Financial Engines, Inc.
Form 10-Q
August 08, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2017

OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
Commission File No. 001-34636

FINANCIAL ENGINES, INC.

(Exact name of registrant as specified in its charter)

Delaware	94-3250323
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1050 Enterprise Way, 3rd Floor

Sunnyvale, CA 94089

(Address of principal executive offices, Zip Code)

(408) 498-6000

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate 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, smaller reporting company, or an emerging growth company. See definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act. (Check one):

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

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

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

As of July 31, 2017, 63,155,310 shares of Common Stock, par value $0.0001, were outstanding.

FINANCIAL ENGINES, INC.

INDEX TO QUARTERLY REPORT ON FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2017

PART I: FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements (Unaudited)

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(Unaudited)

	December 31, 2016		June 30, 2017	
	(In thousands, except per share data)			
Assets				
Current assets:				
Cash and cash equivalents	$	134,246	$	169,918
Accounts receivable, net		103,256		111,163
Prepaid expenses		7,370		8,937
Other current assets		3,468		4,647
Total current assets		248,340		294,665
Property and equipment, net		24,532		23,823
Intangible assets, net		205,751		201,748
Goodwill		312,020		312,020
Long-term deferred tax assets		40,504		55,478
Direct response advertising, net		5,849		4,784
Other assets		3,140		1,617
Total assets	$	840,136	$	894,135
Liabilities and Stockholders’ Equity				
Current liabilities:				
Accounts payable	$	36,780	$	31,031
Accrued compensation		27,667		16,303
Deferred revenue		4,701		4,629
Dividend payable		4,350		4,416
Other current liabilities		4,343		3,086
Total current liabilities		77,841		59,465
Long-term deferred rent		12,269		11,547
Long-term tax liabilities		2,207		—
Other liabilities		488		500

Total liabilities		92,805			71,512	
Contingencies (see Note 11)						
Stockholders' equity:						
Preferred stock, $0.0001 par value - 10,000 authorized as of December 31, 2016 and June 30, 2017; None issued or outstanding as of December 31, 2016 and June 30, 2017		—			—	
Common stock, $0.0001 par value - 500,000 authorized as of December 31, 2016 and June 30, 2017; 63,476 and 64,400 shares issued and 62,199 and 63,123 shares outstanding as of December 31, 2016 and June 30, 2017, respectively		6			6	
Additional paid-in capital		782,079			817,994	
Treasury stock, at cost (1,277 shares and 1,277 shares as of December 31, 2016 and June 30, 2017, respectively)		(47,637	)		(47,637	)
Retained Earnings		12,883			52,260	
Total stockholders' equity		747,331			822,623	
Total liabilities and stockholders' equity	$	840,136		$	894,135	

See accompanying notes to the unaudited condensed consolidated financial statements.

1

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Income

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2017	2016	2017
	(In thousands, except per share data)			
Revenue:				
Professional management	$96,071	$110,640	$178,877	$217,400
Platform	7,173	6,784	14,271	13,678
Other	2,989	1,050	5,143	1,491
Total revenue	106,233	118,474	198,291	232,569
Costs and expenses:				
Cost of revenue	46,540	53,286	85,871	104,811
Research and development	8,967	11,119	18,234	21,687
Sales and marketing	21,686	21,189	40,149	40,504
General and administrative	9,809	8,566	24,409	20,760
Amortization of intangible assets, including internal use software	4,099	4,231	7,125	8,394
Total costs and expenses	91,101	98,391	175,788	196,156
Income from operations	15,132	20,083	22,503	36,413
Interest (expense) income	(20)	196	(16)	263
Other expense, net	(427)	(44)	(460)	(172)
Income before income taxes	14,685	20,235	22,027	36,504
Income tax expense	5,642	7,432	9,655	11,527
Net and comprehensive income	$9,043	$12,803	$12,372	$24,977
Dividends declared per share of common stock	$0.07	$0.07	$0.14	$0.14
Net income per share attributable to holders of common stock				
Basic	$0.15	$0.20	$0.21	$0.40
Diluted	$0.14	$0.20	$0.20	$0.39
Shares used to compute net income per share attributable to holders of common stock				
Basic	61,716	62,998	59,986	62,723
Diluted	62,770	64,826	60,979	64,666

See accompanying notes to the unaudited condensed consolidated financial statements.

2

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended June 30, 2016	2017
	(In thousands)	
Cash flows from operating activities:		
Net income	$12,372	$24,977
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,307	4,202
Amortization of intangible assets	6,922	8,130
Stock-based compensation	14,727	17,602
Amortization of deferred sales commissions	831	575
Amortization and impairment of direct response advertising	2,425	1,951
Amortization of discount on short-term investments	(5)	—
Provision for doubtful accounts	455	304
Write-off of notes receivable	240	—
Deferred tax	4,462	10,053
Loss on fixed asset disposal	133	155
Loss on sale of short-term investments	18	—
Changes in operating assets and liabilities, net of acquired assets and liabilities:		
Accounts receivable	(1,207)	(8,211)
Prepaid expenses	(1,447)	(1,650)
Direct response advertising	(1,740)	(906)
Other assets	(1,816)	(1,392)
Accounts payable	(7,492)	(6,668)
Accrued compensation	(5,059)	(11,364)
Deferred revenue	(312)	(145)
Deferred rent	699	(93)
Other liabilities	(2,131)	(24)
Net cash provided by operating activities	26,382	37,496
Cash flows from investing activities:		
Purchase of property and equipment	(3,955)	(2,345)
Capitalization of internal use software	(3,568)	(3,947)
Sale of short-term investments	39,923	—
Cash paid for acquisitions, net of cash acquired	(254,610)	—
Net cash used in investing activities	(222,210)	(6,292)
Cash flows from financing activities:		
Payments on capital lease obligations	(53)	(67)
Payments related to business combinations	—	(2,093)
Net share settlements for minimum tax withholdings	(656)	(3,496)
Proceeds from issuance of common stock	1,112	18,872
Cash dividend payments	(8,553)	(8,748)

Net cash (used in) provided by financing activities	(8,150)	4,468
Net (decrease) increase in cash and cash equivalents	(203,978)	35,672
Cash and cash equivalents, beginning of period	305,216	134,246
Cash and cash equivalents, end of period	$101,238	$169,918
Supplemental cash flows information:		
Income taxes paid, net of refunds	$2,389	$6,168
Interest paid	$7	$57
Non-cash operating, investing and financing activities:		
Issuance of common stock related to acquisition	$267,018	$—
Unpaid purchases of property and equipment	$680	$1,113
Purchase of property and equipment with noncash tenant improvement allowance	$1,924	$162
Purchase of property and equipment under capital lease	$—	$221
Capitalized stock-based compensation for internal use software	$388	$444
Capitalized stock-based compensation for direct response advertising	$42	$28
Dividends declared but not yet paid	$3,697	$4,416

See accompanying notes to the unaudited condensed consolidated financial statements.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1 — Organization and Description of the Business

The Company

Financial Engines, Inc. (the Company) was incorporated on May 13, 1996 under the laws of the State of California and is headquartered in Sunnyvale, California. In February 2010, the Company was reincorporated under the laws of the State of Delaware.

The Company is a leading provider of independent, technology-enabled comprehensive financial advisory services, discretionary portfolio management, personalized investment advice, financial and retirement income planning, financial education and guidance. The Company helps individuals, either online or with an advisor, develop a strategy to reach investing and retirement goals by offering a comprehensive set of services, including holistic, personalized plans for saving and investing, assessments of retirement income, and the option to meet face-to-face with a dedicated financial advisor at one of more than 130 advisor centers nationwide. The Company's advice and planning services cover employer-sponsored defined contribution (DC) accounts (401(k), 457, and 403(b) plans), IRA accounts, and taxable accounts.

The Company's business model is based primarily on providing advisory services to DC plan participants in the workplace. The Company also provides advisory services directly to individual clients outside of the workplace. Clients are defined as individuals who utilize our services, including Professional Management, Personal Advisor, Online Advice, education or guidance. The Company works with three key constituencies: individual investors, plan sponsors (employers offering DC plans to their employees) and plan providers (companies providing administrative services to plan sponsors).

The Company's investment advisory and management services are provided through its subsidiary, Financial Engines Advisors L.L.C., a federally registered investment adviser. In February 2016, the Company completed the acquisition of Kansas City 727 Acquisition LLC, a Delaware limited liability corporation, as well as its subsidiaries (collectively, The Mutual Fund Store).

NOTE 2 — Basis of Presentation and Principles of Consolidation

Interim Financial Statements

The accompanying condensed consolidated financial statements and notes thereto are unaudited. These unaudited interim condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) and applicable rules and regulations of the Securities and Exchange Commission (SEC) regarding interim financial reporting. Certain information and note disclosures normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. Accordingly, these unaudited interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes contained in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2016, as filed on February 27, 2017 with the SEC (the 2016 Annual Report). The Condensed Consolidated Balance Sheet as of December 31, 2016, included herein, was derived from the audited financial statements as of that date but does not include all disclosures including notes required by GAAP.

The unaudited condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments necessary for the fair presentation of the Company’s Balance Sheets as of December 31, 2016 and June 30, 2017, the Company’s Statements of Income for the three and six months ended June 30, 2016 and 2017 and the Company’s Statements of Cash Flows for the six months ended June 30, 2016 and 2017. The results for the three and six months ended June 30, 2017 are not necessarily indicative of the results to be expected for the year ending December 31, 2017.

The unaudited condensed consolidated financial statements include the accounts of the Company and all of its subsidiaries. Intercompany balances and transactions have been eliminated in consolidation. Comprehensive income is defined as the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. Comprehensive income is the same as net income for all periods presented.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the reporting period. Actual results could differ from those estimates under different assumptions or conditions.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

Segment Information

The Company's chief operating decision-maker, its chief executive officer, reviews the Company's operating results on an aggregate, consolidated basis and manages its operations as a single operating segment. In addition, all of the Company's operations and assets are based in the United States.

Business Combinations

The Company accounts for business combinations under the acquisition method. The cost of an acquired company is assigned to the tangible and intangible assets acquired and the liabilities assumed on the basis of their fair values at the date of acquisition. The determination of fair values of assets acquired and liabilities assumed requires management to make estimates and use valuation techniques when market values are not readily available. Any excess of the aggregate purchase price over the fair value of net tangible and identifiable intangible assets acquired is allocated to goodwill. Transaction costs associated with business combinations are expensed as incurred.

Goodwill and Intangible Assets

Goodwill consists of the excess of the aggregate purchase price over the fair value of net tangible and identifiable intangible assets acquired by the Company. The carrying amount of goodwill is tested for impairment each year in the fourth quarter, or more frequently if facts and circumstances warrant a review, by using a two-step process. The Company has concluded that it has a single reporting unit for the purpose of goodwill impairment testing, and accordingly, all goodwill resides within a single reporting unit. The Company compares the fair value of the reporting unit with its carrying amount, including goodwill. If the fair value of the reporting unit exceeds its carrying value, goodwill of the reporting unit is not considered impaired. If the carrying value of the reporting unit exceeds its fair value, the Company would perform a measurement of the amount of impairment by comparing the carrying amount of the goodwill to a determination of the implied fair value of the goodwill. If the carrying amount of the goodwill is greater than the implied value, an impairment loss is recognized for the difference. There have been no goodwill impairment losses recognized to date.

The Company does not have any indefinite lived intangible assets besides goodwill. Intangible assets with definite useful lives are recorded their acquired value less accumulated amortization. Intangible assets are reviewed for impairment whenever events or changes in circumstances raise doubt about recoverability of the net assets. Such reviews include an analysis of current results and take into consideration the undiscounted value of projected operating cash flows. There were no impairments or changes in useful lives of acquired intangible assets for the periods presented.

Intangible assets consist primarily of customer relationships, trademarks, trade names, internal use software and reacquired franchisee rights. These intangible assets are acquired through business combinations or, in the case of capitalized software costs, are internally developed. Intangible assets are amortized on a straight-line basis over their estimated useful lives which range from less than 1 year to 20 years.

Long-Lived Assets

Long-lived assets, such as property, equipment, direct response advertising and intangible assets, including capitalized internal use software, subject to depreciation and amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset or an asset group may not be recoverable. When such events or changes in circumstances occur, the Company assesses recoverability by determining whether the carrying value of such assets or asset group will be recovered through the undiscounted expected future cash flows. If the future undiscounted cash flows of the assets or asset group are less than their carrying amount, the Company would recognize an impairment loss based on any excess of the carrying amount of the asset or asset group over their fair value.

Management evaluates the useful lives of these assets on an annual basis and tests for impairment whenever events or changes in circumstances occur that could impact the recoverability of these assets. Impairment charges related to long-lived assets were immaterial for the periods presented.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

Revenue Recognition

The Company recognizes revenue when all of the following conditions are met:

- There is persuasive evidence of an arrangement, as evidenced by a signed contract;
- Delivery has occurred or the service has been made available to the customer, which occurs upon completion of implementation and connectivity services, if applicable, and acceptance by the customer;
- The collectability of the fees is reasonably assured; and
- The amount of fees to be paid by the customer is fixed or determinable.

The Company generates its revenue through three primary sources: professional management, platform and other revenue.

Professional Management. The Company derives professional management revenue from client fees paid by or on behalf of both DC and individual investor clients who are enrolled in one of its discretionary portfolio management services (either the Professional Management service or the Personal Advisor service) for the management of their account assets. The Company continues to use the term professional management revenue to include revenue from both the Professional Management and Personal Advisor services. The Company’s Professional Management service is a discretionary personalized portfolio management service for DC participants who want to work with or delegate the management of their retirement accounts to a professional with the help of an advisor team. Personal Advisor is a personalized service that can provide discretionary portfolio management on a client’s 401(k), IRA and/or taxable assets, as well as comprehensive financial planning and a dedicated advisor representative that participants can meet with in person, online or by phone. The Company’s retirement income solutions, including Income+ and Retirement Paycheck, which are features of its Professional Management and Personal Advisor services, respectively, provide clients approaching or in retirement with discretionary portfolio management with an income objective and steady monthly payments from their accounts during retirement, including Social Security claiming guidance and planning. The services are generally made available to prospective clients by written agreements with the plan provider, the plan sponsor and the plan participant in a DC plan (and may be provided on a subadvisory basis) and by written agreements with individual investors.

The Company’s arrangements with clients using discretionary portfolio management services generally provide for fees based on the value of assets managed and are generally payable quarterly in arrears. The majority of client fees for DC accounts, for both advisory and subadvisory relationships, are calculated on a monthly basis, as the product of client fee rates and the value of assets under management (AUM) at or near the end of each month. For IRA and taxable accounts, client fees are calculated on a quarterly basis at the end of each quarter.

Platform. The Company derives platform revenue from recurring, subscription-based fees for access to its services, including Online Advice, education and guidance, and to a lesser extent, from setup fees. Online Advice is a non-discretionary, Internet-based investment advisory service, which includes personalized online savings and investment advice and retirement income projections for clients who want to manage their retirement themselves. The arrangements generally provide for fees to be paid by the plan sponsor, plan provider or the DC plan itself, depending on the plan structure. Platform revenue is generally paid annually or quarterly in advance and recognized ratably over the term of the subscription period beginning after the completion of customer setup and data connectivity. Setup fees are recognized ratably over seven years.

Other. Other revenue includes reimbursement for a portion of marketing and client materials from certain subadvisory relationships. Non-retirement account servicing fees were applicable for the period of February 1, 2016 to December 31, 2016. The fees for non-retirement account servicing do not impact client fees paid for discretionary portfolio management services, and are disclosed in the applicable Form ADV of the Company's advisory subsidiaries. Franchise royalty fees were applicable for the period of February 1, 2016 to September 30, 2016, as the Company had acquired all remaining franchises as of October 2016. Professional management revenue earned subsequent to the respective acquisition date of the franchises is included in professional management revenue. The franchise royalty fees were recognized as revenue as the services were performed by the franchisees and were based on specified percentages of the franchisees' advisory fees billed to their clients, which were primarily based on predetermined percentages of the market value of the AUM and were affected by changes in the AUM. Costs associated with reimbursed printed fulfillment materials are expensed to cost of revenue as incurred.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

Cost of Revenue

Cost of revenue includes fees paid to plan providers for connectivity to plan and plan participant data, printed materials fulfillment costs for certain subadvisory relationships for which a portion are reimbursed, printed client materials, and employee-related costs for in-person dedicated advisor centers and call center advisors, operations, implementations, technical operations, portfolio management and client service administration. Costs in this area are related primarily to payments to third parties, employee compensation and related expenses, facilities expenses, purchased materials and depreciation.

The expenses included in cost of revenue are shared across the different revenue categories, and the Company is not able to meaningfully allocate such costs between separate categories of revenue. Consequently, all costs and expenses applicable to the Company's revenue are included in the category cost of revenue in the Unaudited Condensed Consolidated Statements of Income. A portion of the amortization of intangible assets, including internal use software, relates to the Company's cost of revenue but is reflected together with all amortization of intangible assets as a separate line item in the Company's Unaudited Condensed Consolidated Statements of Income.

Recent Accounting Pronouncements

On May 28, 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. (ASU) 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. This new standard may also impact how the Company accounts for certain direct costs associated with its revenues. Subsequently, the FASB also issued a series of amendments to the new revenue standard.

These ASUs, which are required to be adopted together will replace most existing revenue recognition guidance in GAAP. The Company intends to adopt these ASUs on January 1, 2018 using either the retrospective or cumulative effect transition method. The Company has not yet selected a transition method, but expects to do so in the second half of 2017 upon completion of further analysis.

Currently, the Company is in the process of reviewing its historical contracts to quantify the impact that the adoption of these standards will have on the identification of and accounting for performance obligations, and on the recognition of costs related to obtaining customer contracts (namely sales commissions and marketing costs). The Company anticipates the adoption of these ASUs will impact the timing of recognition and classification in its consolidated financial statements of certain costs it incurs to obtain sales contracts from its customers. For example, there are direct response advertising costs that the Company currently capitalizes and amortizes for certain printed materials associated with new customer solicitations. Under the new guidance, the Company expects these costs to be expensed as incurred. The Company also expects the new guidance will require additional disclosures. The Company continues to evaluate the impact the update will have on its consolidated financial statements and related disclosures.

On February 25, 2016, FASB issued ASU No. ASU 2016-02, Leases, which requires that lessees recognize assets and liabilities for leases with lease terms greater than twelve months in the balance sheet. The ASU also requires additional disclosures to help users of financial statements better understand the amount, timing and uncertainty of cash flows arising from leases. The ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, with early adoption permitted. Adoption of the standard will require a modified retrospective approach. The Company plans to adopt this ASU on January 1, 2019 and is evaluating the effect that ASU 2016-02 will have on its consolidated financial statements and related disclosures.

On August 26, 2016, FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. This ASU clarifies and provides guidance on eight specific cash flow classification issues that are not currently addressed by current GAAP thereby reducing current diversity in practice. Although early adoption is permitted, the Company plans to adopt the ASU on January 1, 2018 and does not expect it to have a material impact on its consolidated financial statements.

On January 26, 2017, FASB issued ASU No. 2017-04, “Simplifying the Test for Goodwill Impairment.” This standard simplifies the measurement of goodwill impairment by removing the second step of the goodwill impairment test, which requires the determination of the fair value of individual assets and liabilities of a reporting unit. Under this guidance, goodwill impairment is to be measured as the amount by which a reporting unit’s carrying value exceeds its fair value with the loss recognized not to exceed the total amount of goodwill allocated to the reporting unit. The standard will be applied prospectively and is effective for impairment tests performed after December 15, 2019, with early adoption permitted. The standard is not expected to have a material effect on the Company's consolidated financial statements once implemented.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

Recently Adopted Accounting Standards

On March 30, 2016, FASB issued ASU No. 2016-09, Compensation-Stock Compensation (Topic 718): Improvement to Employee Share-Based Payment Accounting. The new standard: (a) requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled, (b) requires classification of excess tax benefits as an operating activity in the statement of cash flows rather than a financing activity, (c) eliminates the requirement to defer recognition of an excess tax benefit until the benefit is realized through a reduction to taxes payable, (d) modifies statutory withholding tax requirements, and (e) provides for a policy election to account for forfeitures as they occur. The ASU is effective for fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. The Company adopted the new standard on January 1, 2017.

As a result of the adoption of the new standard, the Company recorded all income tax effects of share-based awards in its provision for income taxes in its Unaudited Condensed Consolidated Statements of Income for the three and six months ended June 30, 2017. On January 1, 2017, the Company also recorded a cumulative effect adjustment of $24.4 million as an increase of retained earnings on the Company's Unaudited Condensed Consolidated Balance Sheet, which included an increase to deferred tax assets of approximately $27.1 million related primarily to the recognition of excess tax benefits from stock-based compensation. Additionally, the Company adopted the change in presentation in the Unaudited Condensed Consolidated Statements of Cash Flows related to excess tax benefits on a retrospective basis. The Unaudited Condensed Consolidated Statement of Cash Flows for the six months ended June 30, 2016 was adjusted as follows: a $5.4 million increase to net cash provided by operating activities and a $5.4 million increase to net cash used in financing activities. There was no impact for the change in presentation in the statement of cash flows related to statutory tax withholding requirements because the Company has historically classified the statutory tax withholding as a financing activity in its Unaudited Condensed Consolidated Statements of Cash Flows.

In October 2016, FASB issued ASU No. 2016-16, Income Taxes (Topic 740): Intra-Entity Transfer of Assets Other than Inventory (ASU 2016-16), which requires the recognition of the income tax consequences of an intra-entity transfer of an asset, other than inventory, when the transfer occurs. ASU 2016-16 will be effective for the Company in its first quarter of 2018, but the Company early adopted the new standard as of January 1, 2017. The cumulative impact of applying this guidance to retained earnings was approximately $1.1 million.

NOTE 3 – Business Combinations

Acquisition of The Mutual Fund Store

On February 1, 2016, the Company completed the acquisition of The Mutual Fund Store for an aggregate purchase price of $513.0 million, consisting of approximately $246.0 million in cash, net of cash acquired of $5.0 million and 9,885,889 shares of common stock valued at $267 million, pursuant to an Agreement and Plan of Mergers, dated

November 5, 2015, as amended. The acquisition has enabled the Company to expand its independent advisory services to defined contribution participants through comprehensive financial planning and the option to meet face-to-face with a dedicated financial advisor.

During the six months ended June 30, 2016, the Company incurred transaction costs totaling $6.2 million that were expensed as incurred in general and administrative expense in its Unaudited Condensed Consolidated Statements of Income. There were no transaction expenses incurred for the three months ended June 30, 2016 or the three or six months ended June 30, 2017 in connection with this acquisition.

The Mutual Fund Store had an existing compensation arrangement with its key executives for $5.8 million. Fifty percent of the compensation payment, approximately $2.9 million, was paid upon the closing of the acquisition and is reflected in the purchase consideration transferred at closing. The remaining fifty percent of the compensation payment, approximately $2.9 million, required the executives to be employed with the Company for agreed-upon service periods and therefore is accounted for as post-combination compensation expense. Approximately $1.3 million was paid related to this compensation arrangement during the six months ended June 30, 2017.

During the six months ended June 30, 2017, the Company paid $2.1 million primarily for previously withheld consideration for acquisition of The Mutual Fund Store and acquisition of franchises in 2016.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

Acquisition of Franchises

In April 2016, the Company completed the acquisition of seven franchises for a total aggregate cash consideration of $14.4 million, including $0.8 million of holdbacks reserved with respect to indemnification claims on behalf of the Company. In July and August 2016, the Company completed the acquisition of six franchises for a total aggregate cash consideration of $8.1 million, including $0.3 million of holdbacks. In October 2016, the Company completed the acquisition of eight franchises for a total aggregate cash consideration of $12.8 million, including $0.6 million of holdbacks. The purchase price accounting for the October 2016 franchise acquisitions was finalized during the three months ended March 31, 2017 with no adjustments to the preliminary allocation disclosed as of December 31, 2016.

NOTE 4 — Cash and Cash Equivalents

The Company considers all highly liquid investments with an original maturity of three months or less from date of purchase to be cash equivalents. Cash equivalents are comprised of cash held primarily in money market accounts. Cash and cash equivalents consist of the following:

	December 31, 2016	June 30, 2017
	(In thousands)	
Cash	$84,169	$24,626
Money market fund	50,077	145,292
Total cash and cash equivalents	$134,246	$169,918

NOTE 5 — Short-Term Investments

Short-term investments consisted of U.S. Treasury securities. In January 2016, the Company sold all short-term investments, totaling $39.9 million, and realized gains or losses, net of tax, were immaterial.

NOTE 6 — Concentration of Credit Risk and Fair Value of Financial Instruments

The Company measures and reports its investments in money market funds at fair value on a recurring basis, which approximates their carrying value due to the short period of time to maturity. There have been no changes in the Company's valuation techniques during the six months ended June 30, 2017. The money market funds are classified as Level 1.

The following table summarizes the Company's financial assets measured at fair value on a recurring basis:

	As of December 31, 2016				As of June 30, 2017			
	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1) [1]	Significant Other Observable Inputs (Level 2) [2]	Significant Other Unobservable Inputs (Level 3) [3]	Total Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1) [1]	Significant Other Observable Inputs (Level 2) [2]	Significant Other Unobservable Inputs (Level 3) [3]
	(In thousands)							
Assets:								
Money Market Funds	$50,077	$ 50,077	$ —	$ —	$145,292	$ 145,292	$ —	$ —

(1) Level 1: Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

(2) Level 2: Inputs reflect quoted prices for identical assets or liabilities in markets that are not active; quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the assets or liabilities; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.

(3) Level 3: Unobservable inputs reflecting the Company's own assumptions incorporated in valuation techniques used to determine fair value. These assumptions are required to be consistent with market participant assumptions that are reasonably available.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist principally of cash, cash equivalents and accounts receivable. The Company maintains its cash and cash equivalents primarily in highly-rated taxable money market funds which hold securities issued or guaranteed by the United States government or their agencies. These deposits may exceed federal deposit insurance limits. The fair value of the Company's money market funds is based on a trade date basis on the last business day of the accounting period. The fair value of the Company's accounts receivable and accounts payable approximates the carrying amount due to their short duration.

The Company's customers are concentrated in the United States. The Company performs ongoing credit evaluations of its customers and does not require collateral. The Company reviews the need for allowances for potential credit losses and such losses have been insignificant to date.

The Company did not have any customers that comprised 10% or more of the accounts receivable balance as of December 31, 2016 or June 30, 2017. The Company also did not have any customer that comprised 10% or more of revenue for the three and six months ended June 30, 2016 and 2017.

NOTE 7 — Goodwill and Intangible Assets

There were no transactions or events that impacted goodwill during the six months ended June 30, 2017. Accordingly, goodwill was $312.0 million at both December 31, 2016 and June 30, 2017.

Intangible assets as of December 31, 2016 and June 30, 2017 consisted of the following:

		December 31, 2016 (In thousands)			June 30, 2017		
	Useful Life (years)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	14 - 19	$164,338	$ 7,781	$ 156,557	$164,338	$ 12,228	$ 152,110
Franchise agreements and reacquired franchisee rights	<1 - 9	2,697	498	2,199	2,697	644	2,053

Favorable leases, net	6	140	22	118	140	34	106
Trademarks/Trade names	20	39,230	1,810	37,420	39,230	2,798	36,432
Internal use software	2 - 4	60,965	51,508	9,457	65,356	54,309	11,047
Total		$267,370	$ 61,619	$ 205,751	$271,761	$ 70,013	$ 201,748

Amortization expense related to intangible assets was as follows:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2016	2017	2016	2017
	(In thousands)			
Customer relationships	$2,087	$2,224	$3,415	$4,447
Franchise agreements and reacquired franchisee rights	329	73	343	146
Favorable leases, net	6	6	10	12
Trademarks/Trade names	494	494	823	988
Internal use software(1)	1,183	1,434	2,534	2,801
Amortization expense	$4,099	$4,231	$7,125	$8,394

(1) For the three and six months ended June 30, 2016, internal use software amortization included approximately $0.1 million and $0.2 million of stock-based compensation expense, respectively, and for the three and six months ended June 30, 2017, internal use software amortization included approximately $0.2 million and $0.3 million of stock-based compensation expense, respectively.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

The following table presents the estimated future amortization of intangible assets as of June 30, 2017:

(In thousands)	
Years ending December 31:	
2017	$8,292
2018	15,526
2019	13,572
2020	12,665
2021	11,147
Thereafter	140,546
	$201,748

NOTE 8 — Stockholders' Equity

Stock-based Compensation

The following table summarizes the stock-based compensation, as included in the Unaudited Condensed Consolidated Statements of Income, by functional area:

	Three Months Ended		Six Months Ended	
	June 30, 2016[(1)]	2017	June 30, 2016	2017
	(In thousands)			
Stock-based compensation:				
Cost of revenue	$1,936	$2,555	$3,495	$4,950
Research and development	1,489	2,103	2,579	3,670
Sales and marketing	2,428	2,137	4,569	3,648
General and administrative	2,571	2,228	3,881	5,070
Amortization of internal use software, included in amortization of intangible assets	99	136	203	264
Total stock-based compensation	$8,523	$9,159	$14,727	$17,602

(1) The amounts in the above table for the three and six months ended June 30, 2016, have been adjusted to reflect the appropriate amounts of stock-based compensation recognized for each of the financial statement captions. There was no impact to the total amount of stock-based compensation recognized for the period.

On January 1, 2017, the Company adopted ASU No. ASU 2016-09, Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting and elected to account for forfeitures as they occur, which may cause the timing of stock-based compensation expense to be more volatile.

Stock-based compensation expense for performance stock units (PSUs) associated with the 2013-2017 Long Term Incentive Program (LTIP) is based on the award's fair value as of the grant date, as well as the estimated probability of achieving the objective performance criteria pre-established by the Compensation Committee of the Board of Directors. As of June 30, 2017, the Company determined that certain performance criteria were improbable of achievement and accordingly reversed plan-to-date stock-based compensation expense recognized related to these certain criteria, which was immaterial for the periods presented.

Cash Dividends

On July 25, 2017, the Board of Directors declared a quarterly dividend of $0.07 per share to be paid on October 4, 2017 to record-holders as of September 20, 2017. While the Company currently expects to pay comparable cash dividends on a quarterly basis in the future, any future determination with respect to the declaration and payment of dividends will be at the discretion of the Board of Directors. As of June 30, 2017, the Company had a dividend payable balance of $4.4 million, which was paid to stockholders in July 2017.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

NOTE 9 — Net Income Per Common Share

Basic net income per common share is computed by dividing net income attributable to common stockholders by the weighted average number of common shares outstanding during the period. Diluted net income per common share is computed by giving effect to all dilutive potential common shares, including options, RSUs, and PSUs. Repurchased shares are held as treasury stock and outstanding shares used to calculate earnings per share have been reduced by the weighted number of repurchased shares.

On February 1, 2016, the Company issued 9,885,889 shares of its common stock as part of the consideration to acquire The Mutual Fund Store.

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

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2017	2016	2017
	(In thousands, except per share data)			
Numerator (basic and diluted):				
Net income	$9,043	$12,803	$12,372	$24,977
Denominator (basic):				
Net weighted average common shares outstanding	61,716	62,998	59,986	62,723
Denominator (diluted):				
Weighted average common shares outstanding	61,716	62,998	59,986	62,723
Dilutive stock options outstanding	590	1,006	602	1,073
Dilutive unvested restricted stock units	451	805	379	853
Dilutive unvested performance stock units	13	17	12	17
Net weighted average common shares outstanding	62,770	64,826	60,979	64,666
Net income per share attributable to holders of common stock:				
Basic	$0.15	$0.20	$0.21	$0.40
Diluted	$0.14	$0.20	$0.20	$0.39

Diluted net income per share does not include the effect of the following anti-dilutive common equivalent shares:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2017	2016	2017
	(In thousands)			
Stock options outstanding	3,905	1,502	3,574	1,307
Restricted stock units outstanding	—	1	139	86
Total anti-dilutive common equivalent shares	3,905	1,503	3,713	1,393

NOTE 10 — Income Taxes

The Company recorded an income tax provision of $5.6 million and $7.4 million for the three months ended June 30, 2016 and 2017, resulting in an effective tax rate of 38% and 37%, respectively. During the three months ended June 30, 2017, the Company's effective tax rate decreased due primarily to adopting ASU 2016-09, effective January 1, 2017, which requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled.

FINANCIAL ENGINES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (Continued)

(Unaudited)

The Company recorded an income tax provision of $9.7 million and $11.5 million for the six months ended June 30, 2016 and 2017, respectively, resulting in an effective tax rate of 44% and 32%, respectively. During the six months ended June 30, 2016, the Company’s effective tax rate increased as compared to the statutory rate due primarily to non-deductible expenditures incurred in connection with acquisition activity. During the six months ended June 30, 2017, the Company’s effective tax rate decreased as compared to the statutory rate due primarily to adoption of ASU 2016-09, effective January 1, 2017.

The Company is subject to income taxes in the U.S. federal jurisdiction and various state jurisdictions. All tax years since inception are open due to loss carryforwards and may be subject to examination in one or more jurisdictions.

At December 31, 2016, the Company had net operating loss carryforwards for federal purposes of approximately $83.1 million that expire at varying dates through 2036.

As of December 31, 2016, the Company continued to believe that sufficient positive evidence exists from historical operations and future projections to conclude that it is more likely than not to fully realize its deferred tax assets in future periods. The Company continuously evaluates facts representing positive and negative evidence in the determination of the realizability of the deferred tax assets. As of December 31, 2016, the Company had gross unrecognized tax benefits for income taxes associated with uncertain tax positions of $5.5 million, and does not expect this to change materially for the remainder of the year.

On January 1, 2017, the Company adopted ASU 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting, which requires excess tax benefits and deficiencies to be a component of income tax expense, and has increased volatility within the Company's provision for income taxes as the amount of excess tax benefits or deficiencies from stock-based compensation awards are dependent on the stock price at the date the awards vest. As a result, the Company's income tax expense and associated effective tax rate will be impacted by fluctuations in stock price between the grant dates and vesting dates of equity awards. For the three and six months ended June 30, 2017, the excess benefits from stock options decreased the effective tax rate by 2% and 7%, respectively.

NOTE 11— Commitments and Contingencies

Service Level Agreements

The Company includes service level agreements with its customers warranting certain levels of reliability and performance. The maximum total commitments under these obligations would have less than a $1.0 million impact on the Company's annual operating results.

Self-Insurance

The Company provides self-insured medical benefits for employees based upon their coverage elections. The medical plan carries a stop-loss policy which will protect from individual claims during the plan year exceeding $100,000 and when cumulative medical claims exceed 120% of expected claims for the plan year. The Company records estimates of the total costs of claims incurred based on an analysis of historical data. The liability for self-insured medical claims is included within accrued compensation and benefits in the Company's Unaudited Condensed Consolidated Balance sheet and was $0.4 million as of June 30, 2017.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

This Report contains forward-looking statements that involve risks and uncertainties. In some cases, you can identify forward-looking statements by terms such as “may,” “will,” “goal,” “intend,” “could,” “can,” “would,” “expect,” “believe,” “d “estimate,” “predict,” “potential,” “plan,” or the negative of these terms, and similar expressions intended to identify forward-looking statements. These statements reflect our current views with respect to future events and are based on assumptions and subject to risks and uncertainties. Given these uncertainties, you should not place undue reliance on these forward-looking statements. Forward-looking statements include, but are not limited to, statements regarding: anticipated trends and challenges in our business and the markets in which we operate; the capabilities, benefits and effectiveness of our services; our strategy; our plans for future services, enhancements of existing services and our growth; the effect of the integration of the acquisition of The Mutual Fund Store on our business, financial condition and operating results, including our revenue and expenses; the impact of our commitments of our obligations under our service level agreements with customers; our expectations regarding our expenses and revenue; our headcount; our effective tax rate, our deferred tax assets, our anticipated cash needs and uses of cash; the amount and timing of our expected cash expenditures associated with capital improvements to our advisor centers; our estimates regarding our capital requirements and our needs for additional financing; factors which may impact our professional management operating metrics; the utility of these metrics, including our belief that DC AUC and eligible prospective clients are useful indicators of potential DC AUM and clients available for enrollment into our Professional Management service; factors which may impact AUM, including market performance, enrollment, and cancellation rates; estimated cash incentive compensation payments, including the amounts and timing thereof, expectations regarding cash payments for tax withholding, including the amounts and timing thereof, our exposure to market risk, including our expectations regarding the percentage of revenue derived from fees based on the market value of AUM increasing over time and the impact our fee calculation methodologies, our ability to retain and attract customers; our regulatory environment; our expectations regarding the amounts, timing and frequency of any payment of dividends; our expectations for granting equity awards, and the potential financial and accounting impact related thereto; impact of our accounting policies including the anticipated effects of adopting accounting standards updates; benefit of non-GAAP financial measures; our disclosure controls and procedures; our expectations regarding competition; and sources of revenue. These statements involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performances or achievements expressed or implied by the forward-looking statements. Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those projected. These risks and uncertainties include, but are not limited to, the risks set forth throughout this Report, including under Item 1A, “Risk Factors.” These forward-looking statements speak only as of the date hereof. We expressly disclaim any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in our expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

Financial Engines, Inc. was incorporated on May 13, 1996 under the laws of the state of California and is headquartered in Sunnyvale, California. In February 2010, Financial Engines, Inc. was reincorporated in the state of Delaware. Our investment advisory and management services are provided through our subsidiary, Financial Engines Advisors L.L.C., a federally registered investment adviser. In February 2016, we completed the acquisition of Kansas City 727 Acquisition LLC, a Delaware limited liability corporation, as well as its subsidiaries and certain affiliates (collectively, The Mutual Fund Store). The Mutual Fund Store operated as a federally registered investment advisor. References in this Report to “Financial Engines,” “our company” “we,” “us” and “our” refer to Financial Engines, Inc. and its consolidated subsidiaries during the periods presented unless the context requires otherwise.

Overview

We are a leading provider of independent, technology-enabled comprehensive financial advisory services, discretionary portfolio management, personalized investment advice, financial and retirement income planning, financial education and guidance. We help individuals, either online or with an advisor, develop a strategy to reach investing and retirement goals by offering a comprehensive set of services, including holistic, personalized plans for saving and investing, assessments of retirement income, and the option to meet face-to-face with a dedicated financial advisor at one of more than 130 advisor centers nationwide. Our advice and planning services cover employer-sponsored defined contribution (DC) accounts (401(k), 457, and 403(b) plans), IRA accounts, and taxable accounts.

We use our proprietary advice technology platform to provide our services to millions of DC plan participants in the workplace and individuals outside of the workplace on a cost-efficient basis. We believe that our services have significantly increased the accessibility to plan participants of low-cost, high-quality, independent, personalized portfolio management services, investment advice and retirement income planning.

Our business model is based primarily on providing advisory services to DC plan participants in the workplace. We also provide advisory services directly to individual clients outside of the workplace. Clients are defined as individuals who utilize our services, including Professional Management, Personal Advisor, Online Advice, education or guidance. We work with three key constituencies: individual investors, plan sponsors (employers offering DC plans to their employees) and plan providers (companies providing administrative services to plan sponsors).

We maintain two types of relationships with DC plan providers. In direct advisory relationships, we are the primary advisor and a plan fiduciary. In subadvisory relationships, the plan provider (or its affiliate) is the primary advisor and plan fiduciary, and we act in a subadvisory capacity.

In February 2016, we completed the acquisition of Kansas City 727 Acquisition LLC, a Delaware limited liability corporation, as well as its subsidiaries and certain affiliates, and also completed the acquisition of all franchises during the period April 2016 to October 2016 (collectively, The Mutual Fund Store).

Revenue

We generate revenue through three primary sources: professional management, platform and other revenue.

Professional Management Revenue

We derive professional management revenue from client fees paid by or on behalf of both DC and individual investor clients who are enrolled in one of our discretionary portfolio management services (either the Professional Management service or the Personal Advisor service) for the management of their account assets. We continue to use the term professional management revenue to include revenue from both the Professional Management and Personal Advisor services. Our Professional Management service is a discretionary personalized portfolio management service for DC participants who want to work with or delegate the management of their retirement accounts to a professional with the help of an advisor team. Personal Advisor is a personalized service that can provide discretionary portfolio management on a client’s 401(k), IRA and/or taxable assets, as well as comprehensive financial planning and a dedicated advisor representative that participants can meet with in person, online or by phone. Our retirement income solutions, including Income+ and Retirement Paycheck, which are features of our Professional Management and Personal Advisor services, respectively, provide clients approaching or in retirement with discretionary portfolio management with an income objective and steady monthly payments from their accounts during retirement, including Social Security claiming guidance and planning. The Professional Management service is generally made available to prospective clients by written agreements with the plan provider, the plan sponsor and the plan participant in a DC plan (and may be provided on a subadvisory basis); and the Personal Advisor service is generally made available by written agreements with individual investors for the Personal Advisor service.

Our arrangements with clients using discretionary portfolio management services generally provide for fees based on the value of assets we manage and are generally payable quarterly in arrears. The majority of our client fees for DC accounts, for both advisory and subadvisory relationships, are calculated on a monthly basis, as the product of client fee rates and the value of assets under management (AUM) at or near the end of each month. In general, we expect this monthly methodology to reduce the impact of financial market volatility on this portion of our professional management revenue, although this methodology may result in lower client fees if the financial markets are down when client fees are calculated, even if the market had performed well earlier in the month or the quarter. For IRA and taxable accounts, our client fees are calculated on a quarterly basis at the end of each quarter. In general, we expect this quarterly methodology to potentially result in greater impact of financial market volatility on this portion of our professional management revenue and may result in lower client fees if the financial markets are down when client fees are calculated, even if the market had performed well earlier in the month or the quarter.

Pursuant to the contracts with our clients, we calculate the fees billed to clients based on the asset amounts in data files as received directly from the account provider or custodian, with no judgments or estimates on our part. None of our professional management fee revenue is based on investment performance or other incentive arrangements. Our fees generally are based on AUM, which is influenced by market performance. Our fees are not based on a share of the capital gains or appreciation in a client’s account. In some cases, our client fees or the applicable fee schedule may adjust downward based on overall participant or DC AUM enrollment performance milestones over time. Our client fees are determined by the value of the assets in the client’s account at specified dates and are recognized as the services are performed.

In order to encourage utilization of our Professional Management service, we use a variety of promotional and communication techniques, some of which can potentially impact the amount of revenue recognized, the timing of revenue recognition or both. Historically, we have seen a general preference from workplace plan sponsors to commence campaigns in the second and third quarters of the year and we expect this trend to continue. We would generally expect our professional management revenue to continue to increase as a percentage of overall revenue, which will cause our revenue to become increasingly more sensitive to market performance.

Professional management revenue is earned as services are performed. We use estimates primarily related to the portion of professional management revenue that has not been invoiced and is not otherwise due from the customer at period end.

Professional Management Revenue Metrics

AUM is defined as the amount of assets that we manage as part of our discretionary portfolio management services, including assets managed through franchises during the period of February 2016 to September 2016. Our AUM is the value of assets under management as reported by plan providers and custodians at or near the end of each month or quarter.

DC AUM is the DC asset balances associated with clients enrolled in the Professional Management service, including those at plan sponsors where enrollment campaigns are not yet concluded or have not yet commenced, as of a specified date. We measure enrollment in our Professional Management service by DC clients as a percentage of eligible DC prospective clients and by DC AUM as a percentage of defined contribution account Assets Under Contract (DC AUC). IRA and taxable account AUM represent the IRA and taxable account asset balances associated with those clients enrolled in the Personal Advisor service as of a specified date.

As of June 30, 2017, we had approximately $151.8 billion of AUM, which includes $140.4 billion of DC AUM and $11.4 billion of IRA and taxable account AUM, associated with approximately 1,020,000 total clients.

DC AUC is defined as the amount of assets in DC plans under contract for which the Professional Management service has been made available to eligible prospective clients in the workplace. Our DC AUC and eligible prospective clients do not include assets or prospective clients in DC plans where we have signed contracts but for which we have not yet made the Professional Management service available.

Eligible prospective clients and DC AUC are reported by plan providers with varying frequency and at different points in time, and are not always updated or marked to market. If markets have declined or if assets have left the plan since the reporting date, our DC AUC may be overstated. If markets have risen, or if assets have been added to the plan, since the reporting date, our DC AUC may be understated. Some prospective clients may not be eligible for our services due to plan sponsor limitations on employees treated as insiders for purposes of securities laws or other characteristics of the prospective client. Certain securities within a plan prospective client’s account may be ineligible for management by us, such as employer stock subject to trading restrictions, and we do not manage or charge a fee for that portion of the account. In both of these circumstances, assets of the relevant prospective clients may be included in DC AUC but cannot be converted to DC AUM. We believe that DC AUC can be a useful indicator of the additional DC plan assets available for enrollment efforts that, if successful, would result in these assets becoming DC AUM. We believe that total eligible prospective clients provides a useful approximation of the number of workplace-based prospective clients available for enrollment into our Professional Management service.

As of June 30, 2017, we had approximately $1.143 trillion of DC AUC and 9.7 million eligible prospective clients in DC plans for which the professional management service is available.

As of June 30, 2017, approximately 10.1% of DC eligible prospective clients were enrolled as clients and 12.3% of DC AUC was enrolled as DC AUM.

Changes in AUM

The following definitions are provided and relate to the table below, illustrating estimated changes in our AUM over the last four quarters.

New assets from new clients represents the aggregate amount of new AUM, measured at or near the end of the quarter, from new clients who enrolled in one of our discretionary portfolio management services within the quarter. We receive DC account balances for each new client at least weekly, and accordingly, we are generally able to measure the DC account asset balances within a week of the end of the quarter for new clients. For new clients with new IRA and taxable accounts assets, we are generally able to measure the account balances as of the last day of the quarter. New client assets for IRA and taxable accounts are those assets acquired within a ninety-day period after enrollment during which assets may be rolled into those accounts, and new client assets acquired in the subsequent quarter after enrollment are valued as of the last day of that subsequent quarter.

New assets from existing clients represents the aggregate amount of new AUM within the quarter from existing clients who originally enrolled in one of our discretionary portfolio management services during a prior period. These new assets include employer and employee contributions into DC plan accounts, as well as assets added by existing clients into new or existing IRA and taxable accounts. Employer and employee DC contributions data is estimated each quarter from annual contribution rates based on data received from plan providers or plan sponsors. Typically, we receive data from plan providers or plan sponsors via weekly client files, allowing us to estimate contributions for those clients for whom we have received this data. After the first 90 days, new clients become existing clients. For new IRA and taxable account assets, we are generally able to measure the new assets from existing clients as of the date the additional assets are deposited.

Voluntary cancellations represent the aggregate amount of assets, measured at or near the start of the quarter, for clients who have voluntarily terminated their discretionary portfolio management service relationship within the period. Clients may cancel at any time without any requirement to provide advance notice. Our quarter-end AUM excludes all of the assets of any accounts cancelled by a client prior to the end of the last day of the quarter. We receive DC account balances for each client at least weekly, and accordingly, we are able to measure the DC account asset balances within a week of the start of the quarter for existing clients. For existing IRA and taxable accounts assets, we are able to measure the account balances as of the first day of the quarter.

Involuntary cancellations represent the aggregate amount of DC assets, measured at or near the start of the quarter, for clients whose Professional Management service relationship was terminated within the period for reasons other than a voluntary termination. Such cancellations may occur when all of the client’s account balances have been reduced to zero or when the cancellation of a plan sponsor contract for the Professional Management service has become effective within the period. Plan sponsors may cancel their contract for the provision of Professional Management services upon specified notice or without notice for fiduciary reasons or breach of contract. If a plan sponsor has provided advance notice of cancellation of the plan sponsor contract, however, the AUM for clients of that plan sponsor is included in our AUM until the effective date of the cancellation, which is typically the business day following the termination date, after which it is no longer part of our AUM. If a client’s accounts value falls to zero, either upon the effective date of a sponsor cancellation or as a result of the client transferring the entire balance of their accounts, we will terminate their Professional Management service relationship.

Assets withdrawn by existing clients includes voluntary withdrawals from IRA and taxable accounts. Voluntary withdrawals represent the aggregate amount of assets, measured at the time of withdrawal, for clients who took automatic distributions or who otherwise withdrew funds from their managed IRA or taxable accounts without terminating their service relationship within the period.

Market movement and other factors affecting AUM include estimated market movement, plan administrative and investment advisory fees, client loans, hardship and other defined contribution account withdrawals, and timing differences for the data feeds for clients enrolled in our Professional Management service throughout the period. We expect that market movement would typically represent the most substantial portion of this line item in any given quarter.

The following table illustrates estimated changes in our AUM over the last four quarters:

	Q3'16	Q4'16	Q1'17	Q2'17
	(In billions)			
AUM, beginning of period	$125.3	$134.4	$138.0	$144.4
New assets - new clients	4.4	5.9	3.4	5.3
New assets - existing clients(1)	2.2	2.1	2.4	2.4
Asset cancellations -voluntary	(1.9)	(2.3)	(2.1)	(1.6)
Asset cancellations - involuntary(2)	(1.8)	(2.1)	(2.7)	(3.3)
Assets withdrawn - existing clients	(0.1)	(0.2)	(0.2)	(0.1)
Net new assets	2.8	3.4	0.8	2.7
Market movement and other	6.3	0.2	5.6	4.7
AUM, end of period	$134.4	$138.0	$144.4	$151.8

(1) For Q3’16, Q4’16, Q1’17 and Q2’17, we estimate employer and employee DC plan contributions to be $2.0 billion, $1.9 billion, $2.1 billion and $2.2 billion, respectively. For the last four quarters, the weekly client files contained annual contribution rates, employer matching and salary levels for a subset of our total DC clients, representing approximately 87-92% of our DC clients. Effective Q1’17, we have changed the basis of this estimate from AUM to clients, as this provides a more accurate estimate. The average contribution rate is calculated using this data and extrapolated to approximate 100% of employee and employer contributions for our overall AUM.

(2) Involuntary client cancellations due to the effective date of a plan sponsor cancellation occurring between July 1, 2017 and July 31, 2017 would cause the total AUM that was reported as of June 30, 2017 to be reduced by 0.4%.

Our AUM increases or decreases based on several factors. AUM can increase due to market performance, by the addition of new assets as clients enroll into our discretionary portfolio management services, and by the addition of new assets from existing clients, including from employee and employer contributions into their DC accounts. AUM can decrease due to market performance and by the reduction of assets as a result of clients terminating their relationships, clients rolling their assets out of their accounts, and sponsors canceling our discretionary portfolio management services. Historically, client cancellation rates have typically increased during periods where there has been a significant decline in stock market performance. In addition, client cancellation rates are typically the highest during the six months immediately following the completion of a given promotion, and certain types of promotional techniques may result in higher than average cancellation rates at the end of the promotional period.

As of June 30, 2017, the approximate aggregate style exposure of the accounts we managed was as follows:

Domestic equity	45 %
International equity	28 %
Bonds	24 %
Cash and uncategorized assets(1)	3 %
Total	100 %

1) Uncategorized assets may include CDs, options, warrants and other vehicles not currently categorized.

The percentages in the table above can be affected by the asset exposures of the overall market portfolio of the accounts we manage, the demographics of our client population including the adoption of Income+, the number of clients who have told us that they want to assume greater or lesser investment risk, and, to a lesser extent given the amount of assets we have under management, the proportion of our clients for whom we have completed the transition from their initial portfolio.

A substantial portion of the assets we manage is invested in equity securities, the market prices of which can vary substantially based on changes in economic conditions. An additional portion is invested in fixed income securities, which will generally have lower volatility than the equity market. Therefore, while any changes in equity market performance would significantly affect the value of our AUM, particularly for the AUM invested in equity securities, such changes would typically result in lower volatility for our AUM than the volatility of the equity market as a whole. Because a substantial portion of our revenue is derived from the value of our AUM, changes in fixed income or equity market performance could significantly affect the amount of revenue in a given period. If any of these factors reduces our AUM, the amount of client fees we would earn for managing those assets would decline, which in turn could negatively impact our revenue.

The trends associated with our professional management revenue are driven primarily by trends related to our AUM, as well as the trends related to client fees. The factors primarily affecting our AUM include our ability to enroll and retain clients in our discretionary portfolio management services, to retain existing and to sign new contracts with sponsors, providers and custodians, the level of employee, employer and individual investor contributions and market performance. The factors primarily affecting our client fees include the value of services provided and related industry pricing trends, our fee structures which typically provide for lower overall average fee rates as account balances increase, contractually-negotiated fee rates we receive for our DC subadvisory services, fee changes as a result of achieving certain sponsor-based enrollment milestones for our DC advisory services and contract modifications.

Platform Revenue

We derive platform revenue from recurring, subscription-based fees for access to our services, including Online Advice, education and guidance, and to a lesser extent, from setup fees. Online Advice is a non-discretionary, Internet-based investment advisory service, which includes personalized online savings and investment advice, and retirement income projections for clients who want to manage their retirement themselves. The arrangements generally provide for our fees to be paid by the plan sponsor, plan provider or the DC plan itself, depending on the plan structure. Platform revenue is generally paid annually or quarterly in advance and recognized ratably over the term of the subscription period beginning after the completion of customer setup and data connectivity. Setup fees are recognized ratably over seven years.

Other Revenue

Other revenue includes reimbursement for a portion of marketing and client materials from certain subadvisory relationships. Non-retirement account servicing fees were applicable for the period of February 1, 2016 to December 31, 2016. The fees for non-retirement account servicing do not impact client fees paid for discretionary portfolio management services, and are disclosed in the applicable Form ADV of our advisory subsidiaries. Franchise royalty fees were applicable for the period of February 1, 2016 to September 30, 2016, as we had acquired all remaining franchises as of October 2016. Professional management revenue earned subsequent to the respective acquisition date of the franchises is included in professional management revenue. The franchise royalty fees were recognized as revenue as the services were performed by the franchisees and were based on specified percentages of the franchisees' advisory fees billed to their clients, which were primarily based on predetermined percentages of the market value of the AUM and were affected by changes in the AUM. Costs associated with reimbursed printed fulfillment materials are expensed to cost of revenue as incurred.

Costs and Expenses

Employee compensation and related expenses represent our largest expense. These expenses include employee-related expenses including wages, benefits expenses and employer payroll tax, cash incentive compensation expense, variable cash compensation expense related to ongoing asset servicing activities by advisor center advisors, commission expense, and non-cash stock-based compensation expense. Our cash incentive compensation plan is based, in part, on achieving pre-determined annual corporate financial objectives and may result in an increased current period expense while the anticipated revenue benefits associated with the achievement of such corporate financial objectives may be realized in future periods. We allocate compensation, including wages, cash incentive compensation expense and non-cash stock-based compensation, and other expenses from overhead departments such as human resources, facilities and information technology to our cost of revenue, research and development, sales and marketing, general and administrative functional areas, as well as to internal use software, which is included in amortization of intangible assets.

We expect our headcount to increase over time, and to be a primary area of growth in our costs and expenses. We anticipate granting equity awards to board members and certain of our employees each year that may result in significant non-cash stock-based compensation expense. We anticipate the largest grant events to typically occur in the first quarter of each year, although significant awards may also be granted at other times. In 2016, we began to issue restricted stock units as the primary stock award for non-executive employees, rather than stock options. We anticipate providing annual compensation increases to certain of our employees each year, typically in the first quarter, that would result in an increase primarily to wages and cash incentive compensation expenses.

Other costs and expenses include the costs of fees paid to plan providers related to the exchange of plan and prospective client data, as well as implementing our transaction instructions for client accounts, printed marketing and client materials and postage, facilities-related expenses, advertising including radio and digital, consulting and professional service expenses, amortization and depreciation for hardware and software purchases and support, and amortization of intangible assets.

The following summarizes our cost of revenue and certain significant operating expenses:

Cost of Revenue. Cost of revenue includes fees paid to plan providers for connectivity to plan and plan prospective client data, printed materials fulfillment costs for certain subadvisory relationships for which a portion are reimbursed, and printed client materials. Also included in cost of revenue are employee-related costs for in-person dedicated advisor centers, including variable cash compensation expense related to ongoing asset servicing activities, as well as employee-related costs for call center advisors, operations, implementations, technical operations, portfolio management and client service administration. Costs in this area are related primarily to payments to third parties, employee compensation and related expenses, facilities-related expenses, purchased materials and depreciation. Costs for connectivity to plan and prospective client data are expected to increase proportionally with our professional management revenue related to DC AUM. The expenses included in cost of revenue are shared across the different revenue categories, and we are not able to meaningfully allocate such costs between separate categories of revenue. Consequently, all costs and expenses applicable to our revenue are included in the category cost of revenue in our Unaudited Condensed Consolidated Statements of Income.

Research and Development. Research and development expense includes costs associated with defining and specifying new features and ongoing enhancement to our advice engines and other aspects of our service offerings, investment methodology, financial research, quality assurance, related administration and other costs that do not qualify for capitalization. Costs in this area are related primarily to employee compensation for our engineering, product development and investment research personnel and associated expenses, and to a lesser extent, external consulting expenses related to development, support and maintenance of our existing services.

Sales and Marketing. Sales and marketing expense includes costs associated with product and consumer marketing, provider and sponsor relationship management, provider and sponsor marketing, direct sales, corporate communications, public relations, creative services, sales related call center activities, advertising and live seminars, and printing of, and postage for, marketing materials for direct advisory relationships, including amortization of direct response advertising. Costs in this area are related primarily to employee compensation for sales and marketing personnel and related expenses, and also include commissions, printed materials and general marketing programs, including radio and digital advertising. Amounts received for support of marketing and client acquisition efforts are credited ratably to marketing expense. The fees for such support do not impact client fees paid for discretionary portfolio management services, and are disclosed in the applicable Form ADV of the company advisory subsidiaries.

General and Administrative. General and administrative expense includes costs for finance, accounting, legal, compliance, risk management and administration, as well as acquisition-related expenses, when applicable. Costs in this area include employee compensation and related expenses, and fees for consulting and professional services. We have incurred and we expect that we will continue to incur expenses as a result of being a public company for, among other things, SEC reporting and compliance, including compliance with the Sarbanes-Oxley Act of 2002, director compensation, insurance, and other similar expenses.

Amortization of Intangible Assets. Amortization of intangible assets includes the amortization of acquisition-related assets such as customer relationships, trademarks and trade names over the estimated useful lives using a straight-line method of amortization. It also includes the amortization of internal use software, which includes engineering costs associated with enhancing our advisory service platform and developing internal systems for tracking client data, including AUM, client cancellations and other related client and customer experience statistics. Associated direct development costs are capitalized and amortized using the straight-line method over the estimated lives, typically two to three years, of the underlying technology. Costs associated with internal use software include employee compensation and related expenses, and fees for external consulting services.

Acquisition Activity

On February 1, 2016, Financial Engines completed the acquisition of The Mutual Fund Store for an aggregate purchase price of $513 million, consisting of approximately $246 million in cash and 9,885,889 shares of our common stock. As a result of this acquisition, our revenue and expenses increased effective February 1, 2016 upon consolidation of the operations of both entities.

In April 2016, we completed the acquisition of seven franchises for total aggregate cash consideration of $14.4 million. In July and August 2016, we completed the acquisition of six franchises for a total aggregate cash consideration of $8.1 million. In October 2016, we completed the acquisition of the eight remaining franchises for total aggregate cash consideration of $12.8 million.

In connection with these acquisitions, we incurred approximately $2.3 million and $10.5 million of acquisition-related expenses that were charged to expense for the three and six months ended June 30, 2016, respectively, and approximately $0.7 million and $3.9 million of acquisition-related expenses that were charged to expense for the three and six months ended June 30, 2017, respectively.

Results of Operations

The following tables set forth our results of operations. The period to period comparison of financial results is not necessarily indicative of future results.

Comparison of Three Months Ended June 30, 2016 and 2017

	Three Months Ended June 30,		Three Months Ended June 30,		Increase (Decrease)	
	2016	2017	2016	2017	Amount	%
	(As a percentage of revenue)		(In thousands, except percentages)			
Revenue:						
Professional management	90 %	93 %	$96,071	$110,640	$14,569	15 %
Platform	7	6	7,173	6,784	(389)	(5)
Other	3	1	2,989	1,050	(1,939)	(65)
Total revenue	100	100	106,233	118,474	12,241	12
Costs and expenses:						
Cost of revenue	44	45	46,540	53,286	6,746	14
Research and development	9	9	8,967	11,119	2,152	24
Sales and marketing	20	18	21,686	21,189	(497)	(2)
General and administrative	9	7	9,809	8,566	(1,243)	(13)
Amortization of intangible assets, including internal use software	4	4	4,099	4,231	132	3
Total costs and expenses	86	83	91,101	98,391	7,290	8
Income from operations	14	17	15,132	20,083	4,951	33
Interest (expense) income	—	—	(20)	196	216	n/a
Other expense, net	—	—	(427)	(44)	383	(90)
Income before income taxes	14	17	14,685	20,235	5,550	38
Income tax expense	5	6	5,642	7,432	1,790	32
Net and comprehensive income	9 %	11 %	$9,043	$12,803	$3,760	42 %

Revenue

Total revenue increased $12.2 million, or 12%, from $106.2 million for the three months ended June 30, 2016 to $118.5 million for the three months ended June 30, 2017. This increase was due primarily to growth in professional management revenue of $14.6 million for the three months ended June 30, 2017, partially offset by a decrease of $1.9

million and $0.4 million, respectively, in other and platform revenue. Professional management revenue and platform revenue comprised 90% and 7%, respectively, of total revenue for the three months ended June 30, 2016, and 93% and 6%, respectively, of total revenue for the three months ended June 30, 2017.

Professional Management Revenue

Professional management revenue increased $14.6 million, or 15%, from $96.1 million for the three months ended June 30, 2016 to $110.6 million for the three months ended June 30, 2017. This increase in professional management revenue was due primarily to an increase in the average AUM used to calculate fees from approximately $125.0 billion for the three months ended June 30, 2016 to approximately $148.5 billion for the three months ended June 30, 2017, which was driven primarily by new assets from new and existing clients and market performance, partially offset by cancellations and withdrawals. The increase in professional management revenue was also driven by franchise acquisitions in 2016, as we now receive all of the advisory fees rather than a royalty percentage. In addition, there was a slight decrease in average fees due to factors that have varying impact and applicability from period to period, including fee reductions based upon individual account balances or achieving plan enrollment thresholds, contract modifications, the timing of promotional and communication techniques, and the net effect of sponsor conversions between advisory and subadvisory status.

Platform Revenue

Platform revenue decreased $0.4 million, or 5%, from $7.2 million for the three months ended June 30, 2016 to $6.8 million for the three months ended June 30, 2017. This decrease was due primarily to a small number of sponsor terminations, as well as platform fee reductions resulting from a small number of sponsors converting to a subadvisory plan provider or adding new services. These decreases were partially offset by an increase in platform fees due to service availability at new sponsors.

Other Revenue

Other revenue decreased $1.9 million, or 65%, from $3.0 million for the three months ended June 30, 2016 to $1.1 million for the three months ended June 30, 2017. This decrease was due primarily to a contract change which eliminated account servicing fees as of January 1, 2017, as well as the elimination of franchise royalty revenue after we acquired all franchises as of October 2016. The franchise acquisitions also resulted in increased professional management revenue as we now receive all of the advisory fees rather than a royalty percentage.

Costs and Expenses

Costs and expenses increased $7.3 million, or 8%, from $91.1 million for the three months ended June 30, 2016 to $98.4 million for the three months ended June 30, 2017. Cost of revenue increased $6.7 million, research and development expense increased $2.2 million, sales and marketing expense decreased $0.5 million, general and administrative expense decreased $1.2 million, and amortization of intangible assets increased $0.1 million for the three months ended June 30, 2017 compared to the three months ended June 30, 2016.

Across all functional areas, employee-related expenses such as wages and cash incentive compensation expense increased due primarily to headcount growth and annual compensation increases. Non-cash stock-based compensation also increased due primarily to awards granted within the last year, partially offset by forfeitures.

We granted equity awards with an aggregate estimated expense value of approximately $28.3 million to certain of our existing executive and non-executive employees in the first quarter of 2017. We will account for these equity awards over a four-year vesting period utilizing the graded-vesting attribution method and this expense may be reduced by forfeitures as they occur.

The non-cash stock-based compensation expense associated with these awards will be in addition to the amortization of both previously and subsequently granted stock awards, including other awards granted in 2017, and expected to be granted in 2017, all of which will utilize the graded-vesting attribution method. We adopted the entity-wide accounting policy election to account for forfeitures when they occur per ASU 2016-09 effective January 1, 2017, which may cause the timing of our non-cash stock-based compensation expense to be more volatile.

Effective January 1, 2017, we no longer account for paid time off for exempt employees due to a change in our benefits program.

Cost of Revenue

Cost of revenue increased $6.7 million, or 14%, from $46.5 million for the three months ended June 30, 2016 to $53.3 million for the three months ended June 30, 2017. There was a $3.0 million increase in employee-related expenses, including wages, a $0.9 million increase in cash incentive compensation expense and a $0.6 million increase non-cash stock-based compensation for the three months ended June 30, 2017 compared to the three months ended June 30, 2016, due primarily to growth in headcount. Variable cash compensation expense related to ongoing asset servicing activities by advisor center advisors resulted in an increase of $0.5 million. In addition, there was a $2.4 million increase in data connectivity fees due primarily to an increase in professional management revenue. These increases were partially offset by $0.3 million decrease in facilities–related overhead expenses, including rent and depreciation, as well as a decrease in other expenses, including subadvisory participant marketing materials and equipment, of $0.4 million. As a percentage of revenue, cost of revenue increased from 44% for the three months ended June 30, 2016 to 45% for the three months ended June 30, 2017. The increase as a percentage of revenue was due primarily to employee-related expenses, including wages, increasing at a faster rate than revenue.

We expect cost of revenue as a percent of revenue to be in the range of 44%-46% for the year ended December 31, 2017.

Research and Development

Research and development expense increased $2.2 million, or 24%, from $9.0 million for the three months ended June 30, 2016 to $11.1 million for the three months ended June 30, 2017. There was a $0.8 million increase in employee-related expense, including wages, and a $0.4 million increase in cash incentive compensation due primarily to annual compensation increases and growth in headcount, as well as a $0.7 million increase in non-cash stock-based compensation expense for the three months ended June 30, 2017 compared to the three months ended June 30, 2016. There was a net increase to other expenses totaling $0.3 million. As a percentage of revenue, research and development expense remained constant at 9% for the three months ended June 30, 2016 and 2017.

Sales and Marketing

Sales and marketing expense decreased $0.5 million, or 2%, from $21.7 million for the three months ended June 30, 2016 to $21.2 million for the three months ended June 30, 2017. There was a $0.8 million decrease in marketing programs expense, due primarily to an increase in the amounts received for support of marketing and client acquisition efforts, partially offset by an increase in marketing programs expense, including radio and digital advertising. In addition, there was a $0.5 million decrease in consulting expense due to a brand integration project incurred for the three months ended June 30, 2016, as well as an acquisition-related consulting contract which terminated in the three months ended March 31, 2017. There was also a $0.3 million decrease in non-cash stock-based compensation expense due to forfeitures related to employee terminations and a $0.1 million decrease in other expenses. These decreases were partially offset by a $0.5 million increase in employee-related expenses, including wages, and a $0.7 million increase in cash incentive compensation expense due primarily to the growth in headcount and annual compensation. As a percentage of revenue, sales and marketing expense decreased from 20% for the three months ended June 30, 2016 to 18% for the three months ended June 30, 2017. The decrease as a percentage of revenue was due primarily to an increase in the amounts received for support of marketing and client acquisition efforts, a decrease in consulting expenses and a decrease in non-cash stock-based compensation.

General and Administrative

General and administrative expense decreased $1.2 million, or 13%, from $9.8 million for the three months ended June 30, 2016 to $8.6 million for the three months ended June 30, 2017. There was a $0.8 million decrease in consulting and professional services fees due to acquisition-related consulting expenses incurred in the three months ended June 30, 2016. There was a $0.3 million decrease in non-cash stock-based compensation expense due to employee terminations and a $0.6 million decrease in other expenses including travel, operations and employee-related expenses, including wages. These decreases were partially offset by a $0.5 million increase in allocated facilities–related overhead expenses, including rent and depreciation. As a percentage of revenue, general and administrative expense decreased from 9% for the three months ended June 30, 2016 to 7% for the three months ended June 30, 2017. The decrease as a percentage of revenue was due primarily to the decrease in consulting and professional services expenses, as well as a decrease in non-cash stock-based compensation.

Amortization of Intangible Assets

Amortization of intangible assets increased $0.1 million, or 3%, from $4.2 million for the three months ended June 30, 2016 to $4.1 million for the three months ended June 30, 2017.

Income Taxes

Income tax expense increased from $5.6 million for the three months ended June 30, 2016 to $7.4 million for the three months ended June 30, 2017. Our effective tax rate decreased from 38% for the three months ended June 30, 2016 to 37% for the three months ended June 30, 2017 due primarily to adopting ASU 2016-09, effective January 1, 2017, which requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled.

Effective January 1, 2017, we adopted ASU 2016-09, which requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. This may also cause our effective tax rate to be more volatile in future periods. We would expect to see an effective tax rate of approximately 38-40%, excluding the effect of research and development credits, any changes in valuation allowances, and discrete items in future periods.

As of June 30, 2017, we continue to believe that sufficient positive evidence exists from historical operations and future projections to conclude that we are more likely than not to fully realize our federal deferred tax assets and our State of California deferred tax assets in future periods. We continuously evaluate additional facts representing positive and negative evidence in the determination of the realizability of the deferred tax assets.

Comparison of Six Months Ended June 30, 2016 and 2017

	Six Months Ended June 30,		Six Months Ended June 30,		Increase (Decrease)	
	2016	2017	2016	2017	Amount	%
	(As a percentage of revenue)		(In thousands, except percentages)			
Revenue:						
Professional management	90 %	93 %	$178,877	$217,400	$38,523	22 %
Platform	7	6	14,271	13,678	(593)	(4)
Other	3	1	5,143	1,491	(3,652)	(71)
Total revenue	100	100	198,291	232,569	34,278	17
Costs and expenses:						
Cost of revenue	43	45	85,871	104,811	18,940	22
Research and development	9	9	18,234	21,687	3,453	19
Sales and marketing	20	17	40,149	40,504	355	1
General and administrative	13	9	24,409	20,760	(3,649)	(15)
Amortization of intangible assets, including internal use software	4	4	7,125	8,394	1,269	18
Total costs and expenses	89	84	175,788	196,156	20,368	12
Income from operations	11	16	22,503	36,413	13,910	62

Interest (expense) income	—	—	(16)	263	279	n/a
Other expense, net	—	—	(460)	(172)	288	(63)
Income before income taxes	11	16	22,027	36,504	14,477	66
Income tax expense	5	5	9,655	11,527	1,872	19
Net and comprehensive income	6 %	11 %	$12,372	$24,977	$12,605	102 %

Revenue

Total revenue increased $34.3 million, or 17%, from $198.3 million for the six months ended June 30, 2016 to $232.6 million for the six months ended June 30, 2017, which included one additional month of revenue from 2016 acquisitions compared to the six months ended June 30, 2016. This increase was due primarily to growth in professional management revenue of $38.5 million for the six months ended June 30, 2017, partially offset by a decrease of $3.7 million and $0.6 million, respectively, in other and platform revenue. Professional management revenue and platform revenue comprised and 90% and 7%, respectively, of total revenue for the six months ended June 30, 2016 and 93% and 6%, respectively, of total revenue for the six months ended June 30, 2017.

Professional Management Revenue

Professional management revenue increased $38.5 million, or 22%, from $178.9 million for the six months ended June 30, 2016 to $217.4 million for the six months ended June 30, 2017, which includes one additional month of professional management revenue from 2016 acquisitions. This increase was due primarily to an increase in the average AUM used to calculate fees from approximately $119.9 billion for the six months ended June 30, 2016 to approximately $145.3 billion for the six months ended June 30, 2017, driven primarily by new assets from new and existing clients and market performance, partially offset by cancellations and withdrawals. The increase in professional management revenue was also driven by franchise acquisitions in 2016, as we now receive all of the advisory fees rather than a royalty percentage. In addition, there was a slight decrease in average fees due to factors that have varying impact and applicability from period to period, including fee reductions based upon individual account balances or achieving plan enrollment thresholds, contract modifications, the timing of promotional and communication techniques, and the net effect of sponsor conversions between advisory and subadvisory status.

Platform Revenue

Platform revenue decreased $0.6 million, or 4%, from $14.3 million for the six months ended June 30, 2016 to $13.7 million for the six months ended June 30, 2017. This decrease was due primarily to a small number of sponsor terminations, as well as platform fee reductions resulting from a small number of sponsors converting to a subadvisory plan provider or adding new services. These decreases were partially offset by an increase in platform fees due to service availability at new sponsors.

Other Revenue

Other revenue decreased $3.7 million, or 71%, from $5.1 million for the six months ended June 30, 2016 to $1.5 million for the six months ended June 30, 2017. This decrease was due primarily to a contract change which eliminated account servicing fees as of January 1, 2017, as well as the elimination of franchise royalty revenue after we acquired all franchises as of October 2016. The franchise acquisitions also resulted in increased professional management revenue as we now receive all of the advisory fees rather than a royalty percentage.

Costs and Expenses

Costs and expenses increased $20.4 million, or 12%, from $175.8 million for the six months ended June 30, 2016 to $196.2 million for the six months ended June 30, 2017, which included one additional month of operating expenses related to 2016 acquisitions. Cost of revenue increased $18.9 million, research and development expense increased $3.5 million, sales and marketing expense increased $0.4 million, general and administrative expense decreased $3.6 million, and amortization of intangible assets increased $1.3 million for the six months ended June 30, 2017 compared to the six months ended June 30, 2016.

Across all functional areas, employee-related expenses such as wages and cash incentive compensation expense increased due primarily to headcount growth and annual compensation increases. Non-cash stock-based compensation also increased due primarily to awards granted within the last year, partially offset by forfeitures.

Cost of Revenue

Cost of revenue increased $18.9 million, or 22%, from $85.9 million for the six months ended June 30, 2016 to $104.8 million for the six months ended June 30, 2017. There was a $7.7 million increase in employee-related expenses, including wages, a $1.6 million increase in cash incentive compensation expense and a $1.4 million increase non-cash stock-based compensation for the six months ended June 30, 2017 compared to the six months ended June 30, 2016, due primarily to growth in headcount. Variable cash compensation expense related to ongoing asset servicing activities by advisor center advisors resulted in an increase of $2.1 million. Facilities–related overhead expenses, including rent and depreciation, increased by $1.2 million, due primarily to increased facilities expenses, as well as increased allocation based on headcount. In addition, there was a $5.6 million increase in data connectivity fees due primarily to an increase in professional management revenue. There was a net increase in other expense $0.2 million. These increases were partially offset by a $0.9 million decrease in printed client and subadvisory marketing materials costs as we move more towards electronic delivery. As a percentage of revenue, cost of revenue increased from 43% for the six months ended June 30, 2016 to 45% for the six months ended June 30, 2017. The increase as a percentage of revenue was due primarily to employee-related expenses, including wages, increasing at a faster rate than revenue.

Research and Development

Research and development expense increased $3.5 million, or 19%, from $18.2 million for the six months ended June 30, 2016 to $21.7 million for the six months ended June 30, 2017. There was a $1.5 million increase in employee-related expense, including wages, and a $0.6 million increase in cash incentive compensation due primarily to annual compensation increases and headcount growth, as well as a $1.2 million increase in non-cash stock-based compensation expense for the six months ended June 30, 2017 compared to the six months ended June 30, 2016. There were other net expense increases, including facilities–related overhead expenses, consulting and equipment related expenses, totaling $0.7 million. These increases were partially offset by a $0.5 million increase in the amount of internal use software capitalized, due primarily to increased labor rates and the number of hours dedicated to internal use software projects. As a percentage of revenue, research and development expense remained constant at 9% for the six months ended June 30, 2016 and 2017.

Sales and Marketing

Sales and marketing expense increased $0.4 million, or 1%, from $40.1 million for the six months ended June 30, 2016 to $40.5 million for the six months ended June 30, 2017. There was a $1.3 million increase in employee-related expenses, including wages, and a $1.3 million increase in cash incentive compensation expense due primarily to the headcount growth and annual compensation increases. There was a $2.3 million increase in marketing programs expense, including radio and digital advertising, due primarily to one additional month of advertising expense given acquisition timing, offset by an increase in the amounts received for support of marketing and client acquisition efforts. Non-capitalized equipment related expenses increased $0.4 million and travel expenses increased by $0.3 million. These increases were partially offset by a $0.9 million decrease in non-cash stock-based compensation expense due to forfeitures related to employee terminations during the six months ended June 30, 2017. There was also a $0.9 million decrease in consulting expenses due to a brand integration project incurred for the six months ended June 30, 2016, as well as an acquisition-related consulting contract which terminated in the three months ended March 31, 2017, which caused expenses to be higher during the three months ended June 30, 2016. In addition, there was a $0.7 million decrease in printed marketing materials expense due to decreases in the amortization of direct response advertising, as well as a decrease in campaign volume due to sponsor campaign timing during the six months ended June 30, 2017. Other expenses, including commissions and facilities-related expenses, decreased by a net of $0.4 million. As a percentage of revenue, sales and marketing expense decreased from 20% for the six months ended June 30, 2016 to 17% for the six months ended June 30, 2017. The decrease as a percentage of revenue was due primarily to a decrease in non-cash stock-based compensation, printed marketing materials expenses, as well as employee-related expenses, including wages, growing at a slower rate than revenue.

General and Administrative

General and administrative expense decreased $3.6 million, or 15%, from $24.4 million for the six months ended June 30, 2016 to $20.8 million for the six months ended June 30, 2017. There was a $5.6 million decrease in consulting fees due primarily to acquisition-related expenses incurred in the six months ended June 30, 2016, as well as a $0.3 million decrease in travel expenses and a $0.3 million decrease in other expenses, including equipment and operations. These decreases were partially offset by a $0.3 million increase in employee-related expenses, including wages, due primarily to annual compensation increases, as well as a $1.2 million increase in non-cash stock-based compensation expense. In addition, there was a $0.6 million increase in allocated facilities–related overhead expenses, including rent and depreciation and a $0.5 million increase in professional services expenses. As a percentage of revenue, general and administrative expense decreased from 13% for the six months ended June 30, 2016 to 9% for the six months ended June 30, 2017. The decrease as a percentage of revenue was due primarily to the decrease in consulting expenses.

Amortization of Intangible Assets

Amortization of intangible assets increased $1.3 million, or 18%, from $7.1 million for the six months ended June 30, 2016 to $8.4 million for the six months ended June 30, 2017, due primarily to one additional month of amortization related to acquisitions closed in 2016 for the six months ended June 30, 2017, as well as the addition of amortization of customer relationships, trademarks and trade names associated with franchise acquisition activity.

Income Taxes

Income tax expense increased from $9.7 million for the six months ended June 30, 2016 to $11.5 million for the six months ended June 30, 2017. Our effective tax rate decreased from 44% for the six months ended June 30, 2016 to 32% for the six months ended June 30, 2017. During the six months ended June 30, 2016, our effective tax rate increased as compared to the statutory rate due primarily to non-deductible expenditures incurred in connection with acquisition activity. During the six months ended June 30, 2017, our effective tax rate decreased as compared to the statutory rate due primarily to adoption of ASU 2016-09, effective January 1, 2017, which requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled.

Non-GAAP Adjusted EBITDA, Adjusted Net Income and Adjusted Earnings Per Share

Adjusted EBITDA represents net income before net interest expense (income), income tax expense (benefit), depreciation, amortization of intangible assets, including internal use software, amortization and impairment of direct response advertising, amortization of deferred sales commissions, non-cash stock-based compensation expense, expenses related to the closing and integration of acquisitions and losses incurred on acquisitions, if applicable for the period. Adjusted net income represents net income before non-cash stock-based compensation expense, amortization of intangible assets related to assets acquired, including customer relationships, trade names and trademarks, expenses related to the closing and integration of acquisitions, losses incurred on acquisitions and certain other items such as the income tax benefit from the release of valuation allowances, if applicable for the period, partially offset by the related tax impact of these items. Adjusted earnings per share is defined as adjusted net income divided by the weighted average of dilutive common share equivalents outstanding.

Our management uses adjusted EBITDA, adjusted net income and adjusted earnings per share as measures of operating performance, for planning purposes (including the preparation of annual budgets), to allocate resources to enhance the financial performance of our business, to evaluate the effectiveness of our business strategies and in communications with our Board of Directors concerning our financial performance. In addition, management currently uses non-GAAP measures in determining cash incentive compensation.

We present adjusted EBITDA, adjusted net income and adjusted earnings per share as supplemental performance measures because we believe that these measures provide our Board of Directors, management and investors with additional information and greater transparency with respect to our performance and decision-making. We feel these performance measures provide investors and others with a better understanding and ability to evaluate our operating results and future prospects and provides the same performance measurement information as utilized by management. Adjusted EBITDA reflects the elements of profitability that can be most directly impacted by employees and our management believes that tracking this metric motivates executives to focus on profitable growth. Management believes it is useful to exclude non-cash stock-based compensation expense from our non-GAAP metrics because this expense is based upon the historical value of each award at the time of grant, which may not be reflective of the current compensation value, and the ongoing expense is outside of the control of management in the current reporting period. Adjusted EBITDA also excludes non-cash items such as depreciation and various types of amortization, as well as income taxes, which are largely non-cash at this point in time. We exclude expenses related to the closing and integration of acquisitions for comparability purposes as these are short-term in nature. Management believes it is useful to exclude these items as they do not necessarily reflect how our business is performing during the period reported. Adjusted net income and adjusted earnings per share exclude non-cash stock-based compensation expense, expenses related to the closing and integration of acquisitions, as well as losses incurred on acquisitions, for comparability purposes as these are short-term in nature, and amortization of intangible assets related to acquired assets including customer relationships, trade names and trademarks for comparability purposes. Adjusted EBITDA, adjusted net income and adjusted earnings per share are not measurements of our financial performance under GAAP and should not be considered as an alternative to net income, operating income, earnings per share or any other performance measures derived in accordance with GAAP, or as an alternative to cash flows from operating activities as a measure of our profitability or liquidity.

We understand that, although adjusted EBITDA, adjusted net income and adjusted earnings per share are frequently used by securities analysts, lenders and others in their evaluation of companies, adjusted EBITDA, adjusted net income and adjusted earnings per share have limitations as an analytical tool, and you should not consider them in isolation, or as a substitute for an analysis of our results as reported under GAAP. In particular, you should consider:

- Adjusted EBITDA, adjusted net income and adjusted earnings per share do not reflect our cash expenditures, or future requirements for capital expenditures or contractual commitments;
- Adjusted EBITDA, adjusted net income and adjusted earnings per share do not reflect changes in, or cash requirements for, our working capital needs;
- Adjusted EBITDA, adjusted net income and adjusted earnings per share do not reflect the non-cash component of employee compensation;

- Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized generally required prior cash outlays and generally will have to be replaced in the future by payment of cash, and adjusted EBITDA does not reflect any cash requirements for such replacements; and
- Other companies in our industry may calculate adjusted EBITDA, adjusted net income and adjusted earnings per share differently than we do, limiting their usefulness as a comparative measure.

Given the limitations associated with using adjusted EBITDA, adjusted net income and adjusted earnings per share, these financial measures should be considered in conjunction with our financial statements presented in accordance with GAAP and the reconciliation of adjusted EBITDA and adjusted net income to the most directly comparable GAAP measure, net income, and adjusted earnings per share to the most directly comparable GAAP measure, diluted earnings per share. Further, management also reviews GAAP measures and evaluates individual measures that are not included in adjusted EBITDA, such as our level of capital expenditures and equity issuance, among other measures.

The table below sets forth a reconciliation of GAAP net income to non-GAAP adjusted EBITDA based on our historical results:

Non-GAAP adjusted EBITDA	Three Months Ended June 30, 2016	2017	Six Months Ended June 30, 2016	2017
	(In thousands, unaudited)			
GAAP net income	$9,043	$12,803	$12,372	$24,977
Interest expense (income)	20	(196)	16	(263)
Income tax expense	5,642	7,432	9,655	11,527
Depreciation and amortization	2,260	2,084	4,307	4,202
Amortization of intangible assets (excluding internal use software)	2,916	2,797	4,591	5,593
Amortization of internal use software	1,084	1,298	2,331	2,537
Amortization and impairment of direct response advertising	1,211	1,032	2,425	1,951
Amortization of deferred sales commissions	413	287	831	575
Stock-based compensation	8,523	9,159	14,727	17,602
Acquisition-related expenses[(1)]	2,334	719	10,474	3,910
Non-GAAP adjusted EBITDA	$33,446	$37,415	$61,729	$72,611

(1) We expect to incur a minimal amount of acquisition-related expenses through December 31, 2017.

The table below sets forth a reconciliation of net income to non-GAAP adjusted net income based on our historical results:

Non-GAAP adjusted net income	Three Months Ended June 30, 2016	2017	Six Months Ended June 30, 2016	2017

	(In thousands, unaudited)			
GAAP net income	$9,043	$12,803	$12,372	$24,977
Stock-based compensation	8,523	9,159	14,727	17,602
Amortization of intangible assets (excluding internal use software)	2,916	2,797	4,591	5,593
Acquisition-related expenses	2,334	719	10,474	3,910
Income tax expense from non-deductible transaction expenses[1]	—	—	1,162	—
Tax-effect of adjustments[2]	(5,262)	(4,842)	(11,381)	(10,354)
Non-GAAP adjusted net income	$17,554	$20,636	$31,945	$41,728

(1) This amount represents estimated additional income tax expense incurred in the period for non-deductible transaction expenses related to acquisition activity.

(2) An estimated statutory tax rate of 38.2% has been applied to eliminate the tax-effect for all periods presented.

The table below sets forth a reconciliation of diluted earnings per share to non-GAAP adjusted earnings per share based on our historical results:

Non-GAAP adjusted earnings per share	Three Months Ended June 30, 2016	2017	Six Months Ended June 30, 2016	2017
	(In thousands, except per share data, unaudited)			
GAAP diluted earnings per share	$0.14	$0.20	$0.20	$0.39
Stock-based compensation	0.13	0.14	0.24	0.27
Amortization of intangible assets (excluding internal use software)	0.05	0.04	0.08	0.09
Acquisition-related expenses	0.04	0.01	0.17	0.06
Income tax expense from non-deductible transaction expenses[1]	—	—	0.02	—
Tax-effect of adjustments[2]	(0.08)	(0.07)	(0.19)	(0.16)
Non-GAAP adjusted earnings per share	$0.28	$0.32	$0.52	$0.65
Shares of common stock outstanding	61,716	62,998	59,986	62,723
Dilutive stock options, RSUs and PSUs	1,054	1,828	993	1,943
Non-GAAP adjusted common shares outstanding	62,770	64,826	60,979	64,666

(1) This amount represents estimated additional income tax expense incurred in the period for non-deductible transaction expenses related to acquisition activity.
(2) An estimated statutory tax rate of 38.2% has been applied to eliminate the tax-effect for all periods presented.

For the non-GAAP metrics above, the variances in the comparable periods are consistent with the GAAP variances discussed in the comparison of the three and six months ended June 30, 2016 and 2017 as presented above in our “Management’s Discussion and Analysis of Financial Condition and Results of Operations”.

Liquidity and Capital Resources

Sources of Liquidity

As of June 30, 2017, we had total cash and cash equivalents of $169.9 million, compared to $134.2 million of cash and cash equivalents as of December 31, 2016. Since February 1, 2016, we have used approximately $274.6 million of cash related to acquisitions, net of cash received and including holdbacks reserved with respect to indemnification claims. Over the next twelve months, and in the longer term, we expect that our cash and liquidity needs will be met by existing resources, consisting of cash and cash equivalents, and cash generated from ongoing operations. We plan to use existing cash and cash generated in the ongoing operations of our business to fund our current operations, capital expenditures and possible future acquisitions.

Consolidated Cash Flow Data

	Six Months Ended June 30,	
	2016	2017
	(In thousands)	
Net cash provided by operating activities	$26,382	$37,496
Net cash used in investing activities	(222,210)	(6,292)
Net cash (used in) provided by financing activities	(8,150)	4,468
Net (decrease) increase in cash and cash equivalents	$(203,978)	$35,672
Cash and cash equivalents, end of period	$101,238	$169,918

Operating Activities

Net cash provided by operating activities for the six months ended June 30, 2017 of $37.5 million was the result of net income of $25.0 million and adjustments for non-cash expenses of $43.0 million, primarily related to non-cash stock-based compensation expense, deferred tax assets, amortization of intangible assets, depreciation, and amortization and impairment of direct response advertising. In addition, there was a decrease in cash related to changes in operating assets and liabilities of $30.5 million. This decrease in cash related to operating assets and liabilities was due primarily to a decrease in accrued compensation as a result of the 2016 cash incentive program payments, an increase in accounts receivable as revenue increased, a decrease in accounts payable primarily related to a decrease in provider payables, as well as an increase in prepaid expenses and other assets.

We incurred cash payments totaling $3.9 million during the six months ending June 30, 2017 associated with a change to our paid time off program for exempt employees effective January 1, 2017.

As a result of retrospectively presenting ASU 2016-09, the excess tax benefit associated with non-cash stock-based compensation for the six months ended June 30, 2016 is now presented within operating activities. Net cash provided by operating activities for the six months ended June 30, 2016 was the result of net income of $12.4 million and adjustments for non-cash expenses of $34.5 million, primarily related to non-cash stock-based compensation expense, amortization of intangible assets, deferred tax assets, depreciation, and amortization and impairment of direct response advertising. In addition, there was a decrease in cash related to changes in operating assets and liabilities of $20.5 million. This decrease in cash related to operating assets and liabilities was due primarily to a decrease in accrued compensation as a result of the 2015 cash incentive program payments, a decrease in accounts payable related mainly to payments of transaction expenses related to the acquisition activity and a decrease in provider payables, and an increase in accounts receivable, prepaid expense and other assets due primarily to acquisition activity, partially offset by an increase in deferred rent due primarily to the new Overland Park, Kansas facility.

Investing Activities

Net cash used in investing activities was $222.2 million for the six months ended June 30, 2016 compared to $6.3 million for the six months ended June 30, 2017. For the six months ended June 30, 2017, the purchase of property and equipment decreased $1.6 million, as we spent $4.0 million for the six months ended June 30, 2016 related to capital expenditures, which included capital equipment purchases related to the build out of the new Overland Park, Kansas facility, compared to $2.3 million during the six months ended June 30, 2017. For the six months ended June 30, 2017, the capitalization of internal use software increased $0.4 million from $3.6 million for the six months ended June 30, 2016 to $3.9 million for the six months ended June 30, 2017. Cash provided by the sale of all remaining short-term investments was $39.9 million for the six months ended June 30, 2016. All short-term investments were sold as of January 2016.

On February 1, 2016, we completed the acquisition of The Mutual Fund Store for approximately $241.0 million in cash consideration, net of $5.0 million cash acquired, and approximately $267 million in common stock consideration. In April 2016, we completed the acquisition of seven franchises for a total aggregate cash consideration of $14.4 million, including $0.8 million of holdbacks reserved with respect to indemnification claims.

We expect to incur cash expenditures of approximately $7.0 million associated with capital improvements to our advisor centers during the second half of 2017.

Financing Activities

Net cash used in financing activities was $8.2 million for the six months ended June 30, 2016 compared to net cash provided by financing activities of $4.5 million for the six months ended June 30, 2017. As a result of retrospectively adopting ASU 2016-09 to present the excess tax benefit associated with non-cash stock-based compensation as operating activities, net cash used by financing activities for the six months ended June 30, 2016 was adjusted with an increase of $5.4 million, from $2.8 million to $8.2 million. For the six months ended June 30, 2016, we received $1.1 million of proceeds from the issuance of common stock due to the exercise of stock options compared to $18.9 million during the six months ended June 30, 2017. During the six months ended June 30, 2017, we paid $2.1 million primarily for previously withheld consideration for acquisition of The Mutual Fund Store and the acquisition of franchises in 2016.

For the six months ended June 30, 2016, we incurred cash dividend payments totaling $8.6 million compared to cash dividend payments totaling $8.7 million for the six months ended June 30, 2017. In July 2017, we incurred a subsequent payment of $4.4 million relating to dividends payable as of June 30, 2017. Based on the shares outstanding as of June 30, 2017 of 63,123,174 and assuming a $0.07 per share quarterly dividend for 2017, we would estimate dividend payments to total approximately $8.8 million for the period July 1, 2017 through December 31, 2017. Any future determination with respect to the declaration and payment of dividends will be at the discretion of our Board of Directors.

We expect to incur cash payments in an amount necessary to satisfy the minimum tax withholding obligations for restricted stock units previously granted to employees, which will be determined based on the fair value of our common stock and applicable tax rates on the vesting dates. For the six months ended June 30, 2016, we incurred $0.7 million of cash payments related to minimum tax withholding obligations compared to $3.5 million for the six months ended June 30, 2017. Based on the fair value of our common stock as of June 30, 2017 of $36.60 and assuming a 40% tax rate, the estimated minimum tax withholding obligations would be approximately $3.2 million for the period July 1, 2017 to December 31, 2017, which may be reduced by forfeitures. We anticipate these cash payments to occur throughout each year with the largest amounts typically occurring in the first and fourth quarters, and with the payment amounts determined by the number of shares released, the fair value of our common stock and applicable tax rates at that point in time.

Off-Balance Sheet Arrangements

As of June 30, 2017, we did not have any off-balance sheet arrangements, as defined in Item 303(a)(4)(ii) of Regulation S-K promulgated by the SEC, that have or are reasonably likely to have a current or future effect on our financial condition, changes in our financial condition, revenues, or expenses, results of operations, liquidity, capital expenditures, or capital resources that is material to investors.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market Risk

Our exposure to market risk is directly related to our role as an investment manager for investor accounts for which we provide portfolio management services. For the six months ended June 30, 2017, 93% of our revenue was derived from fees based on the market value of AUM compared to 91% for the year ended December 31, 2016. In general, we expect the percentage of revenue that is derived from fees based on the market value of AUM to increase over time.

A substantial portion of the assets we manage is invested in equity securities, the market prices of which can vary substantially based on changes in economic conditions. An additional portion is invested in fixed income securities, which will generally have lower volatility than the equity market. Therefore, while any changes in equity market performance would significantly affect the value of our AUM, particularly for the AUM invested in equity securities, such changes would typically result in lower volatility for our AUM than the volatility of the equity market as a whole. Because a substantial portion of our revenue is derived from the value of our AUM, any changes in fixed income or equity market performance would significantly affect the amount of revenue in a given period. If any of these factors reduces our AUM, the amount of client fees we would earn for managing those assets would decline, which in turn could negatively impact our revenue.

For DC professional management revenue, fees are calculated at or near the end of each month. We expect this monthly methodology potentially reduces the impact of financial market volatility on this portion of our professional management revenue. For IRA and taxable professional management revenue, fees are calculated at the end of each quarter. We expect this quarterly methodology potentially results in greater impact of financial market volatility on this portion of our professional management revenue.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (or the Exchange Act)) as of the end of the period covered by this report. Based on their evaluation, our Chief Executive Officer (our principal executive officer) and our Chief Financial Officer (our principal financial officer) have concluded that our disclosure controls and procedures as of the end of the period covered by this report were designed and were functioning effectively at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

On February 1, 2016, we acquired The Mutual Fund Store, and subsequently acquired all franchises during the year ended December 31, 2016, as further described in Note 3 to the unaudited condensed consolidated financial statements. During the first quarter of 2017, we updated our internal control structure to reflect the integration of these acquired entities into our overall internal control over financial reporting processes, including the policies, processes, people, technology and operations for our combined operations. We will continue to evaluate the impact of any related changes that have materially affected or are likely to materially affect our internal control over financial reporting during the year ended December 31, 2017. Except for the impact of these acquired entities on our internal control processes, there was no change in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II — OTHER INFORMATION

Item 1A. Risk Factors

You should carefully review and consider the information regarding certain factors that could materially affect our business, financial condition or future results set forth under Part I—Item 1A (Risk Factors) in our Annual Report on Form 10-K for the fiscal year ended December 31, 2016. There have been no material changes from the risk factors disclosed in our 2016 Annual Report on Form 10-K.

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

Unregistered Sales of Equity Securities

For the three months ended June 30, 2017, we issued 45,950 shares of unregistered common stock for an aggregate purchase price of $0.3 million upon the exercise of previously granted options, which was paid in cash. These transactions were effected under Rule 701 of the Securities Act of 1933, applicable to our 1998 Stock Option Plan. All recipients either received adequate information about us or had access, through employment or other relationships, to such information. There were no underwriters employed in connection with these transactions.

Item 6. Exhibits

Exhibit Number	Description
2.1	Agreement and Plan of Mergers, dated as of November 5, 2015 by and among Financial Engines, Inc., Mayberry Acquisition Sub I, LLC, Mayberry Acquisition Sub, Inc., Mayberry Acquisition Sub II, LLC, Kansas City 727 Acquisition Corporation, TMFS Holdings, Inc., Kansas City 727 Acquisition LLC, and, solely in its capacity as representative of the Sellers, WP Fury Holdings, LLC (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed November 9, 2015, and incorporated herein by reference) and First Amendment thereto, dated as of February 1, 2016 (filed as Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed February 3, 2016, and incorporated herein by reference).*
3.(i)	Restated Certificate of Incorporation of the Registrant (filed as Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 2010, filed May 13, 2010, and incorporated herein by reference).
3.(ii)	Bylaws of the Registrant (filed as Exhibit 3.(ii)2 to the Registrant's Registration Statement on Form S-1, file no. 333-163581, filed December 9, 2009, and incorporated herein by reference).
4.1	Specimen Common Stock Certificate (filed as Exhibit 4.1 to the Registrant's Registration Statement on Form S-1, file no. 333-163581, filed February 22, 2010, and incorporated herein by reference).
31.1	Certificate of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).
31.2	Certificate of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).
32.1(1)	Certificate of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).
32.2(1)	Certificate of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. Section 1350).
101.INS	XBRL Instance Document
101.SCH	XBRL Schema Document
101.CAL	XBRL Calculation Linkbase Document
101.DEF	XBRL Definition Linkbase Document
101.LAB	XBRL Label Linkbase Document

101.PRE	XBRL Presentation Linkbase Document

(1) The material contained in Exhibit 32.1 and Exhibit 32.2 is not deemed “filed” with the SEC and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933 (the Securities Act) or the Exchange Act, whether made before or after the date hereof and irrespective of any general incorporation language contained in such filing, except to the extent that the registrant specifically incorporates it by reference.
(#) Indicates management contract or compensatory plan or arrangement.
(*) Financial Engines hereby undertakes to furnish supplementally a copy of any omitted schedule or exhibit to such agreement to the U.S. Securities and Exchange Commission upon request.

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.

Date: August 8, 2017

FINANCIAL ENGINES, INC.

/s/ Lawrence M. Raffone
Lawrence M. Raffone
President and Chief Executive Officer
(Duly authorized officer and principal executive officer)

/s/ Raymond J. Sims
Raymond J. Sims
Executive Vice President, Chief Financial Officer
(Duly authorized officer and principal financial officer)

/s/ Jeffrey C. Grace
Jeffrey C. Grace
VP, Controller and Principal Accounting Officer
(Duly authorized officer and principal accounting officer)

Exhibit Index

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(#) Indicates management contract or compensatory plan or arrangement.
(*) Financial Engines hereby undertakes to furnish supplementally a copy of any omitted schedule or exhibit to such agreement to the U.S. Securities and Exchange Commission upon request.