fair value of cash equivalents have been classified as Level 1 in accordance with the fair value hierarchy.

Investment Securities

Investment securities are classified as either trading, equity method investments or available-for-sale and are carried at fair value. Fair value is determined based on quoted market prices in active markets for identical or similar instruments.

Investment securities classified as trading consist of equity securities, fixed income securities, and investments in mutual funds for which the Company provides advisory services. Realized and unrealized gains and losses on trading securities are recorded in net gains (losses) on investments in the consolidated statements of operations. At September 30, 2018, trading securities consist solely of investments held by the Company to provide initial cash seeding for product development purposes.

Investments classified as equity method investments represent seed investments in which the Company owns between 20-50% of the outstanding voting interests in the affiliated fund or when it is determined that the Company is able to exercise significant influence but not control over the investments. If the seed investment results in significant influence, but not control, the investment will be accounted for as an equity method investment. When using the equity method, the Company recognizes its share of the investee's net income or loss for the period which is recorded in net gains (losses) on investments in the consolidated statements of operations.

Investment securities classified as available-for-sale consist of U.S. Treasury notes, corporate bonds and other short-term investments. Unrealized gains and losses on available-for-sale securities are excluded from earnings and are reported, net of deferred income tax, as a separate component of accumulated other comprehensive income in stockholders' equity until realized. The Company periodically reviews each individual security position that has an unrealized loss, or impairment, to determine if that impairment is other-than-temporary. If impairment is determined to be other-than-temporary, the carrying value of the security will be written down to fair value and the loss will be recognized in earnings. Realized gains and losses on sales of available-for-sale securities are computed on a specific identification basis and are recorded in net gains (losses) on investments in the consolidated statements of operations.

Manning & Napier, Inc.
Notes to Consolidated Financial Statements (Continued)

Property and Equipment

Property and equipment is presented net of accumulated depreciation of approximately $11.1 million and $11.4 million as of September 30, 2018 and December 31, 2017, respectively.

Goodwill and Intangible Assets

Goodwill represents the excess cost over the fair value of the identifiable net assets of acquired companies. Identifiable intangible assets generally represent the cost of client relationships and investment management agreements acquired as well as trademarks. Goodwill and indefinite-lived assets are tested for impairment annually or more frequently if events or circumstances indicate that the carrying value may not be recoverable. Intangible assets subject to amortization are tested for impairment whenever events or circumstances indicate that the carrying value may not be recoverable. Goodwill and intangible assets require significant management estimate and judgment, including the valuation and expected life determination in connection with the initial purchase price allocation and the ongoing evaluation for impairment.

On January 16, 2018, the Company sold a Rainier U.S. mutual fund to a third party for approximately $2.1 million, based on total assets under management on the closing date of approximately $0.3 billion. The carrying value of the intangible assets for client relationships associated with these products was zero as a result of the impairment loss recognized in 2016. During the first quarter of 2018, the Company recognized a gain of approximately $2.1 million for the sale of this fund, as included in other operating costs in the consolidated statements of operations.

Operating Segments

The Company operates in one segment, the investment management industry.

Recently Adopted Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). The revenue standard contains principals to determine the measurement of revenue and timing of recognition and also impacts the accounting for incremental costs to obtain a contract. The Company adopted the new standard on its effective date of January 1, 2018. Refer to Note 3 for further discussion regarding the impact of adoption of this standard.

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, which requires all equity investments to be measured at fair value with changes in the fair value recognized through net income. The guidance is effective on January 1, 2018. The Company's adoption of ASU 2016-01 on January 1, 2018 did not have a material impact on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments, to clarify guidance on the classification of certain cash receipts and cash payments in the statement of cash flows. The FASB issued the ASU with the intent of reducing diversity in practice regarding eight types of cash flows. The ASU is effective for annual reporting periods beginning after December 15, 2017, including interim periods within those annual reporting periods. The Company's adoption of ASU 2016-15 on January 1, 2018 did not have a material impact on its consolidated financial statements.

Recent Accounting Pronouncements Not Yet Adopted

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which is intended to increase transparency and comparability among organizations by recognizing all lease transactions (with terms in excess of 12 months) on the balance sheet as a lease liability and a right-of-use asset (as defined). In July 2018, the FASB issued ASU 2018-11, Leases - Targeted Improvements, which provides an optional transition method related to implementing the new lease standard. Under this new transition method, an entity initially applies the new leases standard at the adoption date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. The Company plans to adopt the new standard on January 1, 2019, using the optional transition method. The Company is currently evaluating the impact of adoption on its consolidated financial statements and its efforts are primarily focused on completing the identification of all leases, and quantifying the lease liability and right-of-use asset that will be recorded upon adoption.

In January 2017, the FASB issued ASU 2017-04, Intangibles - Goodwill and Other (Topic 350), Simplifying the Test for Goodwill Impairment, which simplifies the accounting for goodwill impairments by eliminating step two from the goodwill impairment test. The ASU requires goodwill impairments to be measured on the basis of the fair value of the reporting unit relative to the reporting unit's carrying amount rather than on the basis of the implied amount of goodwill relative to the goodwill balance of the reporting unit. The ASU is effective for annual and interim impairment tests for periods beginning after December 15, 2019. Early adoption is allowed for annual and interim impairment tests occurring after January 1, 2017. The Company is evaluating the effect of adopting this new accounting standard.

In February 2018, the FASB issued ASU No. 2018-02, Income Statement - Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. The ASU requires a reclassification

Manning & Napier, Inc.
Notes to Consolidated Financial Statements (Continued)

from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the newly enacted federal corporate income tax rate as a result of the Tax Cuts and Jobs Act. The amount of the reclassification is the difference between the historical corporate income tax rate and the newly enacted 21% corporate income tax rate. The ASU will be effective for fiscal years beginning after December 15, 2018, with early adoption permitted. The Company is evaluating the effect of adopting this new accounting standard.

Note 3—Revenue, Contract Assets and Contract Liabilities

Adoption of ASU 2014-09, Revenue from Contracts with Customers (Topic 606)

On January 1, 2018, the Company adopted Topic 606 using the modified retrospective approach with the cumulative effect of initial application recognized January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with the Company's historic accounting policies under Topic 605. The Company elected the practical expedient to adjust for active contracts that existed at the date of adoption. A reduction to opening shareholders' equity and noncontrolling interests of $1.5 million, net of taxes, as of January 1, 2018 has been recorded due to the cumulative impact of adopting Topic 606 related to the capitalization of incremental contract costs.

While there were no changes in the timing of revenue recognition, upon the adoption of Topic 606, the Company changed the presentation of certain revenue related costs on a gross versus net basis. The changes did not have a significant impact to total revenue, distribution, servicing and custody expenses and other operating costs, and had no impact on net income. Changes in the presentation of revenue related costs on a gross versus net basis are summarized below:

- Fees in the amount of $0.7 million and $2.0 million for the three and nine months ended September 30, 2018, respectively, due to third parties who provide record-keeping and administrative services for employee benefit plans participating in the Company's collective investment trusts are presented net as a reduction of mutual fund and collective investment trust revenue. Prior to the adoption of Topic 606 third party record-keeper fees associated with the Company's collective investment trusts were reported as distribution, servicing and custody expense.
- Fees in the amount of $0.5 million and $1.5 million for the three and nine months ended September 30, 2018, respectively, due to a third party who provides accounting and administrative services on behalf of the Company to its affiliated mutual fund are presented as other operating costs. Prior to the adoption of Topic 606, these fees were presented as a reduction of other revenue.
- Fees in the amount of $0.1 million and $0.4 million for the three and nine months ended September 30, 2018, respectively, due to a third party who provides safeguarding and administrative services on behalf of the Company are presented as distribution, servicing and custody expense. Prior to the adoption of Topic 606, these fees were presented as a reduction of custodial service revenue.

Disaggregated Revenue

The following table represents the Company’s separately managed account and mutual fund and collective investment trust investment management revenue by investment portfolio for the three and nine months ended September 30, 2018:

	Three months ended September 30, 2018			Nine months ended September 30, 2018		
	Separately managed accounts	Mutual funds and collective investment trusts	Total	Separately managed accounts	Mutual funds and collective investment trusts	Total
	(in thousands)					
Blended Asset	$17,864	$ 6,485	$24,349	$54,183	$ 19,635	$73,818
Equity	5,736	3,988	9,724	17,923	12,699	30,622
Fixed Income	628	123	751	1,960	272	2,232
Total	$24,228	$ 10,596	$34,824	$74,066	$ 32,606	$106,672

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Manning & Napier, Inc.
Notes to Consolidated Financial Statements (Continued)

Accounts Receivable

Accounts receivable as of September 30, 2018 and December 31, 2017 consisted of the following:

	September 30, 2018	December 31, 2017
	(in thousands)	
Accounts receivable - third parties	$6,747	$ 7,278
Accounts receivable - affiliated mutual funds and collective investment trusts	6,529	8,059
Total accounts receivable	$13,276	$ 15,337

Accounts receivable: Accounts receivable represents the Company's unconditional rights to consideration arising from its performance under separately managed account, mutual fund and collective investment trust, distribution and shareholder servicing, and custodial service contracts. Accounts receivable balances do not include an allowance for doubtful accounts nor has any significant bad debt expense attributable to accounts receivable been recorded during the three and nine months ended September 30, 2018 or 2017. Accounts receivable are stated at cost, which approximates net realizable value due to the short-term collection period.

Advisory and Distribution Agreements

The Company earns investment advisory fees, distribution fees and administrative service fees under agreements with affiliated mutual funds and collective investment trusts. Fees earned for advisory and distribution services provided were approximately $13.8 million and $42.6 million for the three and nine months ended September 30, 2018, respectively, and approximately $19.4 million and $64.6 million for the three and nine months ended September 30, 2017, respectively, which represents greater than 10% of revenue in each period. The following provides amounts due from affiliated mutual funds and collective investment trusts reported within accounts receivable in the consolidated statement of financial condition as of September 30, 2018 and December 31, 2017:

	September 30, 2018	December 31, 2017
	(in thousands)	
Affiliated mutual funds [(1)]	$5,021	$ 6,219
Affiliated collective investment trusts	1,508	1,840
Accounts receivable - affiliated mutual funds and collective investment trusts	$6,529	$ 8,059

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(1) December 31, 2017 balance includes $0.7 million of distribution and servicing fees receivable, which in the prior fiscal period were reflected in "Accounts Receivable". This amount was reclassified to conform to the current period presentation (Note 2).

Contract assets and liabilities

Accrued accounts receivable: Accrued accounts receivable represents the Company's contract asset for revenue that has been recognized in advance of billing separately managed account contracts. Consideration for the period billed in arrears is dependent on the client’s AUM on a future billing date and therefore conditional as of the reporting period end. During the nine months ended September 30, 2018, revenue was decreased by less than $0.1 million for changes in transaction price. Accrued accounts receivable of $0.3 million is reported within prepaid expenses and other assets in the consolidated statement of financial condition as of September 30, 2018.

Deferred revenue: Deferred revenue is recorded when consideration is received or unconditionally due in advance of providing services to the Company's customer. Revenue recognized for the nine months ended September 30, 2018 that was included in deferred revenue at the beginning of the period was approximately $9.9 million.

Costs to obtain a contract: Incremental first year commissions directly associated with new separate account and collective investment trust contracts are capitalized and amortized straight-line over an estimated customer contract period of 7 years for separate accounts and 3 years for collective investment trust contracts. The total net asset as of

September 30, 2018 was approximately $1.4 million. Amortization expense included in compensation and related costs totaled approximately $0.1 million and $0.4 million for the three and nine months ended September 30, 2018, respectively. An impairment loss of approximately $0.1 million was recognized for the nine months ended September 30, 2018 related to contract acquisition costs for client contracts that canceled during the period.

Manning & Napier, Inc.
Notes to Consolidated Financial Statements (Continued)

Note 4—Noncontrolling Interests

Manning & Napier holds an economic interest of approximately 18.2% in Manning & Napier Group, but as managing member controls all of the business and affairs of Manning & Napier Group. As a result, the Company consolidates the financial results of Manning & Napier Group and records a noncontrolling interest on its consolidated statement of financial condition with respect to the remaining approximately 81.8% aggregate economic interest in Manning & Napier Group held by M&N Group Holdings and MNCC. Net income attributable to noncontrolling interests on the statements of operations represents the portion of earnings attributable to the economic interest in Manning & Napier Group held by the noncontrolling interests.

The following provides a reconciliation from "Income before provision for income taxes" to "Net income attributable to Manning & Napier, Inc.":

	Three months ended September 30,		Nine months ended September 30,	
	2018	2017	2018	2017
	(in thousands)			
Income before provision for income taxes	$5,252	$12,591	$19,685	$46,279
Less: income (loss) before provision for income taxes of Manning & Napier, Inc. (1)	97	(51)	356	(45)
Income before provision for income taxes, as adjusted	5,155	12,642	19,329	46,324
Controlling interest percentage (2)	18.2 %	17.8 %	18.2 %	17.7 %
Net income attributable to controlling interest	941	2,261	3,514	8,189
Plus: income (loss) before provision for income taxes of Manning & Napier, Inc. (1)	97	(51)	356	(45)
Income before income taxes attributable to Manning & Napier, Inc.	1,038	2,210	3,870	8,144
Less: provision for income taxes of Manning & Napier, Inc. (3)	258	689	1,110	3,041
Net income attributable to Manning & Napier, Inc.	$780	$1,521	$2,760	$5,103

(1) Manning & Napier, Inc. incurs certain income or expenses that are only attributable to it and are therefore excluded from the net income attributable to noncontrolling interests.

(2) Income before provision for income taxes is allocated to the controlling interest based on the percentage of units of Manning & Napier Group held by Manning & Napier, Inc. The amount represents the Company's weighted ownership of Manning & Napier Group for the respective periods.

(3) The consolidated provision for income taxes is equal to the sum of (i) the provision for income taxes for entities other than Manning & Napier, Inc. and (ii) the provision for income taxes of Manning & Napier, Inc. which includes all U.S. federal and state income taxes. The consolidated provision for income taxes was $0.3 million and $1.2 million for the three and nine months ended September 30, 2018, respectively, and $0.7 million and $3.3 million for the three and nine months ended September 30, 2017, respectively.

As of September 30, 2018, a total of 63,349,721 units of Manning & Napier Group were held by the noncontrolling interests. Pursuant to the terms of the exchange agreement entered into at the time of the Company's initial public offering, such units may be exchangeable for shares of the Company's Class A common stock. For any units exchanged, the Company will (i) pay an amount of cash equal to the number of units exchanged multiplied by the 15-day value of one share of the Company's Class A common stock less a market discount and expected expenses, or, at the Company's election, (ii) issue shares of the Company's Class A common stock on a one-for-one basis, subject to customary adjustments. As the Company receives units of Manning & Napier Group that are exchanged, the Company's ownership of Manning & Napier Group will increase.

During the nine months ended September 30, 2018, M&N Group Holdings and MNCC exchanged a total of 581,344 Class A units of Manning & Napier Group for approximately $1.9 million in cash. Subsequent to the exchange the

Class A units were retired, resulting in an increase in Manning & Napier's ownership in Manning & Napier Group. In addition, during the nine months ended September 30, 2018, Class A common stock was issued under the Company's 2011 Equity Compensation Plan (the "Equity Plan") for which Manning & Napier, Inc. acquired an equivalent number of Class A units of Manning & Napier Group.

Manning & Napier, Inc.
Notes to Consolidated Financial Statements (Continued)

The following is the impact to the Company's equity ownership interest in Manning & Napier Group for the nine months ended September 30, 2018:

	Manning & Napier Group Class A Units Held			
	Manning & Napier	Noncontrolling Interests	Total	Manning & Napier Ownership %
As of December 31, 2017	13,873,042	63,931,065	77,804,107	17.8%
Class A Units issued	253,694	—	253,694	0.3%
Class A Units exchanged	—	(581,344)	(581,344)	0.1%
As of September 30, 2018	14,126,736	63,349,721	77,476,457	18.2%

Since the Company continues to have a controlling interest in Manning & Napier Group, the aforementioned changes in ownership of Manning & Napier Group were accounted for as equity transactions under ASC 810, Consolidation. Additional paid-in capital and noncontrolling interests in the Consolidated Statements of Financial Position are adjusted to reallocate the Company's historical equity to reflect the change in ownership of Manning & Napier Group.
At September 30, 2018 and December 31, 2017, the Company had recorded a total liability of $19.0 million and $21.8 million, respectively, representing the estimated payments due to the selling unit holders under the tax receivable agreement ("TRA") entered into between Manning & Napier and the other holders of Class A Units of Manning & Napier Group. Of these amounts, $0.8 million and $2.5 million was included in accrued expenses and other liabilities as of September 30, 2018 and December 31, 2017, respectively. The Company made payments pursuant to the TRA of approximately $2.5 million and $2.4 million during the nine months ended September 30, 2018 and 2017, respectively.
Obligations pursuant to the TRA are obligations of Manning & Napier. They do not impact the noncontrolling interests. These obligations are not income tax obligations. Furthermore, the TRA has no impact on the allocation of the provision for income taxes to the Company's net income.

Note 5—Investment Securities

The following represents the Company's investment securities holdings as of September 30, 2018 and December 31, 2017:

	September 30, 2018			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
	(in thousands)			
Available-for-sale securities				
Fixed income securities	$19,615	$ —	$ (152)	$19,463
U.S. Treasury notes	21,157	—	(36)	21,121
Short-term investments	22,575	—	—	22,575
				63,159
Trading securities				
Equity securities				5,396
Mutual funds				1,438
				6,834
Total investment securities				$69,993

Manning & Napier, Inc.
Notes to Consolidated Financial Statements (Continued)

	December 31, 2017			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
	(in thousands)			
Available-for-sale securities				
Fixed income securities	$19,589	$ —	$ (29)	$19,560
U.S. Treasury notes	22,428	—	(42)	22,386
Short-term investments	22,323	—	—	22,323
				64,269
Trading securities				
Equity securities				3,548
Mutual funds				1,409
				4,957
Equity method investments				