Artisan Partners Asset Management Inc.
Form 10-Q
August 01, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

(Mark One)	
þ	QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2018
OR	
o	TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM TO

Commission file number: 001-35826

Artisan Partners Asset Management Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	45-0969585 (I.R.S. Employer Identification No.)
875 E. Wisconsin Avenue, Suite 800 Milwaukee, WI (Address of principal executive offices)	53202 (Zip Code)

(414) 390-6100
(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 þ No o

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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act. (Check one):

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

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. o

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

The number of outstanding shares of the registrant’s Class A common stock, par value $0.01 per share, Class B common stock, par value $0.01 per share, and Class C common stock, par value $0.01 per share, as of July 27, 2018 were 53,978,323, 8,745,249 and 14,244,130, respectively.

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Except where the context requires otherwise, in this report, references to the “Company”, “Artisan”, “we”, “us” or “our” refer t Artisan Partners Asset Management Inc. (“APAM”) and its direct and indirect subsidiaries, including Artisan Partners Holdings LP (“Artisan Partners Holdings” or “Holdings”). On March 12, 2013, APAM closed its initial public offering and related corporate reorganization. Prior to that date, APAM was a subsidiary of Artisan Partners Holdings.

Forward-Looking Statements

This report contains, and from time to time our management may make, forward-looking statements within the meaning of the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Statements regarding future events and our future performance, as well as management's current expectations, beliefs, plans, estimates, or projections relating to the future, are forward-looking statements within the meaning of these laws. In some cases, you can identify these statements by forward-looking words such as “may”, “might”, “will”, “should”, “expects”, “intends”, “plans”, “anticipates”, “believes”, “estimates”, “predicts”, “potential” or “continue”, the negative of these terms and comparable terminology. These forward-looking statements are only predictions based on current expectations and projections about future events. Forward-looking statements are subject to a number of risks and uncertainties, and there are important factors that could cause actual results, level of activity, performance, actions or achievements to differ materially from the results, level of activity, performance, actions or achievements expressed or implied by the forward-looking statements. These factors include: the loss of key investment professionals or senior management, adverse market or economic conditions, poor performance of our investment strategies, change in the legislative and regulatory environment in which we operate, operational or technical errors or other damage to our reputation and other factors disclosed in the Company's filings with the Securities and Exchange Commission, including those factors listed under the caption entitled “Risk Factors” in Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2017, filed with the SEC on February 21, 2018, which is accessible on the SEC's website at www.sec.gov. We undertake no obligation to publicly update any forward-looking statements in order to reflect events or circumstances that may arise after the date of this report, except as required by law.

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Forward-looking statements include, but are not limited to, statements about:

- our anticipated future results of operations;
- our potential operating performance and efficiency;
- our expectations with respect to future levels of assets under management, including the capacity of our strategies and client cash inflows and outflows;
- our expectations with respect to industry trends and how those trends may impact our business;
- our financing plans, cash needs and liquidity position;
- our intention to pay dividends and our expectations about the amount of those dividends;
- our expected levels of compensation of our employees, including equity compensation;
- our expectations with respect to future expenses and the level of future expenses;
- our expected tax rate, and our expectations with respect to deferred tax assets; and
- our estimates of future amounts payable pursuant to our tax receivable agreements.

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Part I — Financial Information
Item 1. Unaudited Consolidated Financial Statements
ARTISAN PARTNERS ASSET MANAGEMENT INC.
Unaudited Condensed Consolidated Statements of Financial Condition
(U.S. dollars in thousands, except per share amount)

	June 30, 2018	December 31, 2017
ASSETS		
Cash and cash equivalents	$190,358	$ 137,286
Accounts receivable	76,819	76,693
Investment securities	5,603	4,978
Property and equipment, net	20,801	21,025
Deferred tax assets	439,114	429,212
Restricted cash	629	629
Prepaid expenses and other assets	14,616	13,364
Assets of consolidated investment products		
Cash and cash equivalents	46,625	21,881
Accounts receivable and other	19,735	16,768
Investment assets, at fair value	136,425	115,319
Total assets	$950,725	$ 837,155
LIABILITIES, REDEEMABLE NONCONTROLLING INTERESTS, AND STOCKHOLDERS' EQUITY		
Accounts payable, accrued expenses, and other	$23,869	$ 23,019
Accrued incentive compensation	75,978	2,911
Borrowings	199,213	199,129
Amounts payable under tax receivable agreements	377,504	385,413
Liabilities of consolidated investment products		
Accounts payable, accrued expenses, and other	13,119	8,180
Investment liabilities, at fair value	50,811	47,857
Total liabilities	740,494	666,509
Commitments and contingencies		
Redeemable noncontrolling interests	96,474	62,581
Common stock		
Class A common stock ($0.01 par value per share, 500,000,000 shares authorized, 53,978,658 and 50,463,126 shares outstanding at June 30, 2018 and December 31, 2017, respectively)	540	505
Class B common stock ($0.01 par value per share, 200,000,000 shares authorized, 8,745,249 and 11,922,192 shares outstanding at June 30, 2018 and December 31, 2017, respectively)	88	119
Class C common stock ($0.01 par value per share, 400,000,000 shares authorized, 14,244,130 and 13,184,527 shares outstanding at June 30, 2018 and December 31, 2017, respectively)	142	132
Additional paid-in capital	82,791	147,910
Retained earnings (deficit)	28,694	(37,870)
Accumulated other comprehensive income (loss)	(1,477)	(873)
Total Artisan Partners Asset Management Inc. stockholders' equity	110,778	109,923
Noncontrolling interest - Artisan Partners Holdings	2,979	(1,858)
Total stockholders' equity	113,757	108,065
Total liabilities, redeemable noncontrolling interests, and stockholders' equity	$950,725	$ 837,155

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

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ARTISAN PARTNERS ASSET MANAGEMENT INC.
Unaudited Consolidated Statements of Operations
(U.S. dollars in thousands, except per share amounts)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2018	2017	2018	2017
Revenues				
Management fees	$210,029	$195,951	$421,995	$380,025
Performance fees	2,267	322	2,309	322
Total revenues	$212,296	$196,273	$424,304	$380,347
Operating Expenses				
Compensation and benefits				
Salaries, incentive compensation and benefits	106,744	96,426	211,968	189,675
Pre-offering related compensation - share-based awards	—	6,339	—	12,678
Total compensation and benefits	106,744	102,765	211,968	202,353
Distribution, servicing and marketing	6,847	7,292	13,856	14,666
Occupancy	4,302	3,660	8,227	7,166
Communication and technology	8,966	8,601	17,626	17,024
General and administrative	6,560	7,452	13,764	14,603
Total operating expenses	133,419	129,770	265,441	255,812
Total operating income	78,877	66,503	158,863	124,535
Non-operating income (loss)				
Interest expense	(2,846)	(2,920)	(5,622)	(5,801)
Net investment gain (loss) of consolidated investment products	2,941	18	9,226	18
Net investment income	304	—	625	93
Other non-operating income (expense)	356	173	489	233
Total non-operating income (loss)	755	(2,729)	4,718	(5,457)
Income before income taxes	79,632	63,774	163,581	119,078
Provision for income taxes	11,987	14,941	24,272	27,690
Net income before noncontrolling interests	67,645	48,833	139,309	91,388
Less: Net income attributable to noncontrolling interests - Artisan Partners Holdings	23,307	22,197	49,359	44,957
Less: Net income attributable to noncontrolling interests - consolidated investment products	2,332	4	6,670	4
Net income attributable to Artisan Partners Asset Management Inc.	$42,006	$26,632	$83,280	$46,427
Basic and diluted earnings per share	$0.72	$0.45	$1.48	$0.86
Basic and diluted weighted average number of common shares outstanding	49,041,113	45,241,102	48,205,418	43,142,011
Dividends declared per Class A common share	$0.60	$0.60	$1.99	$1.56

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

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ARTISAN PARTNERS ASSET MANAGEMENT INC.
Unaudited Consolidated Statements of Comprehensive Income
(U.S. dollars in thousands)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2018	2017	2018	2017
Net income before noncontrolling interests	$67,645	$48,833	$139,309	$91,388
Other comprehensive income (loss), net of tax				
Unrealized gain (loss) on investment securities:				
Unrealized gain (loss) on investment securities, net of tax of $0, $39, $0, and $31, respectively	—	120	—	176
Less: reclassification adjustment for gain (loss) included in net income	—	—	—	93
Net unrealized gain (loss) on investment securities	—	120	—	83
Foreign currency translation gain (loss)	(1,042)	523	(410)	729
Total other comprehensive income (loss)	(1,042)	643	(410)	812
Comprehensive income	66,603	49,476	138,899	92,200
Comprehensive income attributable to noncontrolling interests - Artisan Partners Holdings	23,002	22,448	49,293	45,506
Comprehensive income attributable to noncontrolling interests - consolidated investment products	2,332	4	6,670	4
Comprehensive income attributable to Artisan Partners Asset Management Inc.	$41,269	$27,024	$82,936	$46,690

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

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ARTISAN PARTNERS ASSET MANAGEMENT INC.
Unaudited Consolidated Statements of Changes in Stockholders' Equity
(U.S. dollars in thousands)

	Class A Common stock	Class B Common stock	Class C Common stock	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Non-controlling interest - Artisan Partners Holdings	Total stockholders' equity	Redeemable non-controlling interest
Balance at January 1, 2018	$ 505	$ 119	$ 132	$ 147,910	$ (37,870)	$ (873)	$ (1,858)	$ 108,065	$ 62,581
Net income	—	—	—	—	83,280	—	49,359	132,639	6,670
Other comprehensive income - foreign currency translation	—	—	—	—	—	(302)	(108)	(410)	—
Other comprehensive income - available for sale investments, net of tax	—	—	—	—	358	(260)	—	98	—
Cumulative impact of changes in ownership of Artisan Partners Holdings LP, net of tax	—	—	—	(3,091)	—	(42)	3,133	—	—
Amortization of equity-based compensation	—	—	—	20,713	—	—	8,856	29,569	—
Deferred tax assets, net of amounts payable under tax receivable agreements	—	—	—	4,169	—	—	—	4,169	—
Issuance of Class A common stock, net of issuance costs	6	—	—	21,285	—	—	—	21,291	—
Forfeitures and employee/partner terminations	5	(20)	15	—	—	—	—	—	—
Issuance of restricted stock awards	15	—	—	(15)	—	—	—	—	—
Employee net share settlement	(1)	—	—	(1,210)	—	—	(594)	(1,805)	—
Exchange of subsidiary equity	10	(5)	(5)	—	—	—	—	—	—
Purchase of equity and subsidiary equity	—	(6)	—	(21,472)	—	—	—	(21,478)	—
Capital contributions, net	—	—	—	—	—	—	—	—	27,223
Distributions	—	—	—	—	—	—	(55,744)	(55,744)	—
Dividends	—	—	—	(85,498)	(17,074)	—	(65)	(102,637)	—
Balance at June 30, 2018	$ 540	$ 88	$ 142	$ 82,791	$ 28,694	$ (1,477)	$ 2,979	$ 113,757	$ 96,474

	Class A Common	Class B Common stock	Class C Common stock	Additional paid-in capital	Retained earnings	Accumulated other comprehensive	Non-controlling interest - Artisan	Total stockholders' equity	Redeemable non-controlling interest

	stock					income (loss)	Partners Holdings		
Balance at January 1, 2017	$ 421	$ 151	$ 171	$ 119,221	$ 13,395	$ (1,648)	$ (13,997)	$ 117,714	—
Net income	—	—	—	—	46,427	—	44,957	91,384	4
Other comprehensive income - foreign currency translation	—	—	—	—	—	467	262	729	—
Other comprehensive income - available for sale investments, net of tax	—	—	—	—	—	49	36	85	—
Cumulative impact of changes in ownership of Artisan Partners Holdings LP, net of tax	—		—	(4,966)	—	(253)	5,217	(2)	—
Amortization of equity-based compensation	—		—	23,385	—	—	14,255	37,640	—
Deferred tax assets, net of amounts payable under tax receivable agreements	—		—	21,371	—	—	—	21,371	—
Issuance of Class A common stock, net of issuance costs	56		—	161,991	—	—	—	162,047	—
Forfeitures and employee/partner terminations	—		—	—	—	—	—	—	—
Issuance of restricted stock awards	13		—	(13)	—	—	—	—	—
Employee net share settlement	—		—	(530)	—	—	(400)	(930)	—
Exchange of subsidiary equity	7	(6)	(1)	—	—	—	—	—	—
Purchase of equity and subsidiary equity	—	(21)	(35)	(162,438)	—	—	—	(162,494)	—
Capital Contributions, net	—	—	—	—	—	—	—	—	12,654
Distributions	—		—	—	—	—	(54,769)	(54,769)	—
Dividends	—		—	(29,251)	(41,286)	—	(63)	(70,600)	—
Balance at June 30, 2017	$ 497	$ 124	$ 135	$ 128,770	$ 18,536	$ (1,385)	$ (4,502)	$ 142,175	$ 12,658

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

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ARTISAN PARTNERS ASSET MANAGEMENT INC.
Unaudited Consolidated Statements of Cash Flows
(U.S. dollars in thousands)

	For the Six Months Ended June 30,	
	2018	2017
Cash flows from operating activities		
Net income before noncontrolling interests	$139,309	$91,388
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,502	2,549
Deferred income taxes	13,707	18,604
Net investment income	(625)	(93)
Loss on disposal of property and equipment	7	18
Amortization of debt issuance costs	229	224
Share-based compensation	29,569	37,640
Net investment (gain) loss of consolidated investment products	(9,226)	(18)
Purchase of investments by consolidated investment products	(572,217)	(23,194)
Proceeds from sale of investments by consolidated investment products	563,516	6,907
Change in assets and liabilities resulting in an increase (decrease) in cash:		
Accounts receivable	(126)	(8,019)
Prepaid expenses and other assets	(1,868)	(520)
Accounts payable and accrued expenses	74,117	59,234
Class B liability awards	—	(506)
Deferred lease obligations	318	1,512
Net change in operating assets and liabilities of consolidated investment products	1,747	10,774
Net cash provided by operating activities	240,959	196,500
Cash flows from investing activities		
Acquisition of property and equipment	(602)	(823)
Leasehold improvements	(2,161)	(1,468)
Proceeds from sale of investment securities	—	6,382
Purchase of investment securities	—	(3,250)
Net cash provided by (used in) investing activities	(2,763)	841
Cash flows from financing activities		
Partnership distributions	(55,744)	(54,769)
Dividends paid	(102,637)	(70,600)
Payment under the tax receivable agreements	(27,251)	(22,788)
Net proceeds from issuance of common stock	21,478	162,494
Payment of costs directly associated with the issuance of Class A common stock	(166)	(294)
Purchase of equity and subsidiary equity	(21,478)	(162,494)
Taxes paid related to employee net share settlement	(1,805)	(930)
Capital contributions to consolidated investment products, net	27,223	12,654
Net cash used in financing activities	(160,380)	(136,727)
Net increase (decrease) in cash and cash equivalents	77,816	60,614
Cash, cash equivalents and restricted cash		
Beginning of period	159,796	157,406
End of period	$237,612	$218,020
Cash, cash equivalents and restricted cash as of the end of the period		
Cash and cash equivalents	$190,358	$190,258

Restricted cash	629	629
Cash and cash equivalents of consolidated investment products	46,625	27,133
Cash, cash equivalents and restricted cash	$237,612	$218,020
Supplementary information		
Noncash activity:		
Establishment of deferred tax assets	$23,511	$127,771
Establishment of amounts payable under tax receivable agreements	19,342	106,399

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

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ARTISAN PARTNERS ASSET MANAGEMENT INC.
Notes to Unaudited Consolidated Financial Statements
(U.S. currencies in thousands, except per share or per unit amounts and as otherwise indicated)
Note 1. Nature of Business and Organization
Nature of Business
Artisan Partners Asset Management Inc. (“APAM”), through its subsidiaries, is an investment management firm focused on providing high-value added, active investment strategies to sophisticated clients globally. APAM and its subsidiaries are hereafter referred to collectively as “Artisan” or the “Company”.
Artisan’s autonomous investment teams manage a broad range of U.S., non-U.S. and global investment strategies that are diversified by asset class, market cap and investment style. Strategies are offered through multiple investment vehicles to accommodate a broad range of client mandates. Artisan offers its investment management services primarily to institutions and through intermediaries that operate with institutional-like decision-making processes and have long-term investment horizons.
Organization
On March 12, 2013, APAM completed its initial public offering (the “IPO”). APAM was formed for the purpose of becoming the general partner of Artisan Partners Holdings LP (“Artisan Partners Holdings” or “Holdings”) in connection with the IPO. Holdings is a holding company for the investment management business conducted under the name “Artisan Partners”. The reorganization (“IPO Reorganization”) established the necessary corporate structure to complete the IPO while at the same time preserving the ability of the firm to conduct operations through Holdings and its subsidiaries.
As the sole general partner, APAM controls the business and affairs of Holdings. As a result, APAM consolidates Holdings’ financial statements and records a noncontrolling interest for the equity interests in Holdings held by the limited partners of Holdings. At June 30, 2018, APAM held approximately 70% of the equity ownership interest in Holdings.
Holdings, together with its wholly owned subsidiary, Artisan Investments GP LLC (“AIGP”), controls a 100% interest in Artisan Partners Limited Partnership (“APLP”), a multi-product investment management firm that is the principal operating subsidiary of Artisan Partners Holdings. APLP is registered as an investment adviser with the U.S. Securities and Exchange Commission under the Investment Advisers Act of 1940. APLP provides investment advisory services to separate accounts and pooled investment vehicles, including Artisan Partners Funds, Inc. (“Artisan Funds”) and Artisan Partners Global Funds plc (“Artisan Global Funds”). Artisan Funds are a series of open-end, diversified mutual funds registered under the Investment Company Act of 1940, as amended. Artisan Global Funds is a family of Ireland-domiciled UCITS.
2018 Follow-On Offering
On February 27, 2018, APAM completed a registered offering of 644,424 shares of Class A common stock (the “2018 Follow-On Offering”) and utilized all of the proceeds to purchase an aggregate of 644,424 common units of Artisan Partners Holdings at a price per unit of $33.33. The offering and subsequent purchase of units had the following impact on the consolidated financial statements:

- APAM received 644,424 GP units of Holdings, which increased APAM’s ownership interest in Holdings. See Note 7, “Noncontrolling interest - Holdings” for the financial statement impact of changes in ownership.
- APAM’s purchase of common units of Holdings with the proceeds resulted in an increase to deferred tax assets and amounts payable under the tax receivable agreements. See Note 11, “Income Taxes and Related Payments”.

Holdings Unit Exchanges
Limited partners of Artisan Partners Holdings are entitled to exchange partnership units (along with a corresponding number of shares of Class B or C common stock of APAM) for shares of Class A common stock from time to time (the “Holdings Common Unit Exchanges”). The following partnership units were exchanged for APAM Class A common stock during the six months ended June 30, 2018:

	Total Common Units	Class A Common Units	Class B Common Units	Class E Common Units

	Exchanged			
Common units exchanged on March 1, 2018	958,288	499,222	449,066	10,000
Common units exchanged on April 2, 2018	452,628	—	—	452,628
Common units exchanged on May 9, 2018	62,000	—	57,000	5,000
Total Units Exchanged	1,472,916	499,222	506,066	467,628

The corresponding shares of APAM Class B and Class C common stock were immediately canceled upon exchange. The Holdings Common Unit Exchanges increased APAM's equity ownership interest in Holdings and resulted in an increase to deferred tax assets and amounts payable under the tax receivable agreements. See Note 11, "Income Taxes and Related Payments".

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Note 2. Summary of Significant Accounting Policies

Basis of presentation

The accompanying financial statements are unaudited. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of such consolidated financial statements have been included. Such interim results are not necessarily indicative of full year results.

The consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") for interim financial reporting and accordingly they do not include all of the information and footnotes required in the annual consolidated financial statements and accompanying footnotes.

The year-end condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP. As a result, the interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in APAM's latest annual report on Form 10-K.

The accompanying financial statements were prepared in accordance with U.S. GAAP and related rules and regulations of the SEC. The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates or assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from these estimates or assumptions.

Principles of consolidation

Artisan's policy is to consolidate all subsidiaries or other entities in which it has a controlling financial interest. The consolidation guidance requires an analysis to determine if an entity should be evaluated for consolidation using the voting interest entity ("VOE") model or the variable interest entity ("VIE") model. Under the VOE model, controlling financial interest is generally defined as a majority ownership of voting interests. Under the VIE model, controlling financial interest is defined as (i) the power to direct activities that most significantly impact the economic performance of the entity and (ii) the right to receive potentially significant benefits or the obligation to absorb potentially significant losses. Artisan generally consolidates VIEs in which it meets the power criteria and holds an equity ownership interest of greater than 10%. The consolidated financial statements include the accounts of APAM and all subsidiaries or other entities in which APAM has a direct or indirect controlling financial interest. All material intercompany balances have been eliminated in consolidation.

Artisan serves as the investment adviser to Artisan Funds, Artisan Global Funds and other investment products, including Artisan sponsored private funds. Artisan Funds and Artisan Global Funds are corporate entities the business and affairs of which are managed by their respective boards of directors. The shareholders of the funds retain voting rights, including rights to elect and reelect members of their respective boards of directors. Each series of Artisan Funds is a VOE and is separately evaluated for consolidation under the VOE model. The shareholders of Artisan Global Funds lack simple majority liquidation rights, and as a result, each sub-fund of Artisan Global Funds is evaluated for consolidation under the VIE model. Artisan sponsored privately offered funds are also evaluated for consolidation under the VIE model because third-party equity holders of the funds generally lack the ability to divest Artisan of its control of the funds.

From time to time, the Company makes investments in Artisan Funds, Artisan Global Funds, and Artisan sponsored private funds. If the investment results in a controlling financial interest, APAM consolidates the fund, and the underlying activity of the entire fund is included in Artisan's Consolidated Financial Statements. As of June 30, 2018, Artisan has a controlling financial interest in three sub-funds of Artisan Global Funds and certain privately offered funds and, as a result, these funds are included in Artisan's Consolidated Financial Statements. Because these consolidated investment products meet the definition of investment companies under U.S. GAAP, Artisan has retained the specialized industry accounting principles for investment companies in its Consolidated Financial Statements. See Note 6, "Variable Interest Entities and Consolidated Investment Products" for additional details.

Recent accounting pronouncements

Accounting standards adopted as of January 1, 2018

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, which supersedes existing accounting standards for revenue recognition and creates a single framework. The guidance also changes the accounting for certain costs to obtain or fulfill a contract. The Company adopted ASU 2014-09 as of January 1, 2018, utilizing the modified retrospective method. There was no cumulative effect adjustment of applying the new revenue standard and the comparative information has not been restated. There are no significant differences between the reported results under the revenue standard and what would have been reported under the previous revenue guidance, other than the disclosures included in Note 9, ”Revenue From Contracts with Customers”.

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The application of ASU 2014-09 had no impact on the Consolidated Statement of Financial Condition as of June 30, 2018, as compared to the previous revenue recognition standard. The application of the new principal versus agent guidance resulted in presentation changes whereby certain costs are now reported on a gross basis, when the Company is acting as principal, and reported on a net basis, when the Company is acting as an agent. The new standard requires the entire amount of fee waivers and expense reimbursements to be presented net against revenue, which resulted in a $13 thousand decrease in management fee revenue and a corresponding $13 thousand decrease in general and administrative expenses within the Consolidated Statements of Operations for the six months ended June 30, 2018. Applying ASU 2014-09 had no impact on operating income or net income, as compared to applying the previous revenue recognition standard. Artisan did not apply any of the practical expedients in ASU 2014-09.

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities, which requires all equity investments to be measured at fair value with changes in the fair value recognized through net income. The Company adopted ASU 2016-01 as of January 1, 2018, utilizing the modified retrospective method. Upon adoption, the Company made a cumulative-effect adjustment to the Company's Consolidated Statements of Financial Condition, which resulted in a $0.4 million decrease to accumulated other comprehensive income (loss) and a corresponding $0.4 million increase to retained earnings (deficit). The application of ASU 2016-01 results in the recognition of the Company's unrealized gains (losses) on investment securities through net income. The Company recognized $0.6 million of unrealized gains in net income for the six months ended June 30, 2018.

In November 2016, the FASB issued ASU 2016-18, Restricted Cash, to clarify guidance on the classification and presentation of restricted cash in the statement of cash flows. Restricted cash and restricted cash equivalents, including cash of consolidated investment products, is required to be included in cash and cash-equivalent balances in the statement of cash flows. The guidance is effective as of January 1, 2018, and requires retrospective application to all periods presented. The Consolidated Statements of Cash Flows includes a reconciliation to the line items on the Consolidated Statements of Financial Condition.

Accounting standards not yet adopted

In February 2016, the FASB issued ASU 2016-02, Leases, which introduces a lessee model that brings most leases on the balance sheet. The new guidance will be effective on January 1, 2019, and will require a modified retrospective approach to adoption. Early adoption is permitted. The Company is currently evaluating the impact of adoption on its Consolidated Financial Statements. The standard is expected to result in a significant increase in total assets and total liabilities, but will not have a significant impact on the Consolidated Statements of Operations.

Note 3. Investment Securities

The disclosures below include details of Artisan's investments, excluding money market funds and consolidated investment products. Investments held by consolidated investment products are described in Note 6, "Variable Interest Entities and Consolidated Investment Products". Artisan's investment securities as of December 31, 2017 consisted of the following:

	Cost	Unrealized Gains	Unrealized Losses	Fair Value
December 31, 2017				
Mutual funds	$4,361	$ 617	$ —	$ 4,978

Artisan's investments in mutual funds consist of investments in shares of Artisan Funds and Artisan Global Funds. As of January 1, 2018, the Company adopted ASU 2016-01, which requires all equity investments to be measured at fair value with changes in the fair value recognized through net income. As a result, the Company made a cumulative-effect adjustment to reclassify $0.4 million of unrealized gains attributable to APAM from accumulated other comprehensive income (loss) to retained earnings (deficit). The remaining $0.2 million of unrealized gains as of January 1, 2018 were attributable to noncontrolling interests. Effective January 1, 2018, unrealized gains and losses are recorded to net investment income in the statement of operations. The table below presents the Company's unrealized gains and losses for the specified period that relate to investment securities held as of June 30, 2018:

	For the Three	For the Six

	Months Ended June 30, 2018	Months Ended June 30, 2018
Net gains (losses) recognized on investment securities	$ 304	$ 625
Less: Net realized gains (losses) recognized on investment securities sold during the period	$ —	$ —
Unrealized gains (losses) recognized on investment securities held as of the end of the period	$ 304	$ 625

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Note 4. Fair Value Measurements

The table below presents information about Artisan's assets and liabilities that are measured at fair value and the valuation techniques Artisan utilized to determine such fair value. The financial instruments held by consolidated investment products are excluded from the table below and are presented in Note 6, "Variable Interest Entities and Consolidated Investment Products".

In accordance with ASC 820, fair value is defined as the price that Artisan would receive upon selling an investment in an orderly transaction to an independent buyer in the principal or most advantageous market for the investment. The following three-tier fair value hierarchy prioritizes the inputs used in measuring fair value:

- Level 1 – Observable inputs such as quoted (unadjusted) market prices in active markets for identical securities.
- Level 2 – Other significant observable inputs (including but not limited to quoted prices for similar instruments, interest rates, prepayment speeds, credit risk, etc.).
- Level 3—Significant unobservable inputs (including Artisan's own assumptions in determining fair value).

The following provides the hierarchy of inputs used to derive fair value of Artisan's assets and liabilities that are financial instruments as of June 30, 2018 and December 31, 2017:

	Assets and Liabilities at Fair Value			
	Total	Level 1	Level 2	Level 3
June 30, 2018				
Assets				
Money market funds	$69,060	$69,060	$ —	$ —
Mutual funds	5,603	5,603		