

WESTWOOD HOLDINGS GROUP INC  
Form 10-Q  
October 26, 2016

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

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FORM 10-Q

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Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the quarterly period ended September 30, 2016

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 1-31234

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WESTWOOD HOLDINGS GROUP, INC.  
(Exact name of registrant as specified in its charter)

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DELAWARE 75-2969997  
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

200 CRESCENT COURT, SUITE 1200 75201  
DALLAS, TEXAS (Address of principal executive office) (Zip Code)  
(214) 756-6900  
(Registrant's telephone number, including area code)

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(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Shares of common stock, par value \$0.01 per share, outstanding as of October 14, 2016: 8,799,797.

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WESTWOOD HOLDINGS GROUP, INC.  
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WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (In thousands, except par value and share amounts)  
 (Unaudited)

|   | September<br>30, 2016 | December<br>31, 2015 |
|---|-----------------------|----------------------|
| <b>ASSETS</b>   |                       |                      |
| Current Assets:   |                       |                      |
| Cash and cash equivalents   | \$30,692              | \$22,740             |
| Accounts receivable   | 22,810                | 19,618               |
| Investments, at fair value  | 49,849                | 72,320               |
| Other current assets  | 2,355                 | 2,926                |
| Total current assets  | 105,706               | 117,604              |
| Goodwill  | 27,144                | 27,144               |
| Deferred income taxes   | 10,950                | 11,042               |
| Intangible assets, net  | 21,884                | 23,354               |
| Property and equipment, net of accumulated depreciation of \$4,365 and \$3,687  | 4,014                 | 2,192                |
| Total assets  | \$169,698             | \$181,336            |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>   |                       |                      |
| Current Liabilities:  |                       |                      |
| Accounts payable and accrued liabilities  | \$3,498               | \$3,549              |
| Dividends payable   | 6,146                 | 5,749                |
| Compensation and benefits payable   | 13,357                | 20,264               |
| Contingent consideration  | —                     | 9,023                |
| Income taxes payable  | 2,482                 | 6,268                |
| Total current liabilities   | 25,483                | 44,853               |
| Accrued dividends   | 1,536                 | 1,699                |
| Deferred rent   | 1,827                 | 817                  |
| Total liabilities   | 28,846                | 47,369               |
| Commitments and contingencies (Note 12)   |                       |                      |
| Stockholders' Equity:   |                       |                      |
| Common stock, \$0.01 par value, authorized 25,000,000 shares, issued 9,830,612 and outstanding 8,830,021 shares at September 30, 2016; issued 9,425,309 and outstanding 8,630,687 shares at December 31, 2015 | 99                    | 94                   |
| Additional paid-in capital  | 159,615               | 143,797              |
| Treasury stock, at cost - 1,000,591 shares at September 30, 2016; 794,622 shares at December 31, 2015   | (44,863 )             | (34,910 )            |
| Accumulated other comprehensive loss  | (3,681 )              | (4,688 )             |
| Retained earnings   | 29,682                | 29,674               |
| Total stockholders' equity  | 140,852               | 133,967              |
| Total liabilities and stockholders' equity  | \$169,698             | \$181,336            |

See notes to condensed consolidated financial statements.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands, except per share data and share amounts)

(Unaudited)

|   | Three Months<br>Ended September<br>30,<br>2016 |           | Nine Months<br>Ended September<br>30,<br>2015 |           |
|---|--|-----------|---|-----------|
| <b>REVENUES:</b>                            |  |           |   |           |
| Advisory fees:                              |  |           |   |           |
| Asset-based                                 | \$23,447                                       | \$24,940  | \$67,928                                      | \$76,327  |
| Performance-based                           | 226  | —         | 635   | 2,206     |
| Trust fees                                  | 7,690  | 7,973     | 22,798  | 21,044    |
| Other, net                                  | 414  | (462)     | 568   | (207)     |
| Total revenues                              | 31,777   | 32,451    | 91,929  | 99,370    |
| <b>EXPENSES:</b>                            |  |           |   |           |
| Employee compensation and benefits          | 15,637   | 15,686    | 47,239  | 47,507    |
| Sales and marketing                         | 408  | 419       | 1,423   | 1,310     |
| Westwood mutual funds                       | 755  | 865       | 2,282   | 2,593     |
| Information technology                      | 1,874  | 1,626     | 6,039   | 4,085     |
| Professional services                       | 1,903  | 1,178     | 4,707   | 4,281     |
| General and administrative                  | 2,147  | 2,175     | 7,028   | 5,962     |
| Total expenses                              | 22,724   | 21,949    | 68,718  | 65,738    |
| Income before income taxes                  | 9,053  | 10,502    | 23,211  | 33,632    |
| Provision for income taxes                  | 3,166  | 3,489     | 8,141   | 11,214    |
| Net income                                  | \$5,887  | \$7,013   | \$15,070                                      | \$22,418  |
| Other comprehensive income (loss):          |  |           |   |           |
| Foreign currency translation adjustments    | (453)  | (1,386)   | 1,007   | (2,541)   |
| Total comprehensive income                  | \$5,434  | \$5,627   | \$16,077                                      | \$19,877  |
| <b>Earnings per share:</b>                  |  |           |   |           |
| Basic                                       | \$0.74   | \$0.90    | \$1.89  | \$2.90    |
| Diluted                                     | \$0.72   | \$0.87    | \$1.84  | \$2.78    |
| <b>Weighted average shares outstanding:</b> |  |           |   |           |
| Basic                                       | 7,995,680                                      | 7,808,239 | 7,952,938                                     | 7,737,608 |
| Diluted                                     | 8,179,956                                      | 8,037,080 | 8,212,468                                     | 8,076,055 |
| Cash dividends declared per share           | \$0.57   | \$0.50    | \$1.71  | \$1.50    |

See notes to condensed consolidated financial statements.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

For the Nine Months Ended September 30, 2016

(In thousands, except share amounts)

(Unaudited)

|   | Common Stock,<br>Par |        | Additional<br>Paid-In<br>Capital | Treasury<br>Stock | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) | Retained<br>Earnings | Total     |
|---|----------------------|--------|----------------------------------|-------------------|---|----------------------|-----------|
|   | Shares               | Amount |                                  |                   |   |                      |           |
| BALANCE, January 1, 2016  | 8,630,687            | \$ 94  | \$143,797                        | \$(34,910)        | \$ (4,688 )   | \$29,674             | \$133,967 |
| Net income  | —                    | —      | —                                | —                 | —   | 15,070               | 15,070    |
| Other comprehensive income                                      | —                    | —      | —                                | —                 | 1,007   | —                    | 1,007     |
| Issuance of common stock for acquisition                        | 80,253               | 1      | 3,733                            | —                 | —   | —                    | 3,734     |
| Issuance of restricted stock, net of forfeitures                | 325,050              | 4      | (4 )                             | —                 | —   | —                    | —         |
| Dividends declared  | —                    | —      | —                                | —                 | —   | (15,062 )            | (15,062 ) |
| Stock based compensation expense                                | —                    | —      | 12,164                           | —                 | —   | —                    | 12,164    |
| Reclassification of compensation liability to be paid in shares | —                    | —      | 167                              | —                 | —   | —                    | 167       |
| Tax deficiencies related to stock based compensation            | —                    | —      | (242 )                           | —                 | —   | —                    | (242 )    |
| Purchases of treasury stock                                     | (117,452 )           | —      | —                                | (5,629 )          | —   | —                    | (5,629 )  |
| Issuance of treasury stock under employee stock plans           | (10,474 )            | —      | —                                | (614 )            | —   | —                    | (614 )    |
| Restricted stock returned for payment of taxes                  | (78,043 )            | —      | —                                | (3,710 )          | —   | —                    | (3,710 )  |
| BALANCE, September 30, 2016                                     | 8,830,021            | \$ 99  | \$159,615                        | \$(44,863)        | \$ (3,681 )   | \$29,682             | \$140,852 |

See notes to condensed consolidated financial statements.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

|   | Nine Months<br>Ended September<br>30, |              |
|---|---------------------------------------|--------------|
|   | 2016                                  | 2015         |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>                                      |                                       |              |
| Net income  | \$ 15,070                             | \$ 22,418    |
| Adjustments to reconcile net income to net cash provided by operating activities: |                                       |              |
| Depreciation  | 732                                   | 606          |
| Amortization of intangible assets   | 1,470                                 | 951          |
| Unrealized gains on trading investments   | (676 )                                | 484          |
| Stock based compensation expense  | 12,164                                | 12,560       |
| Deferred income taxes   | 114                                   | (1,923 )     |
| Excess tax benefits from stock based compensation                                 | (165 )                                | (1,432 )     |
| Net sales of investments - trading securities                                     | 23,147                                | 22,679       |
| Other   | 275                                   | (3 )         |
| Change in operating assets and liabilities:                                       |                                       |              |
| Accounts receivable   | (2,711 )                              | (5,332 )     |
| Other current assets  | 900                                   | 236          |
| Accounts payable and accrued liabilities  | (82 )                                 | 537          |
| Compensation and benefits payable   | (6,758 )                              | (2,052 )     |
| Income taxes payable  | (4,637 )                              | 1,899        |
| Other liabilities   | 154                                   | (28 )        |
| Net cash provided by operating activities   | 38,997                                | 51,600       |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>                                      |                                       |              |
| Purchase of property and equipment  | (1,680 )                              | (704 )       |
| Acquisition of Woodway, net of cash acquired                                      | —                                     | (24,133 )    |
| Net cash used in investing activities   | (1,680 )                              | (24,837 )    |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>                                      |                                       |              |
| Purchases of treasury stock   | (5,629 )                              | —            |
| Purchase of treasury stock under employee stock plans                             | (614 )                                | (1,327 )     |
| Restricted stock returned for payment of taxes                                    | (3,710 )                              | (5,621 )     |
| Excess tax benefits from stock based compensation                                 | 165                                   | 1,432        |
| Payment of contingent consideration in acquisition                                | (5,562 )                              | —            |
| Cash dividends  | (14,827 )                             | (13,065 )    |
| Net cash used in financing activities   | (30,177 )                             | (18,581 )    |
| Effect of currency rate changes on cash   | 812                                   | (2,430 )     |
| <b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>                                  | <b>7,952</b>                          | <b>5,752</b> |
| Cash and cash equivalents, beginning of period                                    | 22,740                                | 18,131       |
| Cash and cash equivalents, end of period  | \$ 30,692                             | \$ 23,883    |
| Supplemental cash flow information:   |                                       |              |
| Cash paid during the period for income taxes                                      | \$ 12,632                             | \$ 11,664    |
| Common stock issued for acquisition   | \$ 3,734                              | \$ 5,292     |
| Non-cash accrued contingent consideration   | \$ —                                  | \$ 9,102     |
| Accrued dividends   | \$ 7,682                              | \$ 6,452     |
| Tenant allowance included in Property and equipment                               | \$ 1,128                              | \$ —         |

See notes to condensed consolidated financial statements.

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WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. DESCRIPTION OF THE BUSINESS

Westwood Holdings Group, Inc. (“Westwood”, the “Company”, “we”, “us” or “our”) was incorporated under the laws of the State of Delaware on December 12, 2001. Westwood provides investment management services to institutional investors, private wealth clients and financial intermediaries through its subsidiaries, Westwood Management Corp. and Westwood Advisors, LLC (together “Westwood Management”), Westwood Trust (“Westwood Trust”), and Westwood International Advisors Inc. (“Westwood International”). Revenue is largely dependent on the total value and composition of assets under management (“AUM”). Accordingly, fluctuations in financial markets and in the composition of AUM impact revenues and results of operations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying condensed consolidated financial statements are unaudited and are presented in accordance with the requirements for quarterly reports on Form 10-Q and consequently do not include all of the information and footnote disclosures required by accounting principles generally accepted in the United States of America (“GAAP”). The Company’s condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) necessary in the opinion of management to present fairly our interim financial position and results of operations and cash flows for the periods presented. The accompanying condensed consolidated financial statements are presented in accordance with GAAP and the rules and regulations of the Securities and Exchange Commission (“SEC”).

The accompanying unaudited condensed consolidated financial statements should be read in conjunction with our consolidated financial statements, and notes thereto, included in our Annual Report on Form 10-K for the year ended December 31, 2015. Operating results for the periods in these condensed consolidated financial statements are not necessarily indicative of the results for any future period. The accompanying condensed consolidated financial statements include the accounts of Westwood and its subsidiaries. All intercompany accounts and transactions have been eliminated upon consolidation.

Recent Accounting Pronouncements

In January 2016, the FASB issued ASU 2016-01, Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities. The main objective of this update is to enhance the reporting model for financial instruments to provide users of financial statements with more useful information for making decisions. The amendment addresses various aspects of recognition, measurement, presentation and disclosure of financial instruments. The amendment is effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. We are currently evaluating the impact that the application of ASU 2016-01 will have on our consolidated financial statements and disclosures and expect to adopt the new standard in the required time frame.

In February 2016, the FASB issued ASU 2016-02, Leases. ASU 2016-02 requires lessees to recognize a lease liability and a right-of-use asset for all leases at the commencement date, excluding short-term leases. The amendment is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application is permitted. We are currently evaluating the impact that the application of ASU 2016-02 will have on our consolidated financial statements and disclosures and expect to adopt the standard within the required time frame.

In March 2016, the FASB issued ASU 2016-08, Revenue from Contracts with Customers (Reporting Revenue Gross versus Net), which clarifies the implementation guidance on principal versus agent considerations in ASU 2014-09. The amendment is effective for fiscal years beginning after December 14, 2017, including interim reporting periods within that reporting year. We do not expect the adoption of ASU 2016-08 to have a material impact on our consolidated financial statements and disclosures and expect to adopt the standard within the required time frame.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)  
 (Unaudited)

In March 2016, the FASB issued ASU 2016-09, Compensation-Stock Compensation: Improvements to Employee Share-Based Payment Accounting. The purpose of the amendment is to simplify the accounting for share-based payment transactions, and includes changes to the accounting for the classification of awards as either equity or liabilities, classification of certain share-based payment items on the statement of cash flows, the accounting for forfeitures and certain income tax consequences. The amendment is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early adoption is permitted. Amendments related to the presentation of employee taxes paid on the statement of cash flows should be applied retrospectively. Amendments requiring recognition of excess tax benefits and tax deficiencies in the income statement and the practical expedient for estimating expected term should be applied prospectively. An entity may elect to apply the amendments related to the presentation of tax benefits on the statement of cash flows using either a prospective or retrospective transition method. We are currently evaluating the impact that the application of ASU 2016-09 will have on our consolidated financial statements and disclosures and expect to adopt the new standard within the required time frame.

In April 2016, the FASB issued ASU 2016-10, Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing, which clarifies the guidance related to identifying performance obligations and the licensing guidance in ASU 2014-09. The amendment is effective for fiscal years beginning after December 14, 2017, including interim reporting periods within that reporting year. We do not expect the adoption of ASU 2016-10 to have a material impact on our consolidated financial statements and disclosures and expect to adopt the standard within the required time frame.

In August 2016, the FASB issued ASU 2016-15, Classification of Certain Cash Receipts and Cash Payments. The amendment addresses eight classification issues related to the statement of cash flows, including debt prepayment or debt extinguishment costs, settlement of zero-coupon bonds, contingent consideration payments made after a business combination, proceeds from settlements of insurance claims, proceeds from settlements of corporate-owned life insurance policies, distributions received from equity method investees, beneficial interests in securitization transactions, and classification of separately identifiable cash flows. Adoption should be applied using the retrospective transition method. Early adoption is permitted. The amendment is effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2017. We do not expect the adoption of ASU 2016-08 to have a material impact on our consolidated financial statements and disclosures and expect to adopt the standard within the required time frame.

### 3. EARNINGS PER SHARE

Basic earnings per common share is computed by dividing net income available to common stockholders by the weighted average number of shares outstanding for the applicable period. Diluted earnings per share is computed based on the weighted average number of shares outstanding plus the effect of any dilutive shares of restricted stock granted to employees and non-employee directors. There were approximately 2,453 and 306 anti-dilutive restricted shares for the three months ended September 30, 2016 and 2015, respectively, and 2,301 and 4,750 anti-dilutive restricted shares for the nine months ended September 30, 2016 and 2015, respectively.

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share and share amounts):

|   | Three Months    |           | Nine Months     |           |
|---|-----------------|-----------|-----------------|-----------|
|   | Ended September |           | Ended September |           |
|   | 30,             | 30,       | 30,             | 30,       |
|   | 2016            | 2015      | 2016            | 2015      |
| Net income  | \$5,887         | \$ 7,013  | \$ 15,070       | \$ 22,418 |
| Weighted average shares outstanding - basic               | 7,995,680       | 8,082,239 | 7,952,938       | 7,737,608 |
| Dilutive potential shares from unvested restricted shares | 184,276         | 185,139   | 259,530         | 316,253   |
| Dilutive potential shares from contingent consideration   | —               | 43,702    | —               | 22,194    |
| Weighted average shares outstanding - diluted             | 8,179,956       | 8,307,080 | 8,212,468       | 8,076,055 |

Earnings per share:

|         |        |         |        |         |
|---------|--------|---------|--------|---------|
| Basic   | \$0.74 | \$ 0.90 | \$1.89 | \$ 2.90 |
| Diluted | \$0.72 | \$ 0.87 | \$1.84 | \$ 2.78 |

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WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)  
 (Unaudited)

#### 4. INVESTMENTS

Investment balances are presented in the table below (in thousands). All investments are carried at fair value and are accounted for as trading securities.

|   | Cost     | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Estimated<br>Market<br>Value |
|---|----------|------------------------------|-------------------------------|------------------------------|
| September 30, 2016:                               |          |                              |                               |                              |
| U.S. Government and Government agency obligations | \$25,209 | \$ 38                        | \$ —                          | \$ 25,247                    |
| Money market funds                                | 12,421   | —                            | —                             | 12,421                       |
| Equity funds                                      | 12,027   | 233                          | (79 )                         | 12,181                       |
| Marketable securities                             | \$49,657 | \$ 271                       | \$ (79 )                      | \$ 49,849                    |
| December 31, 2015:                                |          |                              |                               |                              |
| U.S. Government and Government agency obligations | \$50,972 | \$ 15                        | \$ (15 )                      | \$ 50,972                    |
| Money market funds                                | 9,179    | —                            | —                             | 9,179                        |
| Equity funds                                      | 12,653   | —                            | (484 )                        | 12,169                       |
| Marketable securities                             | \$72,804 | \$ 15                        | \$ (499 )                     | \$ 72,320                    |

As of September 30, 2016 and December 31, 2015, \$11.1 million and \$10.7 million in corporate funds, respectively, were invested in Westwood Funds®, Westwood Common Trust Funds and the UCITS Fund. See Note 8 “Variable Interest Entities.”

#### 5. FAIR VALUE MEASUREMENTS

We determine estimated fair values for our financial instruments using available information. The fair value amounts discussed in our condensed consolidated financial statements are not necessarily indicative of either amounts realizable upon disposition of these instruments or our intent or ability to dispose of these assets. The estimated fair value of cash and cash equivalents, accounts receivable, other current assets, accounts payable and accrued liabilities, dividends payable, compensation and benefits payable and income taxes payable approximates their carrying value due to their short-term maturities. The carrying amount of investments designated as “trading” securities, primarily U.S. Government and Government agency obligations, money market funds, Westwood Funds® mutual funds, the UCITS Fund and Westwood Trust common trust fund shares, equals their fair value based on prices quoted in active markets and, with respect to common trust funds, the net asset value of the shares held as reported by each fund. Market values of our money market holdings generally do not fluctuate. The fair value of contingent consideration related to the Woodway acquisition was categorized as a level 3 liability, as the measurement of the Earn-Out Amount was based primarily on significant inputs not observable in the market. For more information about the Woodway acquisition, see Note 6 “Acquisitions, Goodwill and Other Intangibles”.

ASC 820, Fair Value Measurements and Disclosures, defines fair value, establishes a framework for measuring fair value and requires additional disclosures regarding certain fair value measurements. ASC 820 establishes a three-tier hierarchy for measuring fair value, as follows:

- Level 1 – quoted market prices in active markets for identical assets
- Level 2 – inputs other than quoted prices that are directly or indirectly observable
- Level 3 – significant unobservable inputs where there is little or no market activity

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)  
 (Unaudited)

The following table summarizes the values of our assets and liabilities as of the dates indicated within the fair value hierarchy (in thousands).

|                                   | Level 1  | Level<br>2 | Level 3   | Total    |
|-----------------------------------|----------|------------|-----------|----------|
| As of September 30, 2016:         |          |            |           |          |
| Investments in trading securities | \$46,697 | \$3,152    | \$—       | \$49,849 |
| Total financial instruments       | \$46,697 | \$3,152    | \$—       | \$49,849 |
| As of December 31, 2015:          |          |            |           |          |
| Investments in trading securities | \$69,260 | \$3,060    | \$—       | \$72,320 |
| Contingent consideration          | —        | —          | (9,023 )  | (9,023 ) |
| Total financial instruments       | \$69,260 | \$3,060    | \$(9,023) | \$63,297 |

Investments categorized as level 2 assets consist of investments in common trust funds sponsored by Westwood Trust. Common trust funds are private investment vehicles comprised of commingled investments held in trusts that are valued using the Net Asset Value ("NAV") calculated by us as administrator of the funds. The NAV is calculated using indirectly observed inputs, as the unit price is based on the market value of the underlying investments traded on an active market. We can make withdrawals from the common trust funds on a daily basis as needed for liquidity and there are no restrictions on redemption as of September 30, 2016.

Contingent consideration categorized as a level 3 liability is related to the acquisition of Woodway. As of the acquisition date, the Company estimated that the Earn-Out Amount would be \$9.1 million, based on then existing facts and circumstances.

For the period subsequent to the initial measurement of the contingent consideration, changes in the fair value of the contingent consideration are recorded in "Other, net" on the condensed consolidated statements of comprehensive income. During the first quarter of 2016, the Company revised its estimate of the Earn-Out Amount to \$9.3 million based on the actual revenues from the post-closing business of Woodway for the twelve month period ended March 31, 2016 and recorded a charge of \$286,000 in "Other, net" on the condensed consolidated statements of comprehensive income. During the second quarter of 2016, the Company finalized the Earn-Out Amount and recorded income of \$13,000 in "Other, net" on the condensed consolidated statements of comprehensive income.

The following table provides a reconciliation of the beginning and ending balances of items measured at fair value on a recurring basis that used significant unobservable inputs (in thousands):

|                                      | Contingent<br>Consideration |
|--------------------------------------|-----------------------------|
| Beginning balance, December 31, 2015 | \$ 9,023                    |
| Change in carrying value             | 273                         |
| Payment of contingent consideration  | (9,296 )                    |
| Ending balance, September 30, 2016   | \$ —                        |

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)  
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## 6. ACQUISITIONS, GOODWILL AND OTHER INTANGIBLE ASSETS

### Acquisition of Woodway Financial Advisors

Westwood completed the acquisition of Woodway Financial Advisors, a Trust Company ("Woodway"), on April 1, 2015 (the "Merger"). The total Merger consideration consisted of (i) \$30.6 million in cash and stock, as described below, and (ii) contingent consideration equal to the annualized revenue from the post-closing business of Woodway for the twelve-month period ending March 31, 2016 (the "Earn-Out Period"), adjusted for certain clients or accounts that have terminated, and capped at \$15 million (the "Earn-Out Amount"). The final Earn-Out Amount of \$9.3 million (discounted from \$10.1 million due to certain required holding periods on the Westwood shares) was paid 54.84% in cash and 45.16% in shares of Westwood's common stock, valued using the average closing price during the last 30 calendar days of the Earn-Out Period. In relation to the Merger, Westwood entered into employment agreements with certain Woodway employees, which, among other things, provided for specified compensation and benefits for the related employees.

The Merger consideration of \$39.7 million consisted of (i) closing date consideration of \$25.3 million paid in cash and issuance of 109,712 shares of Westwood common stock, valued at \$5.3 million (discounted from \$6.7 million due to certain required holding periods), and (ii) contingent consideration of \$9.1 million, based on estimates and assumptions on the closing date of the acquisition, to be paid no later than 75 calendar days after the last day of the Earn-Out Period. The estimated fair value of the Earn-Out Amount was determined by using overall revenue growth projections combined with existing customer base lost revenue projections, both discounted and probability-weighted. The fair value measurement of the Earn-Out Amount was based primarily on significant inputs not observable in the market and thus represents a level 3 measurement as defined in ASC 820. See further discussion in Note 5 "Fair Value Measurements."

The acquisition of Woodway was accounted for using the acquisition method of accounting. Accordingly, the purchase price was allocated to the tangible and intangible assets acquired and the liabilities assumed based on their estimated fair values as of the acquisition date. As of September 30, 2016, consideration of \$39.7 million has been allocated using Woodway's historical balance sheet at March 31, 2015 based on valuations of acquired assets and assumed liabilities in connection with the acquisition.

The allocation of the purchase price is as follows (in thousands):

|  |          |
|--|----------|
| Cash and cash equivalents                | \$ 1,205 |
| Accounts receivable                      | 936      |
| Other current assets                     | 253      |
| Goodwill <sup>(i)</sup>                  | 15,889   |
| Identifiable intangibles <sup>(ii)</sup> | 21,334   |
| Property and equipment                   | 197      |
| Accounts payable and accrued liabilities | (61 )    |
| Income tax payable                       | (20 )    |
| Purchase price                           | \$39,733 |

(i) The excess of the purchase price over the fair value amounts assigned to assets acquired and liabilities assumed represents the goodwill amount resulting from the acquisition.

(ii) The fair value of the acquired identifiable intangibles consists of (in thousands, except useful lives):

| Intangible Asset       | Fair Value | Estimated Useful Lives |
|------------------------|------------|------------------------|
| Client relationships   | \$20,391   | 15 years               |
| Non-compete agreements | 257        | 3 years                |
| Trade name             | 686        | 5 years                |

At the time of the acquisition, the Company believed that its enhanced market position and future growth potential were the primary factors that contributed to a total purchase price that resulted in the recognition of goodwill. As of

September 30, 2016, \$15.9 million of the goodwill arising from the acquisition is expected to be deductible for tax purposes.

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WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
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We incurred transaction costs of \$1.1 million related to the Woodway acquisition. Approximately \$732,000 of those costs are included in "Professional services" on our condensed consolidated statements of comprehensive income for the nine months ended September 30, 2015.

Our consolidated results for the three months ended September 30, 2016 included "Total revenues" and "Net income" attributable to Woodway of \$2.5 million and \$700,000, respectively. Our consolidated results for the nine months ended September 30, 2016 included "Total revenues" and "Net income" attributable to Woodway of \$7.1 million and \$1.7 million, respectively.

Pro Forma Financial Information

The following unaudited pro forma results of operations for the three and nine months ended September 30, 2016 and 2015 assume that the Woodway acquisition had occurred on January 1, 2015, after giving effect to acquisition accounting adjustments relating to amortization of the valued intangible assets and to record additional compensation costs related to employment contracts entered into as a result of the acquisition. These unaudited pro forma results exclude one-time, non-recurring costs related to the acquisition, including transaction costs. This unaudited pro forma information should not be relied upon as being necessarily indicative of the historical results that would have been obtained if the Merger had actually occurred on those dates, nor of the results that may be obtained in the future.

|                | Three Months    |          | Nine Months     |           |
|----------------|-----------------|----------|-----------------|-----------|
|                | Ended September |          | Ended September |           |
|                | 30,             | 30,      | 30,             | 30,       |
|                | 2016            | 2015     | 2016            | 2015      |
|                | (in thousands)  |          |                 |           |
| Total revenues | \$31,777        | \$32,451 | \$91,929        | \$102,063 |
| Net income     | \$5,887         | \$7,013  | \$15,070        | \$23,328  |

Goodwill

Goodwill represents the excess of the cost of acquired assets over the fair value of the underlying identifiable assets at the date of acquisition. Goodwill is not amortized but is tested for impairment at least annually. We completed our annual goodwill impairment assessment during the third quarter of 2016 and determined that no impairment loss was required. No impairments were recorded during the three or nine months ended September 30, 2016 or 2015.

Other Intangible Assets

Our intangible assets represent the acquisition date fair value of acquired client relationships, trade names and non-compete agreements and internally developed software and are reflected net of amortization. In valuing these assets, we made significant estimates regarding their useful lives, growth rates and potential attrition. We periodically review intangible assets for events or circumstances that would indicate impairment. There have been no impairments on intangible assets recorded during the three or nine months ended September 30, 2016 or 2015.



WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)  
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## 7. BALANCE SHEET COMPONENTS

### Property and Equipment

The following table reflects information about our property and equipment as of September 30, 2016 and December 31, 2015 (in thousands):

|  | As of<br>September<br>30, 2016 | As of<br>December<br>31, 2015 |
|--|--------------------------------|-------------------------------|
| Leasehold improvements                 | \$ 3,647                       | \$ 1,728                      |
| Furniture and fixtures                 | 2,216                          | 1,804                         |
| Computer hardware and office equipment | 2,283                          | 2,116                         |
| Construction in progress               | 233                            | 231                           |
| Accumulated depreciation               | (4,365 )                       | (3,687 )                      |
| Net property and equipment             | \$ 4,014                       | \$ 2,192                      |

### Stockholders' Equity

#### Accumulated Other Comprehensive Loss

The components of accumulated other comprehensive loss were as follows (in thousands):

|   | As of<br>September<br>30, 2016 | As of<br>December<br>31, 2015 |
|---|--------------------------------|-------------------------------|
| Foreign currency translation adjustment | \$ (3,681 )                    | \$ (4,688 )                   |
| Accumulated other comprehensive loss    | \$ (3,681 )                    | \$ (4,688 )                   |

### Share Repurchase Program

On July 20, 2012, our Board of Directors authorized the repurchase of up to \$10 million of our outstanding common stock on the open market or in privately negotiated transactions. The share repurchase program has no expiration date and may be discontinued at any time by the Board of Directors. In July 2016, Westwood's Board of Directors authorized an additional \$5.0 million of repurchases under the share repurchase program. As of September 30, 2016, approximately \$9.4 million remained available under the share repurchase program.

Between July 1, 2016 and September 30, 2016, under our share repurchase program the Company repurchased 24,199 shares of our common stock at an average price of \$49.92, including commissions, at an aggregate purchase price of \$1.2 million. Between January 1, 2016 and September 30, 2016, under our share repurchase program the Company repurchased 117,452 shares of our common stock at an average price of \$47.93, including commissions, at an aggregate purchase price of \$5.6 million.

## 8. VARIABLE INTEREST ENTITIES

Westwood Trust sponsors common trust funds (“CTFs”) for its clients. These funds allow clients to commingle assets to achieve economies of scale. Westwood International and Westwood Management provide investment advisory services to Westwood Investment Funds PLC (the “UCITS Fund”), which was authorized on June 18, 2013 by the Central Bank of Ireland pursuant to the European Communities (Undertakings for Collective Investment in Transferable Securities) Regulations 2011 (“UCITS”), and which is an umbrella-type, open-ended self-managed investment company domiciled in Ireland. Westwood Management provides investment advisory services to the Westwood Funds®, a family of mutual funds, and one collective investment trust (“CITs”). Some clients of Westwood Management hold their investments in one or more of ten limited liability companies (“LLCs”). The CTFs, UCITS, Westwood Funds®, CITs and LLCs (“Westwood VIEs”) are considered variable interest entities (“VIEs”) because our clients, who hold the equity at risk, do not have a direct or indirect ability through voting or similar rights to make decisions about the funds that would have a significant effect on their success. We receive fees at market rates for managing assets in these entities.



WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
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We evaluate all of our advisory relationships and CTFs to determine whether or not we qualify as the primary beneficiary based on whether there is an obligation to absorb the majority of expected losses or a right to receive the majority of expected residual returns. Since all losses and returns are distributed to the shareholders of the Company's VIEs, we are not the primary beneficiary and consequently the Westwood VIEs are not included in our condensed consolidated financial statements.

In May 2015, the Company provided seed investments of \$5.4 million for two new Westwood mutual funds. In both December 2015 and January 2014, the Company provided seed investments of \$2.0 million to two common trust funds. In October 2014, the Company provided a seed investment of €1.6 million, or \$2.0 million at the prevailing exchange rate, to the UCITS Fund. These seed investments were provided for the sole purpose of showing the economic substance needed to establish the funds or sub-funds. The corporate capital invested in these funds is included in "Investments, at fair value" on our condensed consolidated balance sheet at September 30, 2016.

We have not otherwise provided any financial support we were not previously contractually obligated to provide and there are no arrangements that would require us to provide additional financial support to any of these VIEs. Our investments in the Westwood Funds®, the CTFs and the UCITS Fund are accounted for as investments in accordance with our other investments described in Note 4 "Investments." We recognized fee revenue from the Westwood VIEs of \$13.5 million and \$14.0 million for the three months ended September 30, 2016 and 2015, respectively. We recognized fee revenue from the Westwood VIEs of \$39.5 million and \$43.3 million for the nine months ended September 30, 2016 and 2015, respectively.

The following table displays assets under management, corporate capital invested and risk of loss in each vehicle (in millions):

|                               | As of September 30, 2016      |                         |                   |
|-------------------------------|-------------------------------|-------------------------|-------------------|
|                               | Assets<br>Under<br>Management | Corporate<br>Investment | Amount<br>at Risk |
| VIEs:                         |                               |                         |                   |
| Westwood Funds®               | \$3,753                       | \$ 6                    | \$ 6              |
| Common Trust Funds            | 2,546                         | 3                       | 3                 |
| Collective Investment Trusts  | 48                            | —                       | —                 |
| LLCs                          | 125                           | —                       | —                 |
| UCITS Fund                    | 612                           | 2                       | 2                 |
| VIE totals                    | 7,084                         | 11                      | 11                |
| All other assets:             |                               |                         |                   |
| Private Wealth                | 2,656                         |                         |                   |
| Institutional                 | 11,532                        |                         |                   |
| Total Assets Under Management | \$21,272                      |                         |                   |

## 9. LONG-TERM INCENTIVE COMPENSATION

### Restricted Stock Awards

We have issued restricted shares to our employees and non-employee directors. The Third Amended and Restated Westwood Holdings Group, Inc. Stock Incentive Plan, as amended (the "Plan"), reserves shares of Westwood common stock for issuance to eligible employees, directors and consultants of Westwood or its subsidiaries in the form of restricted stock. The total number of shares issuable under the Plan (including predecessor plans to the Plan) may not exceed 4,398,100 shares. At September 30, 2016, approximately 346,000 shares remain available for issuance under the Plan.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)  
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The following table presents the total stock based compensation expense recorded for stock based compensation arrangements for the periods indicated (in thousands):

|  | Three Months<br>Ended<br>September 30,<br>2016 |         | Nine Months<br>Ended September<br>30,<br>2015 |          |
|--|--|---------|---|----------|
| Service condition stock based compensation expense     | \$2,679  | \$2,550 | \$7,978                                       | \$6,953  |
| Performance condition stock based compensation expense | 1,234  | 2,118   | 3,705   | 5,072    |
| Stock based compensation expense under the Plan        | 3,913  | 4,668   | 11,683  | 12,025   |
| Canadian EB Plan stock based compensation expense      | 169  | 197     | 481   | 535      |
| Total stock based compensation expense                 | \$4,082  | \$4,865 | \$12,164                                      | \$12,560 |

#### Restricted Stock

Under the Plan, we have granted to employees and non-employee directors restricted stock subject to service conditions, and to certain key employees restricted stock subject to both service and performance conditions.

As of September 30, 2016, there was approximately \$27.3 million of unrecognized compensation cost for restricted stock grants under the Plan, which we expect to recognize over a weighted-average period of 2.4 years. Our two types of restricted stock grants under the Plan are discussed below.

#### Restricted Stock Subject Only to a Service Condition

We calculate compensation cost for restricted stock grants by using the fair market value of our common stock at the date of grant, the number of shares issued, an adjustment for restrictions on dividends and an estimate of shares that will not vest due to forfeitures. This compensation cost is amortized on a straight-line basis over the applicable vesting period.

The following table details the status and changes in our restricted stock grants subject only to a service condition for the nine months ended September 30, 2016:

| Restricted shares subject only to a service condition: | Shares    | Weighted<br>Average<br>Grant<br>Date Fair<br>Value |
|--|-----------|--|
| Non-vested, January 1, 2016                            | 580,469   | \$ 56.76   |
| Granted  | 259,293   | 47.97  |
| Vested   | (174,310) | 51.42  |
| Forfeited  | (17,896 ) | 56.60  |
| Non-vested, September 30, 2016                         | 647,556   | \$ 54.68   |

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
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Restricted Stock Subject to Service and Performance Conditions

Under the Plan, certain key employees are provided agreements for grants of restricted shares that vest over multiple years provided that the annual performance goals established by the Compensation Committee of Westwood's Board of Directors are met. Each year the Compensation Committee establishes a specific goal for that year's vesting of the restricted shares, which historically has been based upon Westwood's adjusted pre-tax income, as defined below. The date that the Compensation Committee establishes the annual goal is considered to be the grant date and the fair value measurement date to determine expense on the shares that are likely to vest. In most cases, the vesting period ends when the Compensation Committee formally approves the performance-based restricted stock vesting based on the final calculation of adjusted pre-tax income as derived from the Company's audited consolidated financial statements. Certain performance grants include a scaled vesting based on actual adjusted pre-tax income. If a portion of the performance-based restricted shares does not vest, no compensation expense is recognized for that portion and any previously recognized compensation expense related to shares that do not vest is reversed. In March 2016, the Compensation Committee established the 2016 goal for adjusted pre-tax income, which is equal to income before income taxes increased by expenses incurred for the year for (i) incentive compensation for all officers and employees, (ii) performance-based restricted stock awards, and (iii) mutual fund share incentive awards, and excludes start up, non-recurring and similar expense items, at the Compensation Committee's discretion. Beginning in the first quarter of 2016, we concluded that it was probable that we would meet the performance goals required to vest the applicable performance based restricted shares this year and began recording expense related to those shares.

|  | Shares    | Weighted<br>Average<br>Grant<br>Date Fair<br>Value |
|--|-----------|--|
| Restricted shares subject to service and performance conditions: |           |  |
| Non-vested, January 1, 2016                                      | 101,313   | \$ 61.29   |
| Granted  | 151,334   | 55.90  |
| Vested   | (101,313) | 61.29  |
| Forfeited  | —         | —  |
| Non-vested, September 30, 2016                                   | 151,334   | \$ 55.90   |

The above amounts as of September 30, 2016 do not include 51,258 non-vested restricted shares that potentially vest over performance years subsequent to 2016 inasmuch as the Compensation Committee has not set annual performance goals for later years and therefore no grant date has been established.

Canadian Plan

The Share Award Plan of Westwood Holdings Group, Inc. for Service Provided in Canada to its Subsidiaries (the "Canadian Plan") provides compensation in the form of common stock for services performed by employees of Westwood International. Under the Canadian Plan, no more than \$10 million CDN (\$7.6 million in U.S. Dollars using the exchange rate on September 30, 2016) may be funded to the plan trustee for purchases of common stock with respect to awards granted under the Canadian Plan. At September 30, 2016, approximately \$6.0 million CDN (\$4.5 million in U.S. Dollars using the exchange rate on September 30, 2016) remains available for issuance under the Canadian Plan, or approximately 85,494 shares based on the closing share price of our stock of \$53.11 as of September 30, 2016. During the first nine months of 2016, the trust formed pursuant to the Canadian Plan purchased in the open market 10,474 Westwood common shares for approximately \$614,000. As of September 30, 2016, the trust holds 43,648 shares of Westwood common stock. As of September 30, 2016, unrecognized compensation cost related to restricted stock grants under the Canadian Plan totaled \$813,000, which we expect to recognize over a weighted-average period of 1.6 years.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
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#### Mutual Fund Share Incentive Awards

We grant annually to certain employees mutual fund incentive awards, which are bonus awards based on our mutual funds achieving specific performance goals. Awards granted are notionally credited to a participant account maintained by us that contains a number of mutual fund shares equal to the award amount divided by the net closing value of a fund share on the date the amount is credited to the account.

These awards vest after approximately one year of service following the year in which the participant earns the award. We begin accruing a liability for mutual fund incentive awards when we believe it is probable that the award will be earned and record expense for these awards over the service period of the award, which is approximately two years. During the year in which the amount of the award is determined, we record expense based on the expected value of the award. After the award is earned, we record expense based on the value of the shares awarded and the percentage of the vesting period that has elapsed. Our liability under these awards may increase or decrease based on changes in the value of the mutual fund shares awarded, including reinvested income from the mutual funds during the vesting period. Upon vesting, participants receive the value of the mutual fund share awards adjusted for earnings or losses attributable to the underlying mutual funds. For the three months ended September 30, 2016 and 2015, we recorded expense of \$313,000 and \$149,000, respectively, related to mutual fund share incentive awards. For the nine months ended September 30, 2016 and 2015, we recorded expense of \$933,000 and \$879,000, respectively, related to mutual fund share incentive awards. As of September 30, 2016 and December 31, 2015, we had an accrued liability of \$1.4 million and \$2.0 million, respectively, related to mutual fund share incentive awards.

#### 10. INCOME TAXES

Our effective income tax rate was 35.0% for the third quarter of 2016, compared with 33.2% for the third quarter of 2015. The increase is primarily related to an adjustment related to the filing of our 2015 tax return. Our effective income tax rate was 35.1% for the first nine months of 2016, compared with 33.3% for the first nine months of 2015. The increase is primarily related to a \$341,000 tax charge for uncertain tax positions related to current and prior years (net of federal benefit) recorded in the first nine months of 2016, as well as the adjustment related to the filing of our 2015 tax return in the third quarter of 2016.

As of September 30, 2016 and December 31, 2015, the Company's gross liability related to uncertain tax positions was \$2.2 million and \$1.6 million, respectively. A number of years may elapse before an uncertain tax position is finally resolved. To the extent that the Company has favorable tax settlements, or determines that accrued amounts are no longer needed due to a lapse in the applicable statute of limitations or other changes in circumstances, such liabilities, as well as any related interest and penalties, would be reversed as a reduction of income tax expense, net of federal tax effects, in the period such determination is made. A reconciliation of the change in recorded uncertain tax positions during the nine months ended September 30, 2016 is as follows (in thousands):

|   |         |
|---|---------|
| Balance at January 1, 2016                              | \$1,629 |
| Additions for tax positions related to the current year | 206     |
| Additions for tax positions related to prior years      | 475     |
| Reductions for tax positions related to prior years     | (156 )  |
| Balance at September 30, 2016                           | \$2,154 |

Within the next twelve months, it is reasonably possible that the liability for uncertain tax positions could decrease by as much as \$2.2 million as a result of settlements with certain taxing authorities, which, if recognized, would decrease our provision for income taxes by \$1.4 million.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
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11. RELATED PARTY TRANSACTIONS

Some of our directors, executive officers and their affiliates invest their personal funds directly in trust accounts that we manage. For the three months ended September 30, 2016 and 2015, we recorded trust fees from these accounts of \$108,000 and \$112,000, respectively. For the nine months ended September 30, 2016 and 2015, we recorded trust fees from these accounts of \$305,000 and \$334,000, respectively. There was \$106,000 due from these accounts as of September 30, 2016 and no amounts due from these accounts as of December 31, 2015.

The Company engages in transactions with its affiliates in the ordinary course of business. Westwood International and Westwood Management provide investment advisory services to the UCITS Fund, which began operations in August 2013. Certain members of our management and Board of Directors serve on the Board of Directors of the UCITS Fund. Under the terms of the investment advisory agreements, the Company earns quarterly fees paid by clients of the UCITS Fund and, in certain cases, by the UCITS Fund itself. The fees are based on negotiated fee schedules applied to assets under management. These fees are commensurate with market rates and are negotiated and contracted for at arm's length. For the three months ended September 30, 2016 and 2015, the Company earned approximately \$370,000 and \$298,000, respectively, in fees from the UCITS Fund. For the nine months ended September 30, 2016 and 2015, the Company earned approximately \$1,021,000 and \$994,000, respectively, in fees from the UCITS Fund. These fees do not include fees paid directly to Westwood International by certain clients invested in the UCITS Fund that have an investment management agreement with Westwood International. As of September 30, 2016 and December 31, 2015, \$143,000 and \$96,000, respectively, of these fees were unpaid and included in "Accounts receivable" on our condensed consolidated balance sheets.

12. COMMITMENTS AND CONTINGENCIES

On August 3, 2012, AGF Management Limited and AGF Investments Inc. (collectively, "AGF") filed a lawsuit in the Ontario Superior Court of Justice against Westwood, certain Westwood employees and the executive recruiting firm of Warren International, LLC. ("Warren"). The action relates to the hiring of certain members of Westwood's global and emerging markets investment team previously employed by AGF. AGF is alleging that the former employees breached certain obligations when they resigned from AGF and that Westwood and Warren induced such breaches. AGF is seeking an unspecified amount of damages and punitive damages of \$10 million CDN in the lawsuit. On November 5, 2012, Westwood responded to AGF's lawsuit with a counterclaim against AGF for defamation. Westwood is seeking \$1 million CDN in general damages, \$10 million CDN in special damages, \$1 million CDN in punitive damages, and costs. On November 6, 2012, AGF filed a second lawsuit against Westwood, Westwood Management and an employee of a Westwood subsidiary, alleging that the employee made defamatory statements about AGF. In this second lawsuit, AGF is seeking \$5 million CDN in general damages, \$1 million CDN per defendant in punitive damages, unspecified special damages, interest and costs. The pleadings phase was completed in 2013, and we are currently in the discovery phase.

While we intend to vigorously defend both actions and pursue our counterclaims, we are currently unable to estimate the ultimate aggregate amount of monetary gain, loss or financial impact of these actions and counterclaims. Defending these actions and pursuing these counterclaims may be expensive for us, as well as time consuming for our personnel. While we do not currently believe these proceedings will have a material impact, adverse resolution of these actions and counterclaims could have a material adverse effect on our business, financial condition or results of operations and cash flows.

Our policy is to not accrue legal fees and directly related costs as part of potential loss contingencies. We have agreed with our Directors & Officers insurance provider that 50% of the defense costs related to both AGF claims, excluding Westwood's counterclaim against AGF, are covered by insurance. We expense legal fees and directly related costs as incurred. We have received insurance proceeds of approximately \$928,000 as of September 30, 2016 and recorded a receivable of \$249,000 and \$240,000 as of September 30, 2016 and December 31, 2015, respectively, which represents our current minimum estimate of expenses that we expect to recover under our insurance policy. This receivable is part of "Other current assets" on our condensed consolidated balance sheets.





WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
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13. SEGMENT REPORTING

We operate two segments: Advisory and Trust. These segments are managed separately based on the types of products and services offered and their related client bases. The Company's segment information is prepared on the same basis that management reviews the financial information for operational decision-making purposes. The Company's chief operating decision maker, our Chief Executive Officer, evaluates the performance of our segments based primarily on fee revenues and Economic Earnings. Westwood Holdings Group, Inc., the parent company of Advisory and Trust, does not have revenues and is the entity in which we record typical holding company expenses including employee compensation and benefits for holding company employees, directors' fees and investor relations costs. All segment accounting policies are the same as those described in the summary of significant accounting policies. Intersegment balances that eliminate in consolidation have been applied to the appropriate segment.

Advisory

Our Advisory segment provides investment advisory services to corporate retirement plans, public retirement plans, endowments, foundations, individuals, the Westwood Funds®, and the UCITS Fund, as well as investment subadvisory services to mutual funds and our Trust segment. Westwood Management and Westwood International, which provide investment advisory services to clients of similar type, are included in our Advisory segment along with Westwood Advisors, LLC.

Trust

Trust provides trust and custodial services and participation in common trust funds that it sponsors to institutions and high net worth individuals. Westwood Trust is included in our Trust segment.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
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|  | Advisory       | Trust    | Westwood<br>Holdings | Eliminations | Consolidated |
|--|----------------|----------|----------------------|--------------|--------------|
|  | (in thousands) |          |                      |              |              |
| Three Months Ended September 30, 2016  |                |          |                      |              |              |
| Net fee revenues from external sources | \$23,673       | \$7,690  | \$—                  | \$—          | \$ 31,363    |
| Net intersegment revenues              | 5,275          | 41       | —                    | (5,316 )     | —            |
| Net interest and dividend revenue      | 128            | 5        | —                    | —            | 133          |
| Other, net                             | 279            | 2        | —                    | —            | 281          |
| Total revenues                         | \$29,355       | \$7,738  | \$—                  | \$(5,316 )   | \$ 31,777    |
| Economic Earnings                      | \$10,270       | \$1,690  | \$(1,345 )           | \$—          | \$ 10,615    |
| Less: Restricted stock expense         |                |          |                      |              | 4,082        |
| Intangible amortization                |                |          |                      |              | 490          |
| Deferred taxes on goodwill             |                |          |                      |              | 156          |
| Net income                             |                |          |                      |              | \$ 5,887     |
| Segment assets                         | \$163,826      | \$65,986 | \$13,046             | \$(73,160 )  | \$ 169,698   |
| Segment goodwill                       | \$5,219        | \$21,925 | \$—                  | \$—          | \$ 27,144    |
| Three Months Ended September 30, 2015  |                |          |                      |              |              |
| Net fee revenues from external sources | \$24,941       | \$7,972  | \$—                  | \$—          | \$ 32,913    |
| Net intersegment revenues              | 5,087          | —        | —                    | (5,087 )     | —            |
| Net interest and dividend revenue      | 110            | —        | —                    | —            | 110          |
| Other, net                             | (577 )         | 5        | —                    | —            | (572 )       |
| Total revenues                         | \$29,561       | \$7,977  | \$—                  | \$(5,087 )   | \$ 32,451    |
| Economic Earnings                      | \$11,961       | \$1,592  | \$(1,119 )           | \$—          | \$ 12,434    |
| Less: Restricted stock expense         |                |          |                      |              | 4,865        |
| Intangible amortization                |                |          |                      |              | 400          |
| Deferred taxes on goodwill             |                |          |                      |              | 156          |
| Net income                             |                |          |                      |              | \$ 7,013     |
| Segment assets                         | \$172,034      | \$57,967 | \$7,753              | \$(71,537 )  | \$ 166,217   |
| Segment goodwill                       | \$5,219        | \$19,872 | \$—                  | \$—          | \$ 25,091    |

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)  
 (Unaudited)

|  | Advisory Trust |          | Westwood   | Eliminations | Consolidated |
|--|----------------|----------|------------|--------------|--------------|
|  | (in thousands) |          | Holdings   |              |              |
| Nine Months Ended September 30, 2016   |                |          |            |              |              |
| Net fee revenues from external sources | \$68,563       | \$22,798 | \$ —       | \$ —         | \$ 91,361    |
| Net intersegment revenues              | 14,455         | 82       | —          | (14,537 )    | —            |
| Net interest and dividend revenue      | 360            | 9        | —          | —            | 369          |
| Other, net                             | 462            | (263 )   | —          | —            | 199          |
| Total revenues                         | \$83,840       | \$22,626 | \$ —       | \$(14,537 )  | \$ 91,929    |
| Economic Earnings                      | \$30,493       | \$4,160  | \$(5,559 ) | \$ —         | \$ 29,094    |
| Less: Restricted stock expense         |                |          |            |              | 12,164       |
| Intangible amortization                |                |          |            |              | 1,470        |
| Deferred taxes on goodwill             |                |          |            |              | 390          |
| Net income                             |                |          |            |              | \$ 15,070    |
| Nine Months Ended September 30, 2015   |                |          |            |              |              |
| Net fee revenues from external sources | \$78,534       | \$21,043 | \$ —       | \$ —         | \$ 99,577    |
| Net intersegment revenues              | 14,826         | —        | —          | (14,826 )    | —            |
| Net interest and dividend revenue      | 218            | 1        | —          | —            | 219          |
| Other, net                             | (431 )         | 5        | —          | —            | (426 )       |
| Total revenues                         | \$93,147       | \$21,049 | \$ —       | \$(14,826 )  | \$ 99,370    |
| Economic Earnings                      | \$37,827       | \$3,405  | \$(5,031 ) | \$ —         | \$ 36,201    |
| Less: Restricted stock expense         |                |          |            |              | 12,560       |
| Intangible amortization                |                |          |            |              | 951          |
| Deferred taxes on goodwill             |                |          |            |              | 272          |
| Net income                             |                |          |            |              | \$ 22,418    |

We are providing a performance measure that we refer to as Economic Earnings. Both our management and Board of Directors review Economic Earnings to evaluate our ongoing performance, allocate resources and determine our dividend policy. We also believe that this performance measure is useful for management and investors when evaluating our underlying operating and financial performance and our available resources.

In calculating Economic Earnings, we add to net income the non-cash expense associated with equity-based compensation awards of restricted stock, amortization of intangible assets and the deferred taxes related to the tax-basis amortization of goodwill. Although depreciation on property and equipment is a non-cash expense, we do not add it back when calculating Economic Earnings because depreciation charges represent a decline in the value of the related assets that will ultimately require replacement.

WESTWOOD HOLDINGS GROUP, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS — (Continued)  
 (Unaudited)

The following tables provide a reconciliation of net income to Economic Earnings (in thousands, except per share and share amounts):

|   | Three Months<br>Ended September<br>30, |          |
|---|--|----------|
|   | 2016                                   | 2015     |
| Net Income                                  | \$5,887                                | \$7,013  |
| Add: Stock based compensation expense       | 4,082                                  | 4,865    |
| Add: Intangible amortization                | 490                                    | 400      |
| Add: Tax benefit from goodwill amortization | 156                                    | 156      |
| Economic Earnings                           | \$10,615                               | \$12,434 |
|   | Nine Months<br>Ended September<br>30,  |          |
|   | 2016                                   | 2015     |
| Net Income                                  | \$15,070                               | \$22,418 |
| Add: Stock based compensation expense       | 12,164                                 | 12,560   |
| Add: Intangible amortization                | 1,470                                  | 951      |
| Add: Tax benefit from goodwill amortization | 390                                    | 272      |
| Economic Earnings                           | \$29,094                               | \$36,201 |

#### 14. SUBSEQUENT EVENTS

##### Dividend Declared

In October 2016, Westwood's Board of Directors declared a quarterly cash dividend of \$0.62 per common share, an increase of 9% from the previous quarterly dividend rate, payable on January 3, 2017 to stockholders of record on December 9, 2016.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

Statements in this report and the Annual Report to Stockholders that are not purely historical facts, including, without limitation, statements about our expected future financial position, results of operations or cash flows, as well as other statements including, without limitation, words such as "anticipate," "believe," "plan," "estimate," "expect," "intend," "should," "could," "goal," "may," "target," "designed," "on track," "comfortable with," "optimistic" and other similar expressions, constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Actual results and the timing of some events could differ materially from those projected in or contemplated by the forward-looking statements due to a number of factors, including, without limitation, the risks described under "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2015, filed with the SEC, and those risks set forth below:

- the composition and market value of our assets under management;
- regulations adversely affecting the financial services industry;
- competition in the investment management industry;
- our investments in foreign companies;
- our ability to develop and market new investment strategies successfully;
- our ability to pursue and properly integrate acquired businesses;
- litigation risks;
- our ability to retain qualified personnel;
- our relationships with current and potential customers;
- our ability to properly address conflicts of interest;
- our ability to maintain effective information systems;
- our ability to maintain effective cyber security;
- our ability to maintain adequate insurance coverage;
- our ability to maintain an effective system of internal controls;
- our ability to maintain our fee structure in light of competitive fee pressures;
- our relationships with investment consulting firms; and
- the significant concentration of our revenues in a small number of customers.

You should not unduly rely on these forward-looking statements, which speak only as of the date of this report. We are not obligated and do not undertake an obligation to publicly release any revisions to these forward-looking statements to reflect events or circumstances occurring after the date of this report or to reflect the occurrence of unanticipated events or otherwise.

## Overview

We manage investment assets and provide services for our clients through our subsidiaries, Westwood Management Corp. and Westwood Advisors, LLC (together, "Westwood Management"), Westwood International Advisors Inc. ("Westwood International") and Westwood Trust. Westwood Management provides investment advisory services to institutional investors, a family of mutual funds called the Westwood Funds®, other mutual funds, an Ireland-domiciled fund organized pursuant to the European Union's Undertakings for Collective Investment in Transferable Securities ("UCITS"), individual investors and clients of Westwood Trust. Westwood International provides investment advisory services to institutional clients, the Westwood Funds®, other mutual funds, the UCITS Fund and clients of Westwood Trust. Westwood Trust provides trust and custodial services and participation in self-sponsored common trust funds to institutions and high net worth individuals. Our revenues are generally derived from fees based on a percentage of assets under management.

## Revenues

We derive our revenues from investment advisory fees, trust fees, and other revenues. Our advisory fees are generated by Westwood Management and Westwood International, which manage client accounts under investment advisory and subadvisory agreements. Advisory fees are calculated based on a percentage of assets under management and are paid in accordance with the terms of the agreements. Advisory fees are paid quarterly in advance based on assets under management on the last day of the preceding quarter, quarterly in arrears based on assets under management on the last day of the quarter just ended, or are based on a daily or monthly analysis of assets under management for the stated period. We recognize advisory fee revenues as services are rendered. A limited number of our clients have a contractual performance-based fee component, which generates additional revenues if we outperform a specified index over a specific period of time. We record revenue from performance-based fees when we determine that the fees are probable. This determination is typically made at the end of the measurement periods. Since billing periods for our advance-paying clients coincide with the calendar quarter to which such payments relate, revenue is recognized within the quarter and our condensed consolidated financial statements contain no deferred advisory fee revenues.

Our trust fees are generated by Westwood Trust pursuant to trust or custodial agreements. Trust fees are separately negotiated with each client and are generally based on a percentage of assets under management. Westwood Trust also provides trust services to a small number of clients on a fixed fee basis. During the first quarter of 2016, Westwood Trust changed the billing terms for most of our trust clients from quarterly in advance, based on assets under management on the last day of the preceding quarter, to quarterly in arrears, based on a daily average of assets under management for the quarter. This billing change did not impact revenue recognized during the quarter, as we recognize trust fee revenues as services are rendered. Since billing periods for most of Westwood Trust's clients coincide with the calendar quarter, revenue is fully recognized within the quarter and our condensed consolidated financial statements do not contain a significant amount of deferred revenue.

Our other revenues generally consist of interest and investment income. Although we generally invest most of our cash in U.S. Treasury securities, we also invest in equity and fixed income instruments and money market funds.

## Employee Compensation and Benefits

Employee compensation and benefits costs generally consist of salaries, incentive compensation, equity-based compensation expense and benefits.

## Sales and Marketing

Sales and marketing costs relate to our marketing efforts, including travel and entertainment, direct marketing and advertising costs.

## Westwood Mutual Funds

Westwood Mutual Funds expenses relate to our marketing, distribution and administration of the Westwood Funds®.

Information Technology

Information technology expenses are generally costs associated with proprietary investment research tools, maintenance and support, computing hardware, software licenses, telecommunications and other related costs.

Professional Services

Professional services expenses generally consist of costs associated with subadvisory fees, audit, tax, legal and other professional services.

General and Administrative

General and administrative expenses generally consist of costs associated with the lease of our office space, amortization, depreciation, insurance, custody expense, Board of Directors fees, investor relations, licenses and fees, office supplies and other miscellaneous expenses.

## Assets Under Management

Assets under management ("AUM") increased \$900 million to \$21.3 billion at September 30, 2016 compared with \$20.4 billion at September 30, 2015 as a result of market appreciation, partially offset by net outflows, over the last twelve months. The average of beginning and ending assets under management for the third quarter of 2016 was \$21.1 billion compared to \$21.8 billion for the third quarter of 2015. The decrease in average assets under management is due to net outflows since September 30, 2015, as \$2.3 billion market appreciation over the last twelve months offset the \$2.2 billion market depreciation in the third quarter of 2015.

The following table displays assets under management as of September 30, 2016 and 2015:

|  | As of September 30, |          | % Change                                  |   |
|--|---------------------|----------|---|---|
|  | 2016                | 2015     | September 30, 2016 vs. September 30, 2015 |   |
|  | (in millions)       |          |   |   |
| Institutional                                | \$12,192            | \$11,288 | 8   | % |
| Private Wealth                               | 5,327               | 5,246    | 2   |   |
| Mutual Funds                                 | 3,753               | 3,841    | (2)                                       | ) |
| Total Assets Under Management <sup>(1)</sup> | \$21,272            | \$20,375 | 4   | % |

AUM excludes \$1.1 billion of assets under advisement ("AUA") as of September 30, 2016 related to our model portfolios, including approximately \$800 million in a long-only convertibles fund for which we provide consulting (1) advice but do not have direct discretionary investment authority. AUM excluded approximately \$640 million of AUA as of September 30, 2015, which included assets related to our market neutral income strategy that transitioned from AUA to AUM during the fourth quarter of 2015.

Institutional includes separate accounts of corporate pension and profit sharing plans, public employee retirement funds, Taft Hartley plans, endowments, foundations and individuals; subadvisory relationships where Westwood provides investment management services for funds offered by other financial institutions; pooled investment vehicles, including the UCITS Fund and collective investment trusts; and managed account relationships with brokerage firms and other registered investment advisors that offer Westwood products to their customers.

Private Wealth includes assets for which Westwood Trust provides trust and custodial services and participation in common trust funds that it sponsors to institutions and high net worth individuals pursuant to trust or agency agreements and assets for which Westwood Management provides advisory services in ten limited liability companies to high net worth individuals. Investment subadvisory services are provided for the common trust funds by Westwood Management, Westwood International and external, unaffiliated subadvisors. For certain assets in this category, Westwood Trust currently provides limited custody services for a minimal or no fee, viewing these assets as potentially converting to fee-generating managed assets in the future. As an example, some assets in this category consist of low-basis stock currently held in custody for clients where we believe such assets may convert to fee-generating managed assets during an inter-generational transfer of wealth.

Mutual Funds include the Westwood Funds®, a family of mutual funds for which Westwood Management serves as an advisor. These funds are available to individual investors, as well as offered as part of our investment strategies for institutional and private wealth accounts.



## Roll-Forward of Assets Under Management

| (\$ millions)                      | Three Months                   |          | Nine Months                    |          |
|------------------------------------|--------------------------------|----------|--------------------------------|----------|
|                                    | Ended September<br>30,<br>2016 | 2015     | Ended September<br>30,<br>2016 | 2015     |
| <b>Institutional</b>               |                                |          |                                |          |
| Beginning of period assets         | \$11,921                       | \$13,203 | \$11,752                       | \$12,471 |
| Inflows                            | 420                            | 179      | 1,133                          | 1,549    |
| Outflows <sup>(1)</sup>            | (606 )                         | (540 )   | (1,902 )                       | (1,516 ) |
| Net flows                          | (186 )                         | (361 )   | (769 )                         | 33       |
| Market appreciation (depreciation) | 457                            | (1,554 ) | 1,209                          | (1,216 ) |
| Net change                         | 271                            | (1,915 ) | 440                            | (1,183 ) |
| End of period assets               | 12,192                         | 11,288   | 12,192                         | 11,288   |
| <b>Private Wealth</b>              |                                |          |                                |          |
| Beginning of period assets         | 5,361                          | 5,638    | 5,393                          | 3,974    |
| Inflows                            | 104                            | 222      | 274                            | 506      |
| Outflows                           | (245 )                         | (242 )   | (626 )                         | (590 )   |
| Net flows                          | (141 )                         | (20 )    | (352 )                         | (84 )    |
| Acquisition related                | —                              | —        | —                              | 1,583    |
| Market appreciation (depreciation) | 107                            | (372 )   | 286                            | (227 )   |
| Net change                         | (34 )                          | (392 )   | (66 )                          | 1,272    |
| End of period assets               | 5,327                          | 5,246    | 5,327                          | 5,246    |
| <b>Mutual Funds</b>                |                                |          |                                |          |
| Beginning of period assets         | 3,690                          | 4,283    | 3,617                          | 3,722    |
| Inflows                            | 214                            | 257      | 674                            | 1,031    |
| Outflows                           | (224 )                         | (399 )   | (798 )                         | (657 )   |
| Net flows                          | (10 )                          | (142 )   | (124 )                         | 374      |
| Market appreciation (depreciation) | 73                             | (300 )   | 260                            | (255 )   |
| Net change                         | 63                             | (442 )   | 136                            | 119      |
| End of period assets               | 3,753                          | 3,841    | 3,753                          | 3,841    |
| <b>Total</b>                       |                                |          |                                |          |
| Beginning of period assets         | 20,972                         | 23,124   | 20,762                         | 20,167   |
| Inflows                            | 738                            | 658      | 2,081                          | 3,086    |
| Outflows <sup>(1)</sup>            | (1,075 )                       | (1,181 ) | (3,326 )                       | (2,763 ) |
| Net flows                          | (337 )                         | (523 )   | (1,245 )                       | 323      |
| Acquisition related                | —                              | —        | —                              | 1,583    |
| Market appreciation (depreciation) | 637                            | (2,226 ) | 1,755                          | (1,698 ) |
| Net change                         | 300                            | (2,749 ) | 510                            | 208      |
| End of period assets               | \$21,272                       | \$20,375 | \$21,272                       | \$20,375 |

Outflows for the three and nine months ended September 30, 2016 include approximately \$30 million in an (1) account that transitioned to our model portfolio, for which we no longer have direct discretionary investment authority. This account is now included in AUA aggregating \$1.1 billion as of September 30, 2016.

Three months ended September 30, 2016 and 2015

The \$300 million increase in assets under management for the three months ended September 30, 2016 was due to market appreciation of \$637 million, partially offset by net outflows of \$337 million. Net outflows were primarily related to our SMidCap, LargeCap Value and Market Neutral Income strategies.

The \$2.7 billion decrease in assets under management for the three months ended September 30, 2015 was due to market depreciation of \$2.2 billion and net outflows of \$523 million. Net flows were primarily driven by outflows in our Income Opportunity, SMid Cap and Emerging Markets strategies, partially offset by inflows in our Income Opportunity and Emerging Markets strategies.

Nine months ended September 30, 2016 and 2015

The \$510 million increase in assets under management for the nine months ended September 30, 2016 was due to market appreciation of \$1.8 billion, partially offset by net outflows of \$1.2 billion. Net outflows were primarily related to our SMidCap, SMidCap Plus, LargeCap Value, AllCap Value and Income Opportunity strategies.

The \$208 million increase in assets under management for the nine months ended September 30, 2015 was due to net asset inflows of \$323 million and \$1.6 billion of assets related to the Woodway acquisition, offset by market depreciation of \$1.7 billion. Net flows were primarily driven by inflows into our Emerging Markets, Income Opportunity, MLP and SMid Cap strategies, partially offset by outflows in our LargeCap Value, SMid Cap, Income Opportunity and Emerging Markets strategies.

## Results of Operations

The following table (dollars in thousands) and discussion of our results of operations is based upon data derived from the condensed consolidated statements of comprehensive income contained in our condensed consolidated financial statements and should be read in conjunction with those statements, included elsewhere in this report.

|                                    | Three Months Ended September 30, 2016 |          | Nine Months Ended September 30, 2016 |          | % Change<br>September 30, 2016<br>vs.<br>September 30, 2015 | % Change<br>Nine<br>Months<br>Ended<br>September<br>30, 2016<br>vs.<br>September<br>30, 2015 |
|------------------------------------|---------------------------------------|----------|--------------------------------------|----------|---|--|
| <b>Revenues</b>                    |                                       |          |                                      |          |   |  |
| Advisory fees - asset based        | \$23,447                              | \$24,940 | \$67,928                             | \$76,327 | (6 )%   | (11 )%   |
| Advisory fees - performance based  | 226                                   | —        | 635                                  | 2,206    | 100   | (71 )  |
| Trust fees                         | 7,690                                 | 7,973    | 22,798                               | 21,044   | (4 )  | 8  |
| Other revenues                     | 414                                   | (462 )   | 568                                  | (207 )   | NM  | NM   |
| Total revenues                     | 31,777                                | 32,451   | 91,929                               | 99,370   | (2 )  | (7 )   |
| <b>Expenses</b>                    |                                       |          |                                      |          |   |  |
| Employee compensation and benefits | 15,637                                | 15,686   | 47,239                               | 47,507   | 0   | (1 )   |
| Sales and marketing                | 408                                   | 419      | 1,423                                | 1,310    | (3 )  | 9  |
| Westwood mutual funds              | 755                                   | 865      | 2,282                                | 2,593    | (13 )   | (12 )  |
| Information technology             | 1,874                                 | 1,626    | 6,039                                | 4,085    | 15  | 48   |
| Professional services              | 1,903                                 | 1,178    | 4,707                                | 4,281    | 62  | 10   |
| General and administrative         | 2,147                                 | 2,175    | 7,028                                | 5,962    | (1 )  | 18   |
| Total expenses                     | 22,724                                | 21,949   | 68,718                               | 65,738   | 4   | 5  |
| Income before income taxes         | 9,053                                 | 10,502   | 23,211                               | 33,632   | (14 )   | (31 )  |
| Provision for income taxes         | 3,166                                 | 3,489    | 8,141                                | 11,214   | (9 )  | (27 )  |
| Net income                         | \$5,887                               | \$7,013  | \$15,070                             | \$22,418 | (16 )%  | (33 )%   |

NM Not meaningful

Three months ended September 30, 2016 compared to three months ended September 30, 2015

**Total Revenues.** Our Total revenues decreased \$0.7 million, or 2%, to \$31.8 million for the three months ended September 30, 2016 compared with \$32.5 million for the three months ended September 30, 2015. Asset-based advisory fees decreased \$1.5 million, or 6%, due to lower average assets under management. Trust fees decreased \$0.3 million, or 4%, primarily due to lower average assets under management.

**Employee Compensation and Benefits.** Employee compensation and benefits costs was relatively flat at \$15.6 million for the three months ended September 30, 2016 compared with \$15.7 million for the three months ended September 30, 2015, as increases in average head-count and merit increases were offset by a decrease in restricted stock expense attributable to a non-cash charge related to acceleration of stock based compensation expense for a particular grant during the third quarter of 2015.

**Professional Services.** Professional service expenses increased \$0.7 million, or 62%, to \$1.9 million for the three months ended September 30, 2016 compared to \$1.2 million for the three months ended September 30, 2015, due to increased legal fees.

**Provision for Income Taxes.** The effective tax rate increased to 35.0% for the three months ended September 30, 2016 from 33.2% for the three months ended September 30, 2015. The increase is primarily related to an adjustment related to the filing of our 2015 tax return in the third quarter of 2016.

Nine months ended September 30, 2016 compared to nine months ended September 30, 2015

**Total Revenues.** Our total revenues decreased \$7.5 million, or 7%, to \$91.9 million for the nine months ended September 30, 2016 compared with \$99.4 million for the nine months ended September 30, 2015. This decrease was primarily related to a \$8.4 million, or 11%, decrease in asset-based advisory fees related to lower average assets under management due to net outflows and market depreciation and a \$1.6 million decrease in performance-based fees, partially offset by a \$1.8 million, or 8%, increase in Trust fees as a result of the Woodway acquisition.

**Employee Compensation and Benefits.** Employee compensation and benefits costs decreased slightly to \$47.2 million for the nine months ended September 30, 2016 compared with \$47.5 million for the nine months ended September 30, 2015. Incentive compensation accruals decreased \$2.4 million due to lower results during the first nine months of 2016, and restricted stock expense decreased \$1.3 million as a result of a third quarter 2015 non-cash charge related to acceleration of stock based compensation expense for a particular grant. These decreases were offset by an increase in compensation expenses attributable to increased average headcount and merit increases.

**Information Technology.** Information technology expenses increased \$1.9 million, or 48%, to \$6.0 million for the nine months ended September 30, 2016 compared to \$4.1 million for the nine months ended September 30, 2015, due to costs associated with implementing new information technology platforms, increased research and support expenses and the Woodway acquisition.

**General and Administrative.** General and administrative expenses increased \$1.0 million, or 18%, to \$7.0 million for the nine months ended September 30, 2016 compared to \$6.0 million for the nine months ended September 30, 2015, primarily due to increased rent and depreciation expenses related to the expansion of our corporate headquarters, amortization of intangibles related to the Woodway acquisition and ongoing general and administrative expenses for Woodway.

**Provision for Income Taxes.** The effective tax rate increased to 35.1% for the nine months ended September 30, 2016 from 33.3% for the nine months ended September 30, 2015. The increase is primarily related to adjustments to uncertain tax positions related to current and prior years (net of federal tax benefit) recorded in the first and third quarters of 2016.

## Supplemental Financial Information

As supplemental information, we are providing a non-U.S. generally accepted accounting principles (“non-GAAP”) performance measure that we refer to as Economic Earnings. We provide this measure in addition to, but not as a substitute for, net income reported on a U.S. generally accepted accounting principles (“GAAP”) basis. Our management and Board of Directors review Economic Earnings to evaluate our ongoing performance, allocate resources and review the dividend policy. We believe that this non-GAAP performance measure, while not a substitute for GAAP net income, is useful for management and investors when evaluating our underlying operating and financial performance and our available resources. We do not advocate that investors consider this non-GAAP measure without also considering financial information prepared in accordance with GAAP.

In calculating Economic Earnings, we add to net income the non-cash expense associated with equity-based compensation awards of restricted stock, amortization of intangible assets and the deferred taxes related to the tax-basis amortization of goodwill. Although depreciation on property and equipment is a non-cash expense, we do not add it back when calculating Economic Earnings because depreciation charges represent a decline in the value of the related assets that will ultimately require replacement. In addition, we do not adjust Economic Earnings for tax deductions related to restricted stock expense or amortization of intangible assets.

The following tables provide a reconciliation of net income to Economic Earnings (in thousands, except per share and share amounts):

|   | Three Months        |           |        |
|---|---------------------|-----------|--------|
|   | Ended September 30, |           | %      |
|   | 2016                | 2015      | Change |
| Net Income                                  | \$5,887             | \$ 7,013  | (16 )% |
| Add: Stock based compensation expense       | 4,082               | 4,865     | (16 )  |
| Add: Intangible amortization                | 490                 | 400       | 23     |
| Add: Tax benefit from goodwill amortization | 156                 | 156       | 0      |
| Economic Earnings                           | \$10,615            | \$ 12,434 | (15 )% |
| Diluted weighted average shares outstanding | 8,179,956           | 8,037,080 |        |
| Economic Earnings per share                 | \$1.30              | \$ 1.55   |        |

|   | Nine Months         |           |        |
|---|---------------------|-----------|--------|
|   | Ended September 30, |           | %      |
|   | 2016                | 2015      | Change |
| Net Income                                  | \$15,070            | \$ 22,418 | (33 )% |
| Add: Stock based compensation expense       | 12,164              | 12,560    | (3 )   |
| Add: Intangible amortization                | 1,470               | 951       | 55     |
| Add: Tax benefit from goodwill amortization | 390                 | 272       | 43     |
| Economic Earnings                           | \$29,094            | \$ 36,201 | (20 )% |
| Diluted weighted average shares outstanding | 8,212,468           | 8,076,055 |        |
| Economic Earnings per share                 | \$3.54              | \$ 4.48   |        |

### Liquidity and Capital Resources

We fund our operations and cash requirements with cash generated from operating activities. We may also use cash from operations to pay dividends to our stockholders. As of September 30, 2016 and December 31, 2015, we had no debt. The changes in net cash provided by operating activities generally reflect the changes in earnings plus the effects of non-cash items and changes in working capital. Changes in working capital, especially accounts receivable and accounts payable, are generally the result of timing differences between collection of fees billed and payment of operating expenses.

During the nine months ended September 30, 2016, cash flow provided by operating activities, principally our investment advisory business, was \$39.0 million. Cash flow used in investing activities of \$1.7 million during the nine months ended September 30, 2016 was related to purchases of fixed assets. Cash flow used in financing activities of \$30.2 million for the nine months ended September 30, 2016 was due to the payment of dividends, payment of the contingent consideration related to the Woodway acquisition, repurchases of our common stock under our share repurchase plan, purchases of restricted stock returned for payment of taxes and purchases of treasury shares for our Canadian share award plan.

We had cash and investments of \$80.5 million as of September 30, 2016 and \$95.1 million as of December 31, 2015. Cash and cash equivalents as of September 30, 2016 and December 31, 2015 includes approximately \$20 million and \$13 million, respectively, of undistributed income from Westwood International that we consider to be permanently invested in Canada. At September 30, 2016 and December 31, 2015, working capital aggregated \$80.2 million and \$72.8 million, respectively.

Westwood Trust must maintain cash and investments in an amount equal to the required minimum restricted capital of \$4.0 million, as required by the Texas Finance Code. Restricted capital is included in Investments in the accompanying condensed consolidated balance sheets. At September 30, 2016, Westwood Trust had approximately \$11.4 million in excess of its minimum capital requirement.

Our future liquidity and capital requirements will depend upon numerous factors, including our results of operations, the timing and magnitude of capital expenditures or strategic initiatives, our dividend policy and other business and risk factors described under "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2015, filed with the SEC. We believe that current cash and short-term investment balances and cash generated from operations will be sufficient to meet both the operating and capital requirements of our ordinary business operations through at least the next twelve months. However, there can be no assurance that we will not require additional financing within this time frame. The failure to raise needed capital on attractive terms, if at all, could have a material adverse effect on our business, financial condition and results of operations.

### Contractual Obligations

As of September 30, 2016, there have been no material changes outside the ordinary course of business to our contractual obligations since December 31, 2015. For information regarding our contractual obligations, refer to "Contractual Obligations" in Part II, Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015.

### Critical and Significant Accounting Policies and Estimates

There have been no significant changes in our critical or significant accounting policies and estimates since December 31, 2015. Information with respect to our critical accounting policies and estimates that we believe could have the most significant effect on our reported consolidated results and require difficult, subjective or complex judgment by management are described under "Critical Accounting Policies and Estimates" in Part II, Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015.

#### Accounting Developments

Refer to Note 2 “Summary of Significant Accounting Policies” in our condensed consolidated financial statements included in Part I, Item 1. “Financial Statements” of this Quarterly Report on Form 10-Q for a description of recently issued accounting guidance.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no significant changes in our Quantitative and Qualitative Disclosures about Market Risk from those previously reported in our Annual Report on Form 10-K for the year ended December 31, 2015.

#### ITEM 4. CONTROLS AND PROCEDURES

##### Evaluation of Disclosure Controls and Procedures

Our disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports we file or submit under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), (1) is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and (2) is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, to allow timely decisions regarding required disclosure. An evaluation was performed under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this report. Based on this evaluation, our management, including our Chief Executive Officer and our Chief Financial Officer, concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and is accumulated and communicated to management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

##### Changes in Internal Controls over Financial Reporting

For the quarter ended September 30, 2016, there were no changes in our internal controls over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

## ITEM 1. LEGAL PROCEEDINGS

See discussion of legal proceedings and procedures in Note 12 “Commitments and Contingencies” in our condensed consolidated financial statements included in Part I, Item 1. “Financial Statements” of this Quarterly Report on Form 10-Q.

## ITEM 1A. RISK FACTORS

We face a number of significant risks and uncertainties in our business, including those detailed under “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2015 and summarized in this report under “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” These risks and uncertainties may affect our current position and future prospects and should be considered carefully in evaluating us, including making an investment in our common stock.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table displays information with respect to the treasury shares we purchased during the three months ended September 30, 2016:

| Period                            | Total number of shares purchased | Average price paid per share | Total number of shares purchased as part of publicly announced plans or programs | Maximum number (or approximate dollar value) of shares that may yet be purchased under the plans or programs (1) |
|-----------------------------------|----------------------------------|------------------------------|--|--|
| July 1 through September 30, 2016 |                                  |                              |  |  |
| Repurchase program (1)            | 24,199                           | \$ 49.92                     | 24,199   | \$ 9,370,853   |
| Canadian Plan (2)                 | —                                | \$ —                         | —  | CDN \$ 5,960,344   |
| Employee transactions (3)         | 265                              | \$ 59.61                     | —  | —  |

On July 20, 2012, our Board of Directors authorized management to repurchase up to \$10 million of our outstanding common stock on the open market or in privately negotiated transactions. In July 2016, Westwood's Board of Directors authorized an additional \$5.0 million of repurchases under the share repurchase program. The share repurchase program has no expiration date and may be discontinued at any time by the Board of Directors. On April 18, 2013, our stockholders approved the Share Award Plan of Westwood Holdings Group, Inc. for Service Provided in Canada to its Subsidiaries (the “Canadian Plan”), which contemplates a trustee purchasing up to \$10 million CDN of our outstanding common stock on the open market for the purpose of making share awards to our Canadian employees. The Canadian Plan has no expiration date and may be discontinued at any time by the Board of Directors.

Consists of shares of common stock tendered by an employee at the market close price on the date of vesting in order to satisfy the employee’s minimum tax withholding obligations from vested restricted shares. We anticipate having additional shares tendered in subsequent periods for the same purpose.



ITEM 6. EXHIBITS

- 31.1\* Certification of Chief Executive Officer Pursuant to Securities Exchange Act Rule 13a-14(a)
- 31.2\* Certification of Chief Financial Officer Pursuant to Securities Exchange Act Rule 13a-14(a)
- 32.1\*\* Certification of Chief 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 Chief 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 Extension Schema Document
- 101.CAL\* XBRL Taxonomy Extension Calculation Linkbase Document
- 101.DEF\* XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB\* XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE\* XBRL Taxonomy Extension Presentation Linkbase Document

\* Filed herewith.

\*\* Furnished herewith.

**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.

Dated: October 26, 2016 WESTWOOD HOLDINGS GROUP, INC.

By: /s/ Brian O. Casey  
Brian O. Casey  
President & Chief Executive Officer

By: /s/ Tiffany B. Kice  
Tiffany B. Kice  
Chief Financial Officer and Treasurer