

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2020

OR

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

For the transition period from _____ to _____

Commission File Number: 001-36155

MARCUS & MILLICHAP, INC.

(Exact name of registrant as specified in its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

35-2478370
(I.R.S. Employer
Identification No.)

23975 Park Sorrento, Suite 400
Calabasas, California
(Address of Principal Executive Offices)

91302
(Zip Code)

(818) 212-2250
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Trading Symbol(s) | Name of each exchange on which registered |
|--|-------------------|---|
| Common Stock, par value \$0.0001 per share | MMI | New York Stock Exchange |

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 checkmark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter time period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, anon-accelerated filer, a 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.

| | | | |
|-------------------------|-------------------------------------|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> | Smaller reporting company | <input type="checkbox"/> |
| Emerging growth company | <input type="checkbox"/> | | |

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

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

Number of shares of common stock, par value \$0.0001 per share, of the registrant issued and outstanding as of November 2, 2020 was 39,376,477 shares.

MARCUS & MILLICHAP, INC.
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SIGNATURES

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

MARCUS & MILLICHAP, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except for shares and par value)

| | September 30, 2020 (Unaudited) | December 31, 2019 |
|--|-----------------------------------|----------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 173,112 | \$ 232,670 |
| Commissions receivable, net | 6,846 | 5,003 |
| Prepaid expenses | 8,694 | 10,676 |
| Income tax receivable | 10,023 | 4,999 |
| Marketable debt securities, available-for-sale (includes amortized cost of \$169,239 and \$150,517 at September 30, 2020 and December 31, 2019, respectively, and \$0 allowance for credit losses) | 169,513 | 150,752 |
| Advances and loans, net | 2,090 | 2,882 |
| Other assets | <u>3,013</u> | <u>3,185</u> |
| Total current assets | 373,291 | 410,167 |
| Property and equipment, net | 23,371 | 22,643 |
| Operating lease right-of-use assets, net | 82,202 | 90,535 |
| Marketable debt securities, available-for-sale (includes amortized cost of \$44,246 and \$59,468 at September 30, 2020 and December 31, 2019, respectively, and \$0 allowance for credit losses) | 46,505 | 60,809 |
| Assets held in rabbi trust | 9,467 | 9,452 |
| Deferred tax assets, net | 15,839 | 22,122 |
| Goodwill and other intangible assets, net | 36,883 | 22,312 |
| Advances and loans, net | 104,248 | 66,647 |
| Other assets | <u>4,319</u> | <u>4,347</u> |
| Total assets | <u>\$ 696,125</u> | <u>\$ 709,034</u> |
| Liabilities and stockholders' equity | | |
| Current liabilities: | | |
| Accounts payable and other liabilities | \$ 10,601 | \$ 10,790 |
| Notes payable to former stockholders | — | 6,564 |
| Deferred compensation and commissions | 37,244 | 44,301 |
| Operating lease liabilities | 17,954 | 17,762 |
| Accrued bonuses and other employee related expenses | <u>10,238</u> | <u>22,388</u> |
| Total current liabilities | 76,037 | 101,805 |
| Deferred compensation and commissions | 33,921 | 45,628 |
| Operating lease liabilities | 57,002 | 63,155 |
| Other liabilities | <u>8,131</u> | <u>3,539</u> |
| Total liabilities | <u>175,091</u> | <u>214,127</u> |
| Commitments and contingencies | — | — |
| Stockholders' equity: | | |
| Preferred stock, \$0.0001 par value: | | |
| Authorized shares – 25,000,000; issued and outstanding shares – none at September 30, 2020 and December 31, 2019, respectively | — | — |
| Common stock, \$0.0001 par value: | | |
| Authorized shares – 150,000,000; issued and outstanding shares – 39,376,477 and 39,153,195 at September 30, 2020 and December 31, 2019, respectively | 4 | 4 |
| Additional paid-in capital | 110,625 | 104,658 |
| Stock notes receivable from employees | — | (4) |
| Retained earnings | 407,454 | 388,271 |
| Accumulated other comprehensive income | <u>2,951</u> | <u>1,978</u> |
| Total stockholders' equity | <u>521,034</u> | <u>494,907</u> |
| Total liabilities and stockholders' equity | <u>\$ 696,125</u> | <u>\$ 709,034</u> |

See accompanying notes to condensed consolidated financial statements.

MARCUS & MILLICHAP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF NET AND COMPREHENSIVE INCOME
(in thousands, except per share amounts)
(Unaudited)

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|------------------|-------------------|------------------|
| | September 30, | | September 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| <i>Revenues:</i> | | | | |
| Real estate brokerage commissions | \$ 140,844 | \$ 180,198 | \$ 416,044 | \$ 513,815 |
| Financing fees | 15,620 | 16,013 | 43,674 | 47,487 |
| Other revenues | 2,111 | 2,009 | 6,974 | 7,218 |
| Total revenues | 158,575 | 198,220 | 466,692 | 568,520 |
| <i>Operating expenses:</i> | | | | |
| Cost of services | 99,707 | 124,147 | 287,207 | 343,682 |
| Selling, general and administrative | 49,722 | 48,091 | 148,101 | 149,845 |
| Depreciation and amortization | 2,606 | 1,910 | 7,822 | 5,674 |
| Total operating expenses | 152,035 | 174,148 | 443,130 | 499,201 |
| Operating income | 6,540 | 24,072 | 23,562 | 69,319 |
| Other income (expense), net | 1,615 | 2,573 | 4,224 | 9,067 |
| Interest expense | (199) | (329) | (695) | (1,018) |
| Income before provision for income taxes | 7,956 | 26,316 | 27,091 | 77,368 |
| Provision for income taxes | 1,916 | 7,024 | 7,875 | 21,159 |
| Net income | 6,040 | 19,292 | 19,216 | 56,209 |
| <i>Other comprehensive (loss) income:</i> | | | | |
| Marketable debt securities, available-for-sale: | | | | |
| Change in net unrealized gains and losses | (30) | 160 | 687 | 1,874 |
| Less: reclassification adjustment for net losses (gains) included in other income (expense), net | 8 | (23) | 32 | (41) |
| Net change, net of tax of \$(7), \$46, \$246 and \$617 for the three and nine months ended September 30, 2020 and 2019, respectively | (22) | 137 | 719 | 1,833 |
| Foreign currency translation (loss) gain, net of tax of \$0 for each of the three and nine months ended September 30, 2020 and 2019 | (214) | 114 | 254 | (200) |
| Total other comprehensive (loss) income | (236) | 251 | 973 | 1,633 |
| Comprehensive income | \$ 5,804 | \$ 19,543 | \$ 20,189 | \$ 57,842 |
| <i>Earnings per share:</i> | | | | |
| Basic | \$ 0.15 | \$ 0.49 | \$ 0.49 | \$ 1.43 |
| Diluted | \$ 0.15 | \$ 0.49 | \$ 0.48 | \$ 1.42 |
| <i>Weighted average common shares outstanding:</i> | | | | |
| Basic | 39,681 | 39,441 | 39,617 | 39,383 |
| Diluted | 39,727 | 39,550 | 39,676 | 39,527 |

See accompanying notes to condensed consolidated financial statements.

MARCUS & MILLICHAP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands, except for shares)
(Unaudited)

| | Three Months Ended September 30, 2020 | | | | | | | | |
|---|---------------------------------------|-------------|-------------------|-------------|----------------------------------|--|----------------------|--|------------------|
| | Preferred Stock | | Common Stock | | Additional Paid-In Capital | Stock Notes Receivable From Employees | Retained Earnings | Accumulated Other Comprehensive Income (Loss) | Total |
| | Shares | Amount | Shares | Amount | | | | | |
| Balance at June 30, 2020 | — | \$ — | 39,328,017 | \$ 4 | \$108,308 | \$ — | \$401,414 | \$ 3,187 | \$512,913 |
| Net and comprehensive income (loss) | — | — | — | — | — | — | 6,040 | (236) | 5,804 |
| <i>Stock-based award activity</i> | | | | | | | | | |
| Stock-based compensation | — | — | — | — | 2,383 | — | — | — | 2,383 |
| Shares issued pursuant to employee stock purchase plan | — | — | — | — | — | — | — | — | — |
| Issuance of common stock for vesting of restricted stock units | — | — | 50,912 | — | — | — | — | — | — |
| Issuance of common stock for unvested restricted stock awards | — | — | — | — | — | — | — | — | — |
| Shares withheld related to net share settlement of stock-based awards | — | — | (2,452) | — | (66) | — | — | — | (66) |
| Reduction of stock notes receivable from employees | — | — | — | — | — | — | — | — | — |
| Balance as of September 30, 2020 | <u>—</u> | <u>\$ —</u> | <u>39,376,477</u> | <u>\$ 4</u> | <u>\$110,625</u> | <u>\$ —</u> | <u>\$407,454</u> | <u>\$ 2,951</u> | <u>\$521,034</u> |

| | Three Months Ended September 30, 2019 | | | | | | | | |
|---|---------------------------------------|-------------|-------------------|-------------|----------------------------------|--|----------------------|---|------------------|
| | Preferred Stock | | Common Stock | | Additional Paid-In Capital | Stock Notes Receivable From Employees | Retained Earnings | Accumulated Other Comprehensive Income | Total |
| | Shares | Amount | Shares | Amount | | | | | |
| Balance at June 30, 2019 | — | \$ — | 39,090,861 | \$ 4 | \$100,098 | \$ (4) | \$348,258 | \$ 2,157 | \$450,513 |
| Net and comprehensive income | — | — | — | — | — | — | 19,292 | 251 | 19,543 |
| <i>Stock-based award activity</i> | | | | | | | | | |
| Stock-based compensation | — | — | — | — | 2,114 | — | — | — | 2,114 |
| Shares issued pursuant to employee stock purchase plan | — | — | — | — | — | — | — | — | — |
| Issuance of common stock for vesting of restricted stock units | — | — | 41,257 | — | — | — | — | — | — |
| Issuance of common stock for unvested restricted stock awards | — | — | 2,264 | — | — | — | — | — | — |
| Shares withheld related to net share settlement of stock-based awards | — | — | (2,146) | — | (70) | — | — | — | (70) |
| Balance as of September 30, 2019 | <u>—</u> | <u>\$ —</u> | <u>39,132,236</u> | <u>\$ 4</u> | <u>\$102,142</u> | <u>\$ (4)</u> | <u>\$367,550</u> | <u>\$ 2,408</u> | <u>\$472,100</u> |

See accompanying notes to condensed consolidated financial statements.

MARCUS & MILLICHAP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (continued)
(in thousands, except for shares)
(Unaudited)

| | Nine Months Ended September 30, 2020 | | | | | | | | |
|---|--------------------------------------|--------|--------------|--------|----------------------------------|--|----------------------|---|-----------|
| | Preferred Stock | | Common Stock | | Additional Paid-In Capital | Stock Notes Receivable From Employees | Retained Earnings | Accumulated Other Comprehensive Income | Total |
| | Shares | Amount | Shares | Amount | | | | | |
| Balance at December 31, 2019 | — | \$ — | 39,153,195 | \$ 4 | \$104,658 | \$ (4) | \$388,271 | \$ 1,978 | \$494,907 |
| Cumulative effect of a change in accounting principle, net of tax | — | — | — | — | — | — | (33) | — | (33) |
| Balance at January 1, 2020, as adjusted | — | — | 39,153,195 | 4 | 104,658 | (4) | 388,238 | 1,978 | 494,874 |
| Net and comprehensive income | — | — | — | — | — | — | 19,216 | 973 | 20,189 |
| <i>Stock-based award activity</i> | | | | | | | | | |
| Stock-based compensation | — | — | — | — | 7,551 | — | — | — | 7,551 |
| Shares issued pursuant to employee stock purchase plan | — | — | 15,923 | — | 371 | — | — | — | 371 |
| Issuance of common stock for vesting of restricted stock units | — | — | 248,391 | — | — | — | — | — | — |
| Issuance of common stock for unvested restricted stock awards | — | — | 19,516 | — | — | — | — | — | — |
| Shares withheld related to net share settlement of stock-based awards | — | — | (60,548) | — | (1,955) | — | — | — | (1,955) |
| Reduction of stock notes receivable from employees | — | — | — | — | — | 4 | — | — | 4 |
| Balance as of September 30, 2020 | — | \$ — | 39,376,477 | \$ 4 | \$110,625 | \$ — | \$407,454 | \$ 2,951 | \$521,034 |

| | Nine Months Ended September 30, 2019 | | | | | | | | |
|---|--------------------------------------|--------|--------------|--------|----------------------------------|--|----------------------|---|-----------|
| | Preferred Stock | | Common Stock | | Additional Paid-In Capital | Stock Notes Receivable From Employees | Retained Earnings | Accumulated Other Comprehensive Income | Total |
| | Shares | Amount | Shares | Amount | | | | | |
| Balance at December 31, 2018 | — | \$ — | 38,814,464 | \$ 4 | \$ 97,458 | \$ (4) | \$311,341 | \$ 775 | \$409,574 |
| Net and comprehensive income | — | — | — | — | — | — | 56,209 | 1,633 | 57,842 |
| <i>Stock-based award activity</i> | | | | | | | | | |
| Stock-based compensation | — | — | — | — | 7,040 | — | — | — | 7,040 |
| Shares issued pursuant to employee stock purchase plan | — | — | 11,022 | — | 338 | — | — | — | 338 |
| Issuance of common stock for vesting of restricted stock units | — | — | 366,476 | — | — | — | — | — | — |
| Issuance of common stock for unvested restricted stock awards | — | — | 12,806 | — | — | — | — | — | — |
| Shares withheld related to net share settlement of stock-based awards | — | — | (72,532) | — | (2,694) | — | — | — | (2,694) |
| Balance as of September 30, 2019 | — | \$ — | 39,132,236 | \$ 4 | \$102,142 | \$ (4) | \$367,550 | \$ 2,408 | \$472,100 |

See accompanying notes to condensed consolidated financial statements.

MARCUS & MILLICHAP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

| | Nine Months Ended September 30, | |
|--|------------------------------------|-------------------|
| | 2020 | 2019 |
| Cash flows from operating activities | | |
| Net income | \$ 19,216 | \$ 56,209 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Depreciation and amortization | 7,822 | 5,674 |
| Amortization of right-of-use assets | 16,883 | 15,433 |
| Credit loss expense | 55 | 75 |
| Stock-based compensation | 7,551 | 7,040 |
| Deferred taxes, net | 6,050 | 3,829 |
| Unrealized foreign exchange loss | 276 | — |
| Net realized gains on marketable debt securities, available-for-sale | (180) | (70) |
| Other non-cash items | 930 | 489 |
| Changes in operating assets and liabilities: | | |
| Commissions receivable | (1,928) | (1,368) |
| Prepaid expenses | 1,988 | (1,426) |
| Advances and loans | (36,905) | (20,379) |
| Other assets | (1,087) | (10,923) |
| Accounts payable and other liabilities | (1,373) | 103 |
| Income tax receivable/payable | (5,024) | (12,272) |
| Accrued bonuses and other employee related expenses | (12,145) | (11,314) |
| Deferred compensation and commissions | (17,593) | (24,409) |
| Operating lease liabilities | (13,504) | (12,725) |
| Other liabilities | 702 | (19) |
| Net cash used in operating activities | <u>(28,266)</u> | <u>(6,053)</u> |
| Cash flows from investing activities | | |
| Acquisition of businesses, net of cash received | (11,821) | — |
| Purchases of marketable debt securities, available-for-sale | (179,221) | (115,744) |
| Proceeds from sales and maturities of marketable debt securities, available-for-sale | 175,226 | 143,638 |
| Issuances of employee notes receivable | (243) | (200) |
| Payments received on employee notes receivable | 90 | 28 |
| Purchase of property and equipment | (5,412) | (6,643) |
| Net cash (used in) provided by investing activities | <u>(21,381)</u> | <u>21,079</u> |
| Cash flows from financing activities | | |
| Taxes paid related to net share settlement of stock-based awards | (1,955) | (2,694) |
| Proceeds from issuance of shares pursuant to employee stock purchase plan | 371 | 338 |
| Principal payments on notes payable to former stockholders | (6,564) | (1,087) |
| Principal payments on stock appreciation rights liability | (1,251) | (185) |
| Principal payments on contingent consideration | (420) | — |
| Net cash used in financing activities | <u>(9,819)</u> | <u>(3,628)</u> |
| Effect of currency exchange rate changes on cash and cash equivalents | <u>(92)</u> | <u>—</u> |
| Net (decrease) increase in cash and cash equivalents | (59,558) | 11,398 |
| Cash and cash equivalents at beginning of period | 232,670 | 214,683 |
| Cash and cash equivalents at end of period | <u>\$ 173,112</u> | <u>\$ 226,081</u> |
| Supplemental disclosures of cash flow information | | |
| Interest paid during the period | <u>\$ 1,208</u> | <u>\$ 2,092</u> |
| Income taxes paid, net | <u>\$ 6,849</u> | <u>\$ 29,602</u> |

See accompanying notes to condensed consolidated financial statements.

MARCUS & MILLICHAP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Description of Business and Basis of Presentation

Description of Business

Marcus & Millichap, Inc., (the “Company”, “Marcus & Millichap”, or “MMI”), a Delaware corporation, is a brokerage firm specializing in commercial real estate investment sales, financing, research and advisory services. As of September 30, 2020, MMI operates 83 offices in the United States and Canada through its wholly-owned subsidiaries, including the operations of Marcus & Millichap Capital Corporation.

Reorganization and Initial Public Offering

MMI was formed in June 2013 in preparation for Marcus & Millichap Company (“MMC”) to spin-off its majority owned subsidiary, Marcus & Millichap Real Estate Investment Services, Inc. (“MMREIS”). Prior to the initial public offering (“IPO”) of MMI, all of the preferred and common stockholders of MMREIS (including MMC and employees of MMREIS) contributed all of their outstanding shares to MMI, in exchange for new MMI common stock. As a result, MMREIS became a wholly-owned subsidiary of MMI. Thereafter, MMC distributed 80.0% of the shares of MMI common stock to MMC’s shareholders and exchanged the remaining portion of its shares of MMI common stock for cancellation of indebtedness of MMC. MMI completed its IPO in November 2013.

Basis of Presentation

The financial information presented in the accompanying unaudited condensed consolidated financial statements, has been prepared in accordance with rules and regulations of the U.S. Securities and Exchange Commission (“SEC”) for quarterly reports on Form 10-Q and Article 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles (“U.S. GAAP”) for complete financial statements. In the opinion of management, the accompanying unaudited condensed consolidated financial statements and notes include all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of the condensed consolidated financial position, results of operations and cash flows for the periods presented. These unaudited condensed consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements and notes thereto for the year ended December 31, 2019 included in the Company’s Annual Report on Form 10-K filed on March 2, 2020 with the SEC. The results of the nine months ended September 30, 2020 are not necessarily indicative of the results to be expected for the year ending December 31, 2020, for other interim periods or for future years.

Considerations Related to the COVID-19 Pandemic

The COVID-19 pandemic and resultant shutdown of economic activity across much of the world has led to sharp increases in unemployment, volatility in debt and equity markets and businesses instituting cost-cutting and capital-preservation measures. There has been a significant impact on commercial real estate markets in the United States and Canada that started at the end of first quarter 2020, continued through the second quarter of 2020 and to a lesser extent, through the end of the third quarter of 2020, as many property owners have put transactions on hold, driving significantly lower sales volumes.

The Company could experience other potential impacts as a result of the COVID-19 pandemic. Actual results may differ from the Company’s current estimates as there is considerable uncertainty around the scope and duration of the COVID-19 pandemic, and, as a result, the extent of the impact of COVID-19 on our operational and financial performance is uncertain and cannot be predicted. The Company expects the effects of the COVID-19 pandemic to continue to impact its financial position, results of operations, and cash flows for the remainder of 2020 and into calendar year 2021.

See Note 3 – “Property and Equipment, Net”, Note 6 – “Acquisitions, Goodwill and Other Intangible Assets”, Note 10 – “Fair Value Measurements” and Note 15 – “Commitments and Contingencies” for further discussion on COVID-19.

Consolidation

The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the related disclosures at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period, including the impact COVID-19 may have on our business. Actual results could differ from those estimates.

MARCUS & MILLICHAP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Segment Reporting

The Company follows U.S. GAAP for segment reporting, which requires reporting information on operating segments in interim and annual financial statements. Substantially all of the Company's operations involve the delivery of commercial real estate services to our customers including real estate investment sales, financing (including mortgage servicing) and consulting and advisory services. Management makes operating decisions, assesses performance and allocates resources based on an ongoing review of these integrated operations, which constitute the Company's only operating segment for financial reporting purposes.

Reclassifications

Certain prior-period amounts in the condensed consolidated balance sheet and statement of cash flows, Note 7 – "Selected Balance Sheet Data" and Note 10 – "Fair Value Measurements" have been reclassified to conform to the current period presentation. These changes had no impact on the previously reported condensed consolidated results of operations.

2. Accounting Policies and Recent Accounting Pronouncements

Accounting Policies

The complete list of the Company's accounting policies is included in the Company's Annual Report on Form 10-K filed on March 2, 2020 with the SEC. The following are updated, or new accounting policies related to the adoption of the credit losses standard.

Cash and Cash Equivalents

The Company considers cash equivalents to include short-term, highly liquid investments with maturities of three months or less when purchased. Portions of the balance of cash and cash equivalents were held in financial institutions, various money market funds with fixed and floating net asset values and short-term commercial paper. Money market funds have floating net asset values and may be subject to gating or liquidity fees. The Company assesses short-term commercial paper for impairment in connection with investments in marketable debt securities, available-for-sale. The likelihood of realizing material losses from cash and cash equivalents, including the excess of cash balances over federally insured limits, is remote.

Commissions Receivable, Net

Commissions receivable, net consists of commissions earned on brokerage and financing transactions for which payment has not yet been received. The Company evaluates the need for an allowance for credit losses based on consideration of historical experience, current conditions and forecasts of future economic conditions. The majority of commissions receivable are settled within 10 days after the close of escrow.

Advances and Loans, Net

Advances and loans, net includes amounts advanced and loans due from the Company's investment sales and financing professionals.

In order to attract and retain highly skilled professionals, from time to time, the Company advances funds to its investment sales and financing professionals. The advances are typically in the form of forgivable loans that have terms that are generally between 5 and 10 years. The principal amount of a forgivable loan and accrued interest are forgiven over the term of the loan, so long as the investment sales and financing professionals continue to be a service provider with the Company, or upon achieving contractual performance criteria. Amounts forgiven are charged to selling, general and administrative expense at the time the amounts are forgiven. If the investment sales and financing professional's relationship with the Company is terminated before the amount advanced is forgiven, the unforgiven amount becomes due and payable. The Company evaluates the need for an allowance for credit losses based on amounts advanced and expected forgiveness, in consideration of historical experience, current conditions and forecasts of future economic conditions. Estimated credit losses, net of any reversals, are charged to credit loss expense included in selling, general and administrative expense. Amounts are generally written off when amounts are determined to be no longer collectable. Accrued interest, when applicable, has historically been immaterial.

MARCUS & MILLICHAP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The Company, from time to time, enters into various agreements with certain of its investment sales and financing professionals whereby these individuals receive loans. The notes receivable along with stated interest, are typically collected from future commissions or repaid based on the terms stipulated in the respective agreements that are generally between 1 and 7 years. The Company evaluates the need for an allowance for credit losses for the loans based on historical experience, current conditions and reasonable forecasts of future economic conditions. Estimated credit losses, net of any reversals, are charged to credit loss expense included in selling, general and administrative expense. Amounts are generally written off when amounts are determined to be no longer collectable.

Investments in Marketable Debt Securities, Available-for-Sale

The Company maintains a portfolio of investments in a variety of fixed and variable rate debt securities, including U.S. treasuries, U.S. government sponsored entities, corporate debt, asset-backed securities (“ABS”) and other. The Company considers its investments in marketable debt securities to be available-for-sale, and accordingly are recorded at their fair values. The Company determines the appropriate classification of investments in marketable debt securities at the time of purchase. Interest along with amortization of purchase premiums and accretion of discounts from the purchase date through the estimated maturity date, including consideration of variable maturities and contractual call provisions, are included in other income (expense), net in the condensed consolidated statements of net and comprehensive income. The Company typically invests in highly-rated debt securities, and its investment policy generally limits the amount of credit exposure to any one issuer. The policy requires substantially all investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss and matching long-term liabilities.

The Company reviews quarterly its investment portfolio of all securities in an unrealized loss position to determine if an impairment charge or credit reserve is required. The Company excludes accrued interest from both the fair value and the amortized cost basis of marketable debt securities, available-for-sale, for the purposes of identifying and measuring an impairment. An investment is impaired if the fair value is less than its amortized cost basis. Impairment relating to credit losses is recorded through a reduction in the amortized cost of the security or an allowance for credit losses and credit loss expense (included in selling, general and administrative expense), limited by the amount that the fair value is less than the amortized cost basis. Impairment that has not been recorded as a credit loss is recorded through other comprehensive income/loss, net of applicable taxes. The Company made an accounting policy election to not measure an allowance for credit losses for accrued interest receivables. The Company evaluates write-off of accrued interest receivable by the major security-type level at the time credit loss exists for the underlying security.

Determining whether a credit loss exists requires a high degree of judgment and the Company considers both qualitative and quantitative factors in making its determination. The Company evaluates its intent to sell, or whether the Company will more likely than not be required to sell, the security before recovery of its amortized cost basis. For all securities in an unrealized loss position, the Company evaluates, among other items, the extent and length of time the fair market value of a security is less than its amortized cost, time to maturity, duration, seniority, the financial condition of the issuer including credit ratings, any changes thereto and relative default rates, leverage ratios, availability of liquidity to make principle and interest payments, performance indicators of the underlying assets, analyst reports and recommendations and changes in base and market interest rates. If qualitative and quantitative analysis is sufficient to conclude that an impairment related to credit losses does not exist, the Company typically does not perform further quantitative analysis to estimate the present value of cash flows expected to be collected from the debt security. Estimates of expected future cash flows are the Company’s best estimate based on past events, current conditions and reasonable and supportable economic forecasts.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to a concentration of credit risk principally consist of cash and cash equivalents, investments in marketable debt securities, available-for-sale, security deposits (included under other assets, non-current) and commissions receivable, net. Cash and cash equivalents are placed with high-credit quality financial institutions and invested in high-credit quality money market funds and commercial paper. Concentrations of marketable debt securities, available-for-sale are limited by the approved investment policy.

To reduce its credit risk, the Company monitors the credit standing of the financial institutions money market funds that represent amounts recorded as cash and cash equivalents. The Company historically has not experienced any significant losses related to cash and cash equivalents.

The Company derives its revenues from a broad range of real estate investors, owners, and users in the United States and Canada, none of which individually represents a significant concentration of credit risk. The Company maintains allowances, as needed, for estimated credit losses based on management’s assessment of the likelihood of collection. For the three and nine months ended September 30, 2020 and 2019, no transaction represented 10% or more of total revenues. Further, while one or more transactions may represent 10% or more of commissions receivable at any reporting date, amounts due are typically collected within 10 days of settlement and, therefore, do not expose the Company to significant credit risk.

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During the three and nine months ended September 30, 2020, the Company's Canadian operations represented less than 2% of total revenues. During the three and nine months ended September 30, 2019, the Company's Canadian operations represented less than 1% of total revenues.

During the three and nine months ended September 30, 2020 and 2019, no office represented 10% or more of total revenues.

Recent Accounting Pronouncements

Adopted

In June 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-13, *Financial Instruments - Credit Losses* ("ASU 2016-13"). The new standard requires the use of an expected-loss model for financial assets measured at amortized cost and marketable debt securities, available-for-sale, which requires that identified credit losses be presented as an allowance rather than as an impairment write-down. Reversals of credit losses (in situations in which the estimate of credit losses declines) is permitted in the reporting period that the change occurs. Previously, U.S. GAAP prohibited reflecting any reversals of impairment charges. The Company adopted the new standard on January 1, 2020 using the modified-retrospective transition method for assets measured at amortized cost other than marketable debt securities, available-for-sale, which was adopted using a prospective transition approach as required by the new standard. On the adoption date, the Company recorded a cumulative-effect adjustment related to an allowance for credit losses associated with commissions receivable and advances and loans, net of tax in the amount of \$33,000 with the offset to retained earnings as of the beginning of the period presented after adoption. The adoption of ASU 2016-13 did not have a material impact on the Company's investment policy and impairment model for marketable debt securities, available-for-sale. The Company elected the practical expedient to exclude accrued interest from both the fair value and the amortized cost basis of marketable debt securities, available-for-sale, for the purposes of identifying and measuring an impairment.

In August 2018, the FASB issued ASU No. 2018-15, *Internal-Use Software (Subtopic 350-40) - Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract* ("ASU 2018-15"). ASU 2018-15 aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license), by permitting a customer in a cloud computing arrangement that is a service contract to capitalize certain implementation costs as if the arrangement was an internal-use software project. The Company adopted the new standard effective January 1, 2020, using the prospective method. The adoption of ASU 2018-15 did not have a material effect on the Company's condensed consolidated financial statements.

Pending Adoption

In December 2019, the FASB issued ASU No. 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes* ("ASU 2019-12"). ASU 2019-12 is effective for reporting periods beginning after December 15, 2020. For the Company, the new standard will be effective on January 1, 2021. ASU 2019-12 simplifies the accounting for income taxes by eliminating certain exceptions including the methodology for calculating income taxes in an interim period and the recognition of deferred tax liabilities related to outside basis differences. It also clarifies and simplifies other aspects of the accounting for income taxes such as step-up in tax basis for goodwill and interim recognition of enactment of tax laws or rate changes. The Company is currently evaluating the impact of this new standard and does not expect ASU 2019-12 to have a material effect on its condensed consolidated financial statements.

In March 2020, the FASB issued ASU No. 2020-04, *Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting* ("ASU 2020-04"). ASU 2020-04 provides temporary optional exceptions to the guidance in U.S. GAAP on contract modifications to ease the financial reporting burdens related to the expected market transition from the London Interbank Offered Rate (LIBOR) and other interbank offered rates to alternative reference rates, such as the Secured Overnight Financing Rate. ASU 2020-04 is effective for all entities upon issuance and may be applied prospectively to contract modifications through December 31, 2022. The guidance applies to the Company's Credit Agreement (see Note 15 – "Commitments and Contingencies"), which references LIBOR, and will generally allow it to account for and present a modification as an event that does not require contract remeasurement at the modification date or reassessment of a previous accounting determination. As of September 30, 2020, the Company has not drawn funds from the credit facility. The Company continues to evaluate the impact of this new standard and does not expect ASU 2020-04 to have a material effect on its condensed consolidated financial statements.

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3. Property and Equipment, Net

Property and equipment, net consisted of the following (in thousands):

| | September 30, 2020 | December 31, 2019 |
|---|-----------------------|----------------------|
| Computer software and hardware equipment | \$ 29,704 | \$ 25,252 |
| Furniture, fixtures and equipment | 23,309 | 23,468 |
| Less: accumulated depreciation and amortization | (29,642) | (26,077) |
| | <u>\$ 23,371</u> | <u>\$ 22,643</u> |

During the nine months ended September 30, 2020 and 2019, the Company wrote-off approximately \$968,000 and \$3.3 million, respectively, of fully depreciated computer software and hardware equipment and furniture, fixtures and equipment.

As of September 30, 2020 and 2019, property and equipment additions incurred but not yet paid included in accounts payable and other liabilities were \$430,000 and \$264,000, respectively.

The Company evaluates its fixed assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. As of September 30, 2020, the Company considered the impact of COVID-19 pandemic and evaluated its property and equipment for potential indicators of impairment. The Company concluded that as of September 30, 2020, there was no indicators of impairment of its property and equipment.

4. Operating Leases

The Company has operating leases for all of its facilities and autos. As of September 30, 2020 and December 31, 2019, operating lease right-of-use (“ROU”) assets were \$119.2 million and \$111.1 million, respectively, and the related accumulated amortization was \$37.0 million and \$20.6 million, respectively.

The operating lease cost, included in selling, general and administrative expense in the condensed consolidated statement of net and comprehensive income, consisted of the following (in thousands):

| | Three Months Ended | | Nine Months Ended | |
|------------------------------------|--------------------|-----------------|-------------------|-----------------|
| | September 30, | | September 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| Operating lease cost: | | | | |
| Lease cost ⁽¹⁾ | \$ 6,355 | \$ 6,148 | \$18,959 | \$18,163 |
| Variable lease cost ⁽²⁾ | 1,485 | 1,423 | 4,096 | 3,913 |
| Sublease income | (50) | (68) | (216) | (199) |
| | <u>\$ 7,790</u> | <u>\$ 7,503</u> | <u>\$22,839</u> | <u>\$21,877</u> |

⁽¹⁾ Includes short-term lease cost and ROU asset amortization.

⁽²⁾ Primarily relates to common area maintenance, property taxes, insurance, utilities and parking.

Maturities of lease liabilities by year consisted of the following (in thousands):

| | September 30, 2020 |
|--|--------------------|
| Remainder of 2020 | \$ 5,382 |
| 2021 | 21,495 |
| 2022 | 15,998 |
| 2023 | 12,374 |
| 2024 | 10,211 |
| Thereafter | 15,514 |
| Total future minimum lease payments | 80,974 |
| Less imputed interest | (6,018) |
| Present value of operating lease liabilities | <u>\$ 74,956</u> |

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Supplemental cash flow information and noncash activity related to the operating leases consisted of the following (in thousands):

| | Nine Months Ended September 30, | |
|--|------------------------------------|----------|
| | 2020 | 2019 |
| Operating cash flow information: | | |
| Cash paid for amounts included in the measurement of operating lease liabilities | \$15,566 | \$15,064 |
| Noncash activity: | | |
| ROU assets obtained in exchange for operating lease liabilities | \$ 7,771 | \$17,806 |
| Tenant improvements owned by lessor related to ROU assets ⁽¹⁾ | \$ 949 | \$ 3,642 |

⁽¹⁾ Reclassification from other assets current.

Other information related to the operating leases consisted of the following:

| | September 30, 2020 | December 31, 2019 |
|---|--------------------|-------------------|
| Weighted average remaining operating lease term | 4.70 years | 5.04 years |
| Weighted average discount rate | 3.2% | 3.8% |

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5. Investments in Marketable Debt Securities

Amortized cost, allowance for credit losses, gross unrealized gains/losses in accumulated other comprehensive income/loss and fair value of marketable debt securities, available-for-sale, by type of security consisted of the following (in thousands):

| | September 30, 2020 | | | | |
|------------------------------------|--------------------|-----------------------------------|------------------------------|-------------------------------|------------------|
| | Amortized Cost | Allowance for Credit Losses | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| <i>Short-term investments:</i> | | | | | |
| U.S. treasuries | \$ 93,425 | \$ — | \$ 216 | \$ — | \$ 93,641 |
| U.S. government sponsored entities | 37,721 | — | 19 | — | 37,740 |
| Corporate debt | 38,093 | — | 40 | (1) | 38,132 |
| | <u>\$169,239</u> | <u>\$ —</u> | <u>\$ 275</u> | <u>\$ (1)</u> | <u>\$169,513</u> |
| <i>Long-term investments:</i> | | | | | |
| U.S. treasuries | \$ 3,396 | \$ — | \$ 293 | \$ — | \$ 3,689 |
| U.S. government sponsored entities | 1,233 | — | 36 | — | 1,269 |
| Corporate debt | 32,584 | — | 1,837 | (64) | 34,357 |
| ABS and other | 7,033 | — | 189 | (32) | 7,190 |
| | <u>\$ 44,246</u> | <u>\$ —</u> | <u>\$ 2,355</u> | <u>\$ (96)</u> | <u>\$ 46,505</u> |

| | December 31, 2019 | | | |
|------------------------------------|-------------------|------------------------------|-------------------------------|------------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
| <i>Short-term investments:</i> | | | | |
| U.S. treasuries | \$124,389 | \$ 196 | \$ (5) | \$124,580 |
| U.S. government sponsored entities | — | — | — | — |
| Corporate debt | 26,128 | 44 | — | 26,172 |
| | <u>\$150,517</u> | <u>\$ 240</u> | <u>\$ (5)</u> | <u>\$150,752</u> |
| <i>Long-term investments:</i> | | | | |
| U.S. treasuries | \$ 24,188 | \$ 235 | \$ — | \$ 24,423 |
| U.S. government sponsored entities | 1,353 | 3 | (1) | 1,355 |
| Corporate debt | 25,447 | 1,027 | (3) | 26,471 |
| ABS and other | 8,480 | 93 | (13) | 8,560 |
| | <u>\$ 59,468</u> | <u>\$ 1,358</u> | <u>\$ (17)</u> | <u>\$ 60,809</u> |

The Company's investments in available-for-sale debt securities that have been in a continuous unrealized loss position, for which an allowance for credit losses has not been recorded, by type of security consisted of the following (in thousands):

| | September 30, 2020 | | | | | |
|-----------------|---------------------|-------------------------------|----------------------|-------------------------------|-----------------|-------------------------------|
| | Less than 12 months | | 12 months or greater | | Total | |
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| U.S. treasuries | \$ 5,051 | \$ — | \$ — | \$ — | \$ 5,051 | \$ — |
| Corporate debt | 9,823 | (65) | — | — | 9,823 | (65) |
| ABS and other | 1,143 | (25) | 155 | (7) | 1,298 | (32) |
| | <u>\$16,017</u> | <u>\$ (90)</u> | <u>\$155</u> | <u>\$ (7)</u> | <u>\$16,172</u> | <u>\$ (97)</u> |

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| | December 31, 2019 | | | | | |
|------------------------------------|---------------------|-------------------------|----------------------|-------------------------|-----------------|-------------------------|
| | Less than 12 months | | 12 months or greater | | Total | |
| | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses | Fair Value | Gross Unrealized Losses |
| U.S. treasuries | \$39,823 | \$ (5) | \$— | \$ — | \$39,823 | \$ (5) |
| U.S. government sponsored entities | — | — | 566 | (1) | 566 | (1) |
| Corporate debt | 6,029 | (3) | — | — | 6,029 | (3) |
| ABS and other | 1,971 | (13) | — | — | 1,971 | (13) |
| | <u>\$47,823</u> | <u>\$ (21)</u> | <u>\$566</u> | <u>\$ (1)</u> | <u>\$48,389</u> | <u>\$ (22)</u> |

Gross realized gains and losses from the sales of the Company's available-for-sale debt securities consisted of the following (in thousands):

| | Three Months Ended | | Nine Months Ended | |
|--------------------------------------|--------------------|--------------|-------------------|----------------|
| | September 30, | | September 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| Gross realized gains ⁽¹⁾ | <u>\$ 97</u> | <u>\$ 58</u> | <u>\$ 229</u> | <u>\$ 117</u> |
| Gross realized losses ⁽¹⁾ | <u>\$ (34)</u> | <u>\$ —</u> | <u>\$ (49)</u> | <u>\$ (47)</u> |

⁽¹⁾ Recorded in other income (expense), net in the condensed consolidated statements of net and comprehensive income. The cost basis of securities sold were determined based on the specific identification method.

The Company invests its excess cash in a diversified portfolio of fixed and variable rate debt securities to meet current and future cash flow needs. All investments are made in accordance with the Company's approved investment policy. As of September 30, 2020, the portfolio had an average credit rating of AA and weighted term to final maturity of 1.7 years, with 20 securities in the portfolio with an unrealized loss aggregating \$97,000, or 1% of amortized cost, and a weighted average credit rating of AA-.

As of September 30, 2020, the Company performed an impairment analysis and determined an allowance for credit losses was not required. The Company determined that it did not have an intent to sell and it was not more likely than not that the Company would be required to sell any security based on its current liquidity position, or to maintain compliance with its investment policy, specifically as it relates to minimum credit ratings. The Company evaluated the securities with an unrealized loss considering severity of loss, credit ratings, specific credit events during the period since acquisition, overall likelihood of default, market sector, potential impact from the current economic situation and a review of an issuer's and securities liquidity and financial strength, as needed. The Company concluded that it would receive all scheduled interest and principle payments. The Company, therefore, determined qualitatively that the unrealized loss was related to changes in interest rates and other market factors and therefore no allowance for credit losses was required.

Amortized cost and fair value of marketable debt securities, available-for-sale, by contractual maturity consisted of the following (in thousands, except weighted average data):

| | September 30, 2020 | | December 31, 2019 | |
|--|--------------------|-------------------|-------------------|-------------------|
| | Amortized | | Amortized | |
| | Cost | Fair Value | Cost | Fair Value |
| Due in one year or less | \$169,239 | \$ 169,513 | \$150,517 | \$ 150,752 |
| Due after one year through five years | 29,162 | 30,488 | 41,123 | 41,794 |
| Due after five years through ten years | 10,307 | 11,136 | 12,813 | 13,467 |
| Due after ten years | 4,777 | 4,881 | 5,532 | 5,548 |
| | <u>\$213,485</u> | <u>\$ 216,018</u> | <u>\$209,985</u> | <u>\$ 211,561</u> |
| Weighted average contractual maturity | | 1.7 years | | 1.7 years |

Actual maturities may differ from contractual maturities because certain issuers have the right to prepay certain obligations with or without prepayment penalties.

6. Acquisitions, Goodwill and Other Intangible Assets

During the nine months ended September 30, 2020, the Company expanded its network of its real estate sales and financing professionals and provided further diversification to its real estate brokerage and financing services.

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The Company completed an acquisition of two businesses that were accounted for as business combinations and the results have been included in the condensed consolidated financial statements beginning on the acquisition dates. Aggregate terms of these acquisitions included: (i) cash paid at closing of approximately \$11.8 million, net of cash received, (ii) the fair value of contingent consideration of \$1.8 million with payments conditioned upon achieving certain financial metrics, and (iii) the fair value of deferred consideration of \$3.9 million with the only remaining condition on such payments being the passage of time. Contingent consideration and deferred consideration are included in accounts payable and other liabilities and other liabilities captions in the condensed consolidated balance sheets. See Note 10 – “Fair Value Measurements” for additional information on contingent and deferred consideration.

Based on preliminary purchase price allocations, \$8.3 million was allocated to the fair values of intangible assets with the remainder of \$9.2 million allocated to goodwill. The Company recorded acquisition related costs of \$480,000 and \$199,000 for the three months ended September 30, 2020 and 2019, respectively, and \$1.5 million and \$339,000 for the nine months ended September 30, 2020 and 2019, respectively. These amounts are included in selling, general and administrative expense in the accompanying condensed consolidated statements of net and comprehensive income.

The goodwill recorded as part of the acquisitions primarily arises from the acquired assembled workforce and brokerage and financing sales platforms. The Company expects all of the goodwill to be tax deductible, with the tax-deductible amount of goodwill related to the contingent and deferred consideration to be determined once the cash payments are made to settle any contingent and deferred consideration. The goodwill resulting from acquisitions is allocated to the Company’s one reporting unit.

Goodwill and intangible assets, net consisted of the following (in thousands):

| | September 30, 2020 | | | December 31, 2019 | | |
|--|-----------------------------|-----------------------------|-------------------|-----------------------------|-----------------------------|-------------------|
| | Gross Carrying Amount | Accumulated Amortization | Net Book Value | Gross Carrying Amount | Accumulated Amortization | Net Book Value |
| Goodwill and intangible assets: | | | | | | |
| Goodwill | \$24,319 | \$ — | \$24,319 | \$15,072 | \$ — | \$15,072 |
| Intangible assets ⁽¹⁾ | 17,291 | (4,727) | 12,564 | 9,050 | (1,810) | 7,240 |
| | <u>\$41,610</u> | <u>\$ (4,727)</u> | <u>\$36,883</u> | <u>\$24,122</u> | <u>\$ (1,810)</u> | <u>\$22,312</u> |

⁽¹⁾ Total weighted average amortization period was 5.18 years and 4.37 years as of September 30, 2020 and December 31, 2019, respectively.

The changes in the carrying amount of goodwill consisted of the following (in thousands):

| | Nine Months Ended September 30, | |
|-----------------------------|------------------------------------|-----------------|
| | 2020 | 2019 |
| Beginning balance | \$15,072 | \$11,459 |
| Additions from acquisitions | 9,247 | — |
| Impairment losses | — | — |
| Ending balance | <u>\$24,319</u> | <u>\$11,459</u> |

Estimated amortization expense for intangible assets by year for the next five years and thereafter consisted of the following (in thousands):

| | September 30, 2020 |
|-------------------|--------------------|
| Remainder of 2020 | \$ 934 |
| 2021 | 2,857 |
| 2022 | 2,531 |
| 2023 | 2,476 |
| 2024 | 1,963 |
| Thereafter | 1,803 |
| | <u>\$ 12,564</u> |

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The Company evaluates goodwill for impairment annually in the fourth quarter. In addition to the annual impairment evaluation, the Company evaluates at least quarterly whether events or circumstances have occurred in the period subsequent to the annual impairment testing which indicate that it is more likely than not an impairment loss has occurred. The Company evaluates its intangible assets that have finite useful lives whenever an event or change in circumstances indicates that the carrying value of the asset may not be recoverable.

As of September 30, 2020, the Company considered the impact of COVID-19 pandemic and evaluated its goodwill and intangible assets for impairment testing. The Company considered qualitative and quantitative factors, including the impact from the COVID-19 induced economic slowdown and current projected recovery timeframes. The Company estimated the recoverability of the intangible assets by comparing the carrying amount of each asset to the future undiscounted cash flows that the Company expects the asset to generate. The sum of the undiscounted expected future cash flows was greater than the carrying amount of the intangible assets. The Company concluded that as of September 30, 2020, there was no impairment of its goodwill and intangible assets.

7. Selected Balance Sheet Data

Advances and Loans, Net and Commissions Receivable, Net

Allowance for credit losses for advances and loans and commissions receivable consisted of the following (in thousands):

| | Advances and Loans | Commissions Receivable | Total |
|---|-----------------------|---------------------------|---------------|
| Beginning balance as of January 1, 2020 | \$ 512 | \$ 32 | \$544 |
| Credit loss expense | 13 | 42 | 55 |
| Write-offs | (50) | — | (50) |
| Ending balance as of September 30, 2020 | <u>\$ 475</u> | <u>\$ 74</u> | <u>\$549</u> |
| | Advances and Loans | Commissions Receivable | Total |
| Beginning balance as of January 1, 2019 | \$ 514 | \$ — | \$ 514 |
| Credit loss expense | 75 | — | 75 |
| Write-offs | (185) | — | (185) |
| Ending balance as of September 30, 2019 | <u>\$ 404</u> | <u>\$ —</u> | <u>\$ 404</u> |

Other Assets

Other assets consisted of the following (in thousands):

| | Current | | Non-Current | |
|---|-----------------------|----------------------|-----------------------|----------------------|
| | September 30, 2020 | December 31, 2019 | September 30, 2020 | December 31, 2019 |
| Mortgage servicing rights (“MSRs”), net of amortization | \$ — | \$ — | \$ 2,023 | \$ 2,002 |
| Security deposits | — | — | 1,406 | 1,345 |
| Employee notes receivable ⁽¹⁾ | 177 | 65 | 321 | 323 |
| Customer trust accounts and other | 2,836 | 3,120 | 569 | 677 |
| | <u>\$ 3,013</u> | <u>\$ 3,185</u> | <u>\$ 4,319</u> | <u>\$ 4,347</u> |

⁽¹⁾ Reduction of accrued bonuses and other employee related expenses in settlement of employee notes receivable were \$9 and \$60 for the nine months ended September 30, 2020 and 2019, respectively. See Note 9 – “Related-Party Transactions” for additional information.

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MSRs

The net change in the carrying value of MSRs consisted of the following (in thousands):

| | Nine Months Ended September 30, | |
|-------------------|------------------------------------|-----------------|
| | 2020 | 2019 |
| Beginning balance | \$2,002 | \$ 2,209 |
| Additions | 425 | 243 |
| Amortization | (404) | (413) |
| Ending balance | <u>\$2,023</u> | <u>\$ 2,039</u> |

The portfolio of loans serviced by the Company aggregated \$1.7 billion and \$1.6 billion as of September 30, 2020 and December 31, 2019, respectively. See Note 10 – “Fair Value Measurements” for additional information on MSRs.

In connection with MSR activities, the Company holds funds in escrow for the benefit of the lenders. These funds, which totaled \$2.4 million and \$2.6 million as of September 30, 2020 and December 31, 2019, respectively, and the offsetting obligations are not presented in the Company’s condensed consolidated financial statements as they do not represent assets and liabilities of the Company.

Deferred Compensation and Commissions

Deferred compensation and commissions consisted of the following (in thousands):

| | Current | | Non-Current | |
|---|-----------------------|----------------------|-----------------------|----------------------|
| | September 30, 2020 | December 31, 2019 | September 30, 2020 | December 31, 2019 |
| Stock appreciation rights (“SARs”) liability ⁽¹⁾ | \$ 2,162 | \$ 2,080 | \$ 16,493 | \$ 18,122 |
| Commissions payable to investment sales and financing professionals | 33,166 | 40,235 | 10,996 | 20,818 |
| Deferred compensation liability ⁽¹⁾ | 1,482 | 1,553 | 6,432 | 6,688 |
| Other | 434 | 433 | — | — |
| | <u>\$ 37,244</u> | <u>\$ 44,301</u> | <u>\$ 33,921</u> | <u>\$ 45,628</u> |

- ⁽¹⁾ The SARs and deferred compensation liability become subject to payout as a result of a participant no longer being considered as a service provider. As a result of the retirement of certain participants, estimated amounts to be paid to the participants within the next twelve months have been classified as current.

SARs Liability

Prior to the IPO, certain employees of the Company were granted SARs under a stock-based compensation program assumed by MMC. In connection with the IPO, the SARs agreements were revised, the MMC liability of \$20.0 million for the SARs was frozen as of March 31, 2013 and was transferred to MMI through a capital distribution. The SARs liability will be settled with each participant in ten annual installments in January of each year upon retirement or termination from service, or in full upon consummation of a change in control of the Company.

Under the revised agreements, MMI is required to accrue interest on the outstanding balance beginning on January 1, 2014 at a rate based on the 10-year treasury note, plus 2%. The rate resets annually. The rates at January 1, 2020 and 2019 were 3.920% and 4.684%, respectively. MMI recorded interest expense related to this liability of \$178,000 and \$226,000 for the three months ended September 30, 2020 and 2019, respectively, and \$533,000 and \$678,000 for the nine months ended September 30, 2020 and 2019, respectively.

Estimated payouts within the next twelve months for participants that have separated from service have been classified as current. During the nine months ended September 30, 2020 and 2019, the Company made total payments of \$2.1 million and \$1.8 million, consisting of principal and accumulated interest, respectively.

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Commissions Payable

Certain investment sales professionals have the ability to earn additional commissions after meeting certain annual revenue thresholds. These commissions are recognized as cost of services in the period in which they are earned as they relate to specific transactions closed. The Company has the ability to defer payment of certain commissions, at its election, for up to three years. Commissions payable that are not expected to be paid within twelve months are classified as long-term.

Deferred Compensation Liability

A select group of management is eligible to participate in the Marcus & Millichap Deferred Compensation Plan (the “Deferred Compensation Plan”). The Deferred Compensation Plan is a non-qualified deferred compensation plan that is intended to comply with Section 409A of the Internal Revenue Code and permits participants to defer compensation up to the limits set forth in the Deferred Compensation Plan. Amounts are paid out generally when the participant is no longer a service provider; however, an in-service payout election is available to participants. Participants may elect to receive payouts as a lump sum or quarterly over a two to fifteen-year period. The Company elected to fund the Deferred Compensation Plan through company owned variable life insurance policies. The Deferred Compensation Plan is managed by a third-party institutional fund manager, and the deferred compensation and investment earnings are held as a Company asset in a rabbi trust, which is recorded in assets held in rabbi trust in the accompanying condensed consolidated balance sheets. The assets in the trust are restricted unless the Company becomes insolvent, in which case the trust assets are subject to the claims of the Company’s creditors. The Company may also, in its sole and absolute discretion, elect to withdraw at any time a portion of the trust assets by an amount by which the fair market value of the trust assets exceeds 110% of the aggregate deferred compensation liability represented by the participants’ accounts. Estimated payouts within the next twelve months for participants that have separated from service or elected in service payout have been classified as current. During the nine months ended September 30, 2020 and 2019, the Company made total payments to participants of \$1.2 million and \$1.3 million, respectively.

The assets held in the rabbi trust are carried at the cash surrender value of the variable life insurance policies, which represents its fair value. The net change in the carrying value of the assets held in the rabbi trust and the net change in the carrying value of the deferred compensation liability, each exclusive of additional contributions, distributions and trust expenses consisted of the following (in thousands):

| | Three Months Ended | | Nine Months Ended | |
|---|--------------------|-------|-------------------|--------|
| | September 30, | | September 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| Increase in the carrying value of the assets held in the rabbi trust ⁽¹⁾ | \$ 434 | \$ 31 | \$ 170 | \$ 959 |
| Increase in the net carrying value of the deferred compensation obligation ⁽²⁾ | \$ 388 | \$ 31 | \$ 88 | \$ 943 |

⁽¹⁾ Recorded in other income (expense), net in the condensed consolidated statements of net and comprehensive income.

⁽²⁾ Recorded in selling, general and administrative expense in the condensed consolidated statements of net and comprehensive income.

Other Liabilities

Other liabilities consisted of the following (in thousands):

| | Non-Current | |
|--|-----------------------|----------------------|
| | September 30, 2020 | December 31, 2019 |
| Deferred consideration ⁽¹⁾⁽²⁾ | \$ 3,472 | \$ 830 |
| Contingent consideration ⁽¹⁾⁽²⁾ | 3,443 | 2,709 |
| Other | 1,216 | — |
| | <u>\$ 8,131</u> | <u>\$ 3,539</u> |

⁽¹⁾ The current portions of deferred consideration in the amounts of \$1,880 and \$560 as of September 30, 2020 and December 31, 2019, respectively, are included in accounts payable and other liabilities in the condensed consolidated balance sheets. The current portions of contingent consideration in the amounts of \$1,240 and \$678 as of September 30, 2020 and December 31, 2019, respectively, are included in accounts payable and other liabilities in the condensed consolidated balance sheets.

⁽²⁾ Deferred consideration in the aggregate amount of \$1,401 as of December 31, 2019 was reclassified from contingent consideration during the nine months ended September 30, 2020 and of this amount, \$560 and \$841 pertained to the current and non-current portions, respectively.

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8. Notes Payable to Former Stockholders

In conjunction with the spin-off and IPO, notes payable to certain former stockholders of MMREIS were issued in settlement of restricted stock and SARs awards that were redeemed by MMREIS upon the termination of employment by the former stockholders (“the Notes”). Such Notes had been previously assumed by MMC and were transferred to the Company. The Notes were fully paid in April 2020 in the amount of \$6.9 million (\$6.6 million principal and \$333,000 interest).

9. Related-Party Transactions

Shared and Transition Services

Certain services are provided to the Company under a Transition Services Agreement (“TSA”) between MMC and the Company. The TSA is intended to provide certain services until the Company acquires the services separately. Under the TSA, the Company incurred net costs during the three months ended September 30, 2020 and 2019 of \$10,000 and \$21,000, respectively, and during the nine months ended September 30, 2020 and 2019 of \$52,000 and \$96,000, respectively. These amounts are included in selling, general and administrative expense in the accompanying condensed consolidated statements of net and comprehensive income.

Brokerage and Financing Services with the Subsidiaries of MMC

MMC has wholly or majority owned subsidiaries that buy and sell commercial real estate properties. The Company performs certain brokerage and financing services related to transactions of the subsidiaries of MMC. For the three months ended September 30, 2020 and 2019, the Company earned real estate brokerage commissions and financing fees of \$225,000 and \$1.2 million, respectively, from transactions with subsidiaries of MMC related to these services. The Company incurred cost of services of \$130,000 and \$688,000, respectively, related to these revenues. For the nine months ended September 30, 2020 and 2019, the Company earned real estate brokerage commissions and financing fees of \$1.9 million and \$4.0 million, respectively, from transactions with subsidiaries of MMC related to these services. The Company incurred cost of services of \$1.1 million and \$2.3 million, respectively, related to these revenues.

Operating Lease with MMC

The Company has an operating lease with MMC for a single-story office building located in Palo Alto, California, which expires on May 31, 2022. The related operating lease cost was \$333,000 for each of the three months ended September 30, 2020 and 2019, and \$998,000 and \$999,000 for the nine months ended September 30, 2020 and 2019, respectively. Operating lease cost is included in selling, general and administrative expense in the accompanying condensed consolidated statements of net and comprehensive income. See Note 4 – “Operating Leases” for additional information.

Accounts Payable and Other Liabilities with MMC

As of September 30, 2020, and December 31, 2019, accounts payable and other liabilities with MMC totaling \$9,000 and \$88,000, respectively, remain unpaid and are included in accounts payable and other liabilities in the accompanying condensed consolidated balance sheets.

Other

The Company makes advances to non-executive employees from time-to-time. At September 30, 2020 and December 31, 2019, the aggregate principal amount for employee notes receivable was \$498,000 and \$388,000, respectively, which is included in other assets (current and non-current) in the accompanying condensed consolidated balance sheets. See Note 7 – “Selected Balance Sheet Data” for additional information.

As of September 30, 2020, George M. Marcus, the Company’s founder and Co-Chairman, beneficially owned approximately 40% of the Company’s issued and outstanding common stock, including shares owned by Phoenix Investments Holdings, LLC and the Marcus Family Foundation II.

10. Fair Value Measurements

U.S. GAAP defines the fair value of a financial instrument as the amount that would be received from the sale of an asset in an orderly transaction between market participants at the measurement date. The Company is responsible for the determination of fair value and the supporting methodologies and assumptions. The Company uses various pricing sources and third parties to provide and validate the values utilized.

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The degree of judgment used in measuring the fair value of financial instruments is generally inversely correlated with the level of observable valuation inputs. Financial instruments with quoted prices in active markets generally have more pricing observability and less judgment is used in measuring fair value. Financial instruments for which no quoted prices are available have less observability and are measured at fair value using valuation models or other pricing techniques that require more judgment.

Assets recorded at fair value are measured and classified in accordance with a fair value hierarchy consisting of the three “levels” based on the observability of inputs available in the marketplace used to measure the fair values as discussed below:

- *Level 1:* Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;
- *Level 2:* Quoted prices in markets that are not active, or inputs which are observable, either directly or indirectly, for substantially the full term of the asset or liability; or
- *Level 3:* Unobservable inputs reflect management’s best estimate of what market participants would use in pricing the asset or liability at the measurement date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model. Management estimates include certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

Recurring Fair Value Measurements

The Company values its investments, including commercial paper and floating net asset value money market funds recorded in cash and cash equivalents, investments in marketable debt securities, available-for-sale, assets held in the rabbi trust, deferred compensation liability and contingent consideration at fair value on a recurring basis. Fair values for investments included in cash and cash equivalents and marketable debt securities, available-for-sale were determined for each individual security in the investment portfolio and all these securities are Level 1 or 2 measurements as appropriate.

Fair values for assets held in the rabbi trust and related deferred compensation liability were determined based on the cash surrender value of the company owned variable life insurance policies and underlying investments in the trust, and are Level 2 and Level 1 measurements, respectively.

Contingent consideration in connection with acquisitions, is carried at fair value and determined on a contract-by-contract basis, calculated using unobservable inputs based on the probability of achieving EBITDA and other performance requirements, and is a Level 3 measurement. During the nine months ended September 30, 2020, the Company considered the economic impact of COVID-19 on the probability of achieving EBITDA and other performance targets, and current and future interest rates in its determination of fair value for the contingent consideration. The Company is uncertain to the extent of the volatility in the unobservable inputs in the foreseeable future.

Deferred consideration in connection with acquisitions is carried at fair value and calculated using a discounted cash flow estimate with the only remaining condition on such payments being the passage of time, and is a Level 2 measurement.

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Assets and liabilities carried at fair value on a recurring basis consisted of the following (in thousands):

| | September 30, 2020 | | | | December 31, 2019 | | | |
|---|--------------------|------------------|-----------------|-------------|-------------------|------------------|------------------|-------------|
| | Fair Value | Level 1 | Level 2 | Level 3 | Fair Value | Level 1 | Level 2 | Level 3 |
| Assets: | | | | | | | | |
| Assets held in rabbi trust | \$ 9,467 | \$ — | \$ 9,467 | \$ — | \$ 9,452 | \$ — | \$ 9,452 | \$ — |
| Cash equivalents ⁽¹⁾ : | | | | | | | | |
| Commercial paper and other | \$ 2,950 | \$ — | \$ 2,950 | \$ — | \$ 5,087 | \$ — | \$ 5,087 | \$ — |
| Money market funds | 130,045 | 130,045 | — | — | 185,513 | 185,513 | — | — |
| | <u>\$132,995</u> | <u>\$130,045</u> | <u>\$ 2,950</u> | <u>\$ —</u> | <u>\$190,600</u> | <u>\$185,513</u> | <u>\$ 5,087</u> | <u>\$ —</u> |
| Marketable debt securities, available-for-sale: | | | | | | | | |
| <i>Short-term investments:</i> | | | | | | | | |
| U.S. treasuries | \$ 93,641 | \$ 93,641 | \$ — | \$ — | \$ 124,580 | \$ 124,580 | \$ — | \$ — |
| U.S. government sponsored entities | 37,740 | — | 37,740 | — | — | — | — | — |
| Corporate debt | 38,132 | — | 38,132 | — | 26,172 | — | 26,172 | — |
| | <u>\$169,513</u> | <u>\$ 93,641</u> | <u>\$75,872</u> | <u>\$ —</u> | <u>\$150,752</u> | <u>\$124,580</u> | <u>\$ 26,172</u> | <u>\$ —</u> |
| <i>Long-term investments:</i> | | | | | | | | |
| U.S. treasuries | \$ 3,689 | \$ 3,689 | \$ — | \$ — | \$ 24,423 | \$ 24,423 | \$ — | \$ — |
| U.S. government sponsored entities | 1,269 | — | 1,269 | — | 1,355 | — | 1,355 | — |
| Corporate debt | 34,357 | — | 34,357 | — | 26,471 | — | 26,471 | — |
| ABS and other | 7,190 | — | 7,190 | — | 8,560 | — | 8,560 | — |
| | <u>\$ 46,505</u> | <u>\$ 3,689</u> | <u>\$42,816</u> | <u>\$ —</u> | <u>\$ 60,809</u> | <u>\$ 24,423</u> | <u>\$ 36,386</u> | <u>\$ —</u> |
| Liabilities: | | | | | | | | |
| Contingent consideration | \$ 4,683 | \$ — | \$ — | \$4,683 | \$ 3,387 | \$ — | \$ — | \$3,387 |
| Deferred consideration | \$ 5,352 | \$ — | \$ 5,352 | \$ — | \$ 1,390 | \$ — | \$ 1,390 | \$ — |
| Deferred compensation liability | \$ 7,914 | \$ 7,914 | \$ — | \$ — | \$ 8,241 | \$ 8,241 | \$ — | \$ — |

(1) Included in cash and cash equivalents on the accompanying condensed consolidated balance sheets.

There were no transfers in or out of Level 3 during the nine months ended September 30, 2020 and 2019.

As of September 30, 2020 and December 31, 2019, contingent and deferred consideration has a maximum undiscounted payment of \$6.1 million and \$7.3 million, respectively. Assuming the achievement of the applicable performance criteria and/or service and time requirements, the Company anticipates these earn-out and deferred payments will be made over the next one to five-year period. Changes in fair value are included in selling, general and administrative expense in the condensed consolidated statements of net and comprehensive income.

A reconciliation of contingent consideration measured at fair value on a recurring basis consisted of the following (in thousands):

| | Nine Months Ended | |
|---|-------------------|----------------|
| | September 30, | 2019 |
| | 2020 | 2019 |
| Beginning balance ⁽¹⁾ | \$3,387 | \$2,875 |
| Contingent consideration in connection with acquisitions ⁽²⁾ | 1,800 | — |
| Change in fair value of contingent consideration | 134 | (11) |
| Payments of contingent consideration | (638) | — |
| Ending balance | <u>\$4,683</u> | <u>\$2,864</u> |

(1) Beginning balance for 2020 reflects the reclassification of \$1,401 from contingent consideration related to deferred consideration. See Note 7 – “Selected Balance Sheet Data – Other Liabilities” for additional information.

(2) Contingent consideration in connections with acquisitions represents a noncash investing activity.

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Quantitative information about the valuation technique and significant unobservable inputs used in the valuation of the Company's Level 3 financial liabilities measured at fair value on a recurring basis consisted of the following (dollars in thousands):

| | Fair Value at September 30, 2020 | Valuation Technique | Unobservable inputs | Range (Weighted Average) ⁽¹⁾ |
|--------------------------|-------------------------------------|----------------------|-----------------------------|---|
| Contingent consideration | \$ 4,683 | Discounted cash flow | Expected life of cash flows | 0.5-5.0 years (2.0 years) |
| | | | Discount rate | 4.1%-4.4% (4.2%) |
| | | | Probability of achievement | 62%-100.0% (85.5%) |
| | Fair Value at December 31, 2019 | Valuation Technique | Unobservable inputs | Range (Weighted Average) ⁽¹⁾ |
| Contingent consideration | \$ 3,387 | Discounted cash flow | Expected life of cash flows | 0.4-5.8 years (2.4 years) |
| | | | Discount rate | 3.6%-4.9% (4.1%) |
| | | | Probability of achievement | 33.0%-100.0% (74.3%) |

⁽¹⁾ Unobservable inputs were weighted by the relative fair value of the instruments.

Nonrecurring Fair Value Measurements

In accordance with U.S. GAAP, from time to time, the Company measures certain assets at fair value on a nonrecurring basis. The Company reviews the carrying value of MSRs, intangibles, goodwill and other assets for indications of impairment at least annually. When indications of potential impairment are identified, the Company may be required to determine the fair value of those assets and record an adjustment for the carrying amount in excess of the fair value determined. Any fair value determination would be based on valuation approaches, which are appropriate under the circumstances and utilize Level 2 and Level 3 measurements as required.

MSRs are recorded at fair value upon acquisition of a servicing contract. The Company has elected the amortization method for the subsequent measurement of MSRs. MSRs are carried at the lower of amortized cost or fair value. MSRs are a Level 3 measurement. The Company's MSRs do not trade in an active, open market with readily observable prices. The estimated fair value of the Company's MSRs were developed using a discounted cash flow model that calculates the present value of estimated future net servicing income. The model considers contractual provisions and assumptions of market participants including specified servicing fees, prepayment assumptions, delinquency rates, late charges, other ancillary revenue, costs to service and other economic factors. The Company periodically reassesses and adjusts, when necessary, the underlying inputs and assumptions used to reflect observable market conditions and assumptions that a market participant would consider in valuing an MSR asset. Management made revisions to the assumptions used in the determination of fair value for MSRs after considering the economic impact of the COVID-19 pandemic on default, severity, prepayment and discount rates related to the specific types and underlying collateral of the various serviced loans, interest rates, refinance rates, and current government and private sector responses to the pandemic. The fair value of the MSRs approximated the carrying value at September 30, 2020 and December 31, 2019 after consideration of the revisions to the various assumptions. See Note 7 – "Selected Balance Sheet Data – Other Assets – MSRs" for additional information.

As market conditions change, the Company will re-evaluate assumptions used in the determination of fair value for MSRs and is uncertain to the extent of the volatility in the unobservable inputs in the foreseeable future.

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Quantitative information about the valuation technique and significant unobservable inputs used in the valuation of the Company's Level 3 financial assets measured at fair value on a nonrecurring basis consisted of the following (dollars in thousands):

| | Fair Value at September 30, 2020 | Valuation Technique | Unobservable inputs | Range (Weighted Average) ⁽¹⁾ |
|------|-------------------------------------|----------------------|---------------------------|---|
| MSRs | \$ 2,296 | Discounted cash flow | Constant prepayment rates | 0.0%-20.0% (10.0%) |
| | | | Constant default rate | 0.4%-5.1% (1.5%) |
| | | | Loss severity | 24.2%-50.0% (30.1%) |
| | | | Discount rate | 10.0%-10.0% (10.0%) |
| | Fair Value at December 31, 2019 | Valuation Technique | Unobservable inputs | Range (Weighted Average) ⁽¹⁾ |
| MSRs | \$ 2,204 | Discounted cash flow | Constant prepayment rates | 0.0%-20.0% (10.0%) |
| | | | Constant default rate | 2.0%-2.0% (2.0%) |
| | | | Loss severity | 40.0%-40.0% (40.0%) |
| | | | Discount rate | 9.5%-9.7% (9.7%) |

⁽¹⁾ Weighted average is based on the 10% constant prepayment rate scenario which the Company uses as the reported fair value.

11. Stockholders' Equity

Common Stock

As of September 30, 2020 and December 31, 2019, there were 39,376,477 and 39,153,195 shares of common stock, \$0.0001 par value, issued and outstanding, which include unvested restricted stock awards ("RSAs") issued to non-employee directors, respectively. See Note 14 – "Earnings per Share" for additional information.

Preferred Stock

The Company has 25,000,000 authorized shares of preferred stock with a par value \$0.0001 per share. At September 30, 2020 and December 31, 2019, there were no preferred shares issued or outstanding.

Accumulated Other Comprehensive Income/Loss

Amounts reclassified from accumulated other comprehensive income/loss include marketable debt securities, available for sale are included as a component of other income (expense), net or selling, general and administrative expense, as applicable, in the condensed consolidated statements of net and comprehensive income. The reclassifications were determined on a specific identification basis.

The Company has not provided for U.S. taxes on unremitted earnings of its foreign subsidiary as it is operating at a loss and has no earnings and profits to remit. As a result, deferred taxes were not provided related to the cumulative foreign currency translation adjustments.

12. Stock-Based Compensation Plans

2013 Omnibus Equity Incentive Plan

The Company's board of directors adopted the 2013 Omnibus Equity Incentive Plan (the "2013 Plan"), which became effective upon the Company's IPO. In February 2017, the board of directors amended and restated the 2013 Plan, which was approved by the Company's stockholders in May 2017. Grants are made from time to time by the compensation committee of the Company's board of directors at its discretion, subject to certain restrictions as to the number and value of shares that may be granted to any individual. In addition, non-employee directors receive annual grants under a director compensation policy. As of September 30, 2020, there were 4,931,055 shares available for future grants under the 2013 Plan.

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Awards Granted and Settled

Under the 2013 Plan, the Company has issued RSAs to non-employee directors and restricted stock units (“RSUs”) to employees and independent contractors. RSAs vest in equal annual installments over a one-year period from the date of grant. RSUs generally vest in equal annual installments over a five-year period from the date of grant or earlier as approved by the compensation committee of the Company’s board of directors. Any unvested awards are canceled upon termination as a service provider. As of September 30, 2020, there were no issued or outstanding options, SARs, performance units or performance share awards under the 2013 Plan.

During the nine months ended September 30, 2020, 248,391 shares of RSUs vested and 60,548 shares of common stock were withheld to pay applicable required employee statutory withholding taxes based on the market value of the shares on the vesting date. The shares withheld for taxes were returned to the share reserve and are available for future issuance in accordance with provisions of the 2013 Plan. During the nine months ended September 30, 2020, there were no deferred stock units (“DSUs”) that settled.

Outstanding Awards

Activity under the 2013 Plan consisted of the following (dollars in thousands, except weighted average per share data):

| | RSA Grants to Non-employee Directors | RSU Grants to Employees | RSU Grants to Independent Contractors | Total | Weighted- Average Grant Date Fair Value Per Share |
|--|--|-------------------------------|---|------------------|--|
| Nonvested shares at December 31, 2019 | 17,480 | 525,115 | 257,480 | 800,075 | \$ 33.91 |
| Granted | 19,516 | 306,008 | 83,738 | 409,262 | 32.88 |
| Vested | (20,268) | (164,091) | (84,300) | (268,659) | 33.08 |
| Transferred | — | (18,294) | 18,294 | — | 33.67 |
| Forfeited/canceled | — | (16,804) | (7,230) | (24,034) | 34.84 |
| Nonvested shares at September 30, 2020 | <u>16,728</u> | <u>631,934</u> | <u>267,982</u> | <u>916,644</u> | 33.67 |
| Unrecognized stock-based compensation expense as of September 30, 2020 ⁽¹⁾ | <u>\$ 266</u> | <u>\$ 18,779</u> | <u>\$ 8,174</u> | <u>\$ 27,219</u> | |
| Weighted average remaining vesting period (years) as of September 30, 2020 | <u>0.59</u> | <u>3.74</u> | <u>3.31</u> | <u>3.58</u> | |

⁽¹⁾ The total unrecognized compensation expense is expected to be recognized over a weighted-average period of approximately 3.58 years.

Employee Stock Purchase Plan

In 2013, the Company adopted the 2013 Employee Stock Purchase Plan (“ESPP”). The ESPP is intended to qualify under Section 423 of the Internal Revenue Code and provides for consecutive, non-overlapping 6-month offering periods. The offering periods generally start on the first trading day on or after May 15 and November 15 of each year. Qualifying employees may purchase shares of the Company stock at a 10% discount based on the lower of the market price at the beginning or end of the offering period, subject to IRS limitations. The Company determined that the ESPP was a compensatory plan and is required to expense the fair value of the awards over each 6-month offering period.

The ESPP initially had 366,667 shares of common stock reserved, and 188,550 shares of common stock remain available for issuance as of September 30, 2020. The ESPP provides for annual increases in the number of shares available for issuance under the ESPP, equal to the least of (i) 366,667 shares, (ii) 1% of the outstanding shares on such date, or (iii) an amount determined by the compensation committee of the board of directors. Pursuant to the provisions of the ESPP, the board of directors has determined to not provide for any annual increases to date. At September 30, 2020, total unrecognized compensation cost related to the ESPP was \$30,000 and is expected to be recognized over a weighted average period of 0.13 years.

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SARs and DSUs

Prior to the IPO, certain employees were granted SARs. As of March 31, 2013, the outstanding SARs were frozen at the liability amount, and will be paid out to each participant in installments upon retirement or departure under the terms of the revised SARs agreements. To replace beneficial ownership in the SARs, the difference between the book value liability and the fair value of the awards was granted to plan participants in the form of DSUs, which were fully vested upon receipt and will be settled in actual stock at a rate of 20% per year if the participant remains employed by the Company during that period (otherwise all unsettled shares of stock upon termination from service will be settled five years from the termination date, unless otherwise agreed to by the Company). In the event of death or termination of service after reaching the age of 67, 100% of the DSUs will be settled. As of September 30, 2020, the remaining future share settlements of fully vested DSUs by year consisted of the following:

| | September 30, 2020 |
|------|--------------------|
| 2021 | 60,373 |
| 2022 | 281,193 |
| | 341,566 |

Summary of Stock-Based Compensation

Components of stock-based compensation are included in selling, general and administrative expense in the condensed consolidated statements of net and comprehensive income and consisted of the following (in thousands):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--------------------------------|-------------------------------------|----------|------------------------------------|----------|
| | 2020 | 2019 | 2020 | 2019 |
| ESPP | \$ 62 | \$ 40 | \$ 145 | \$ 108 |
| RSAs – non-employee directors | 120 | 157 | 493 | 481 |
| RSUs – employees | 1,413 | 1,230 | 4,583 | 4,197 |
| RSUs – independent contractors | 788 | 687 | 2,330 | 2,254 |
| | \$ 2,383 | \$ 2,114 | \$ 7,551 | \$ 7,040 |

13. Income Taxes

The Company's effective tax rate for the three and nine months ended September 30, 2020 was 24.1% and 29.1%, respectively, compared to 26.7% and 27.3% for the three and nine months ended September 30, 2019, respectively. The Company provides for the effects of income taxes in interim financial statements based on the Company's estimate of its annual effective tax rate for the full year, which is based on forecasted income by jurisdiction where the Company operates, adjusted for any tax effects of items that relate discretely to the period, if any.

The provision for income taxes differs from the amount computed by applying the U.S. federal statutory rate to income before provision for income taxes and consisted of the following (dollars in thousands):

| | Three Months Ended September 30, | | | | Nine Months Ended September 30, | | | |
|--|----------------------------------|--------|---------|--------|---------------------------------|-------|----------|--------|
| | 2020 | | 2019 | | 2020 | | 2019 | |
| | Amount | Rate | Amount | Rate | Amount | Rate | Amount | Rate |
| Income tax expense at the federal statutory rate | \$1,671 | 21.0% | \$5,526 | 21.0% | \$5,689 | 21.0% | \$16,247 | 21.0% |
| State income tax expense, net of federal benefit | 453 | 5.7% | 1,118 | 4.2% | 1,403 | 5.2% | 3,359 | 4.3% |
| Shortfall (windfall) tax benefits, net related to stock-based compensation | 130 | 1.6% | 53 | 0.2% | 203 | 0.7% | (201) | (0.2)% |
| Change in valuation allowance | 134 | 1.7% | 408 | 1.6% | 594 | 2.2% | 874 | 1.1% |
| Permanent and other items ⁽¹⁾ | (472) | (5.9)% | (81) | (0.3)% | (14) | — | 880 | 1.1% |
| | \$1,916 | 24.1% | \$7,024 | 26.7% | \$7,875 | 29.1% | \$21,159 | 27.3% |

⁽¹⁾ Permanent items relate principally to compensation charges, qualified transportation fringe benefits, meals and entertainment and reversal of uncertain tax positions.

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14. Earnings per Share

Basic and diluted earnings per share for the three and nine months ended September 30, 2020 and 2019, respectively consisted of the following (in thousands, except per share data):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|-------------------------------------|----------------|------------------------------------|----------------|
| | 2020 | 2019 | 2020 | 2019 |
| Numerator (Basic and Diluted): | | | | |
| Net income | \$ 6,040 | \$ 19,292 | \$ 19,216 | \$ 56,209 |
| Denominator: | | | | |
| <i>Basic</i> | | | | |
| Weighted average common shares issued and outstanding | 39,357 | 39,116 | 39,293 | 39,062 |
| Deduct: Unvested RSAs ⁽¹⁾ | (18) | (17) | (18) | (21) |
| Add: Fully vested DSUs ⁽²⁾ | 342 | 342 | 342 | 342 |
| Weighted Average Common Shares Outstanding | <u>39,681</u> | <u>39,441</u> | <u>39,617</u> | <u>39,383</u> |
| Basic earnings per common share | <u>\$ 0.15</u> | <u>\$ 0.49</u> | <u>\$ 0.49</u> | <u>\$ 1.43</u> |
| <i>Diluted</i> | | | | |
| Weighted Average Common Shares Outstanding from above | 39,681 | 39,441 | 39,617 | 39,383 |
| Add: Dilutive effect of RSUs, RSAs & ESPP | 46 | 109 | 59 | 144 |
| Weighted Average Common Shares Outstanding | <u>39,727</u> | <u>39,550</u> | <u>39,676</u> | <u>39,527</u> |
| Diluted earnings per common share | <u>\$ 0.15</u> | <u>\$ 0.49</u> | <u>\$ 0.48</u> | <u>\$ 1.42</u> |
| Antidilutive shares excluded from diluted earnings per common share ⁽³⁾ | <u>696</u> | <u>425</u> | <u>719</u> | <u>325</u> |

- (1) RSAs were issued and outstanding to the non-employee directors and have a one-year vesting term subject to service requirements. See Note 12 – “Stock-Based Compensation Plans” for additional information.
- (2) Shares are included in weighted average common shares outstanding as the shares are fully vested but have not yet been delivered. See Note 12 – “Stock-Based Compensation Plans” for additional information.
- (3) Primarily pertaining to RSU grants to the Company’s employees and independent contractors.

15. Commitments and Contingencies

Credit Agreement

On June 18, 2014, the Company entered into a Credit Agreement with Wells Fargo Bank, National Association (the “Bank”), as amended and restated on May 28, 2019 and further, amended on November 27, 2019 (the “Credit Agreement”). The Credit Agreement provides for a \$60.0 million principal amount senior secured revolving credit facility that is guaranteed by all of the Company’s domestic subsidiaries (the “Credit Facility”) and matures on June 1, 2022. The Company may borrow, repay and reborrow amounts under the Credit Facility until its maturity date, at which time all amounts outstanding under the Credit Facility must be repaid in full.

Borrowings under the Credit Agreement are available for general corporate purposes and working capital. The Credit Facility includes a \$10.0 million sublimit for the issuance of standby letters of credit of which \$533,000 was utilized at September 30, 2020. Borrowings under the Credit Facility will bear interest, at the Company’s option, at either (i) a fluctuating rate per annum 2.00% below the Base Rate (defined as the highest of (a) the Bank’s prime rate, (b) one-month LIBOR plus 1.50%, and (c) the federal funds rate plus 1.50%), or (ii) at a fixed rate per annum determined by Bank to be 0.875% above LIBOR. In connection with the amendment of the Credit Agreement, the Company paid bank fees and other expenses, which are being amortized over the remaining term of the Credit Agreement. The Company pays a commitment fee of up to 0.1% per annum, payable quarterly, based on the amount of unutilized commitments under the Credit Facility. The amortization and commitment fee is included in interest expense in the accompanying condensed consolidated statements of net and comprehensive income and was \$22,000 and \$20,000 during the three months ended September 30, 2020 and 2019, respectively, and \$65,000 and \$72,000 during the nine months ended September 30, 2020 and 2019, respectively. As of September 30, 2020, there were no amounts outstanding under the Credit Agreement.

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The Credit Facility contains customary covenants, including financial and other covenant reporting requirements and events of default. Financial covenants require the Company, on a combined basis with its guarantors, to maintain (i) an EBITDAR Coverage Ratio (as defined in the Credit Agreement) of not less than 1.25:1.0 as of each quarter end, determined on a rolling four-quarter basis, and (ii) total funded debt to EBITDA not greater than 2.0:1.0 as of each quarter end, determined on a rolling four-quarter basis, and also limits investments in foreign entities and certain other loans. The Credit Facility is secured by substantially all assets of the Company, including pledges of 100% of the stock or other equity interest of each subsidiary except for the capital stock of a controlled foreign corporation (as defined in the Internal Revenue Code), in which case no such pledge is required. As of September 30, 2020, the Company was in compliance with all financial and non-financial covenants and has not experienced any limitation in its operations as a result of the covenants.

Other

In connection with certain agreements with investment sales and financing professionals, the Company may agree to advance amounts to certain investment sales and financing professionals upon reaching certain time and performance goals. Such commitments as of September 30, 2020 aggregated \$21.6 million.

16. Subsequent Events

In October 2020, the Company acquired a commercial real estate capital markets advisory firm specializing in debt placement and equity advisory services, commercial and residential loan sales and consultative/due diligence services across all property types in the United States.

In connection with agreements in principal with investment sales and financing professionals and business acquisitions, the Company entered into commitments through the date these condensed consolidated financial statements were issued, aggregating \$24.8 million. Such commitments are subject to various time and performance conditions.

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

Unless the context requires otherwise, the words “Marcus & Millichap,” “we,” the “Company,” “us” and “our” refer to Marcus & Millichap, Inc., Marcus & Millichap Real Estate Investment Services, Inc. and its other consolidated subsidiaries.

Forward-Looking Statements

The following discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of many factors, including but not limited to the continuing impact of the COVID-19 pandemic. The results of operations for the three and nine months ended September 30, 2020 are not necessarily indicative of the results that may be expected for the full year ending December 31, 2020, or for any other future period. The following discussion should be read in conjunction with the unaudited condensed consolidated financial statements and the notes thereto included in Item 1 of this Form 10-Q and in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2019 filed with the SEC on March 2, 2020, including the “Risk Factors” section and the consolidated financial statements and notes included therein.

Overview

We are a leading national brokerage firm specializing in commercial real estate investment sales, financing, research and advisory services. We have been the top commercial real estate investment broker in the United States based on the number of investment transactions over the last 10 years. As of September 30, 2020, we had 1,999 investment sales and financing professionals that are primarily exclusive independent contractors operating in 83 offices, who provide real estate brokerage and financing services to sellers and buyers of commercial real estate. We also offer market research, consulting and advisory services to our clients. During the three and nine months ended September 30, 2020, we closed 2,139 and 5,976 investment sales, financing and other transactions with total sales volume of approximately \$9.1 billion and \$27.8 billion, respectively. During the year ended December 31, 2019, we closed 9,726 investment sales, financing and other transactions with total sales volume of approximately \$49.7 billion.

We generate revenues by collecting real estate brokerage commissions upon the sale, and fees upon the financing of, commercial properties and by providing consulting, advisory and other real estate services. Real estate brokerage commissions are typically based upon the value of the property, and financing fees are typically based upon the size of the loan. During the three months ended September 30, 2020, approximately 89% of our revenues were generated from real estate brokerage commissions, 10% from financing fees and 1% from other real estate related services. During the nine months ended September 30, 2020, approximately 89% of our revenues were generated from real estate brokerage commissions, 9% from financing fees and 2% from other real estate related services. During the year ended December 31, 2019, approximately 91% of our revenues were generated from real estate brokerage commissions, 8% from financing fees and 1% from other real estate related services.

We divide commercial real estate into four major market segments, characterized by price:

- Properties priced less than \$1 million;
- *Private client market*: properties priced from \$1 million to up to but less than \$10 million;
- *Middle market*: properties priced from \$10 million to up to but less than \$20 million; and
- *Larger transaction market*: properties priced from \$20 million and above.

Our strength is in serving private clients in the \$1-\$10 million private client market segment, which contributed approximately 69% and 67% of our real estate brokerage commissions during the three months ended September 30, 2020 and 2019, respectively, and approximately 68% and 67% of our real estate brokerage commissions during each of the nine months ended September 30, 2020 and 2019, respectively. The following table sets forth the number of transactions, sales volume and revenues by commercial real estate market segment for real estate brokerage:

| Real Estate Brokerage | Three Months Ended September 30, | | | | | | Change | | |
|---|----------------------------------|-------------------------|----------------------------|--------------|-------------------------|----------------------------|--------------|-------------------------|----------------------------|
| | 2020 | | | 2019 | | | Number | Volume (in millions) | Revenues (in thousands) |
| | Number | Volume (in millions) | Revenues (in thousands) | Number | Volume (in millions) | Revenues (in thousands) | | | |
| <\$1 million | 241 | \$ 156 | \$ 6,290 | 274 | \$ 173 | \$ 7,182 | (33) | \$ (17) | \$ (892) |
| Private client market (\$1—<\$10 million) | 1,168 | 3,592 | 97,856 | 1,301 | 4,257 | 121,228 | (133) | (665) | (23,372) |
| Middle market (\$10—<\$20 million) | 70 | 945 | 17,643 | 109 | 1,466 | 25,997 | (39) | (521) | (8,354) |
| Larger transaction market (≥\$20 million) | 48 | 2,302 | 19,055 | 69 | 3,675 | 25,791 | (21) | (1,373) | (6,736) |
| | <u>1,527</u> | <u>\$ 6,995</u> | <u>\$ 140,844</u> | <u>1,753</u> | <u>\$ 9,571</u> | <u>\$ 180,198</u> | <u>(226)</u> | <u>\$ (2,576)</u> | <u>\$ (39,354)</u> |

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| Real Estate Brokerage | Nine Months Ended September 30, | | | | | | | | |
|---|---------------------------------|-------------------------|----------------------------|--------------|-------------------------|----------------------------|--------------|-------------------------|----------------------------|
| | 2020 | | | 2019 | | | Change | | |
| | Number | Volume (in millions) | Revenues (in thousands) | Number | Volume (in millions) | Revenues (in thousands) | Number | Volume (in millions) | Revenues (in thousands) |
| <\$1 million | 649 | \$ 410 | \$ 16,550 | 733 | \$ 474 | \$ 19,607 | (84) | \$ (64) | \$ (3,057) |
| Private client market (\$1—<\$10 million) | 3,203 | 10,207 | 282,937 | 3,753 | 12,160 | 345,812 | (550) | (1,953) | (62,875) |
| Middle market (\$10—<\$20 million) | 204 | 2,785 | 51,902 | 312 | 4,234 | 76,521 | (108) | (1,449) | (24,619) |
| Larger transaction market (≥\$20 million) | 161 | 7,459 | 64,655 | 194 | 9,040 | 71,875 | (33) | (1,581) | (7,220) |
| | <u>4,217</u> | <u>\$ 20,861</u> | <u>\$ 416,044</u> | <u>4,992</u> | <u>\$ 25,908</u> | <u>\$ 513,815</u> | <u>(775)</u> | <u>\$ (5,047)</u> | <u>\$ (97,771)</u> |

Acquisitions

We continue to increase our market presence through execution of our growth strategies by targeting markets based on population, employment, level of commercial real estate sales, inventory and competitive opportunities where we believe the markets will benefit from our commercial real estate investment sales, financing, research and advisory services. During the nine months ended September 30, 2020, we completed two acquisitions that expanded our market presence in financing services in the Southwest and in real estate brokerage services in the Southeast.

In October 2020, the Company acquired a commercial real estate capital markets advisory firm specializing in debt placement and equity advisory services, commercial and residential loan sales and consultative/due diligence services across all property types in the United States.

COVID-19

In March 2020, the World Health Organization characterized COVID-19 as a pandemic. Many states and cities, including where we conduct our business activities, reacted by instituting quarantines, restrictions on travel, “shelter in place” rules, and restrictions on types of business that may continue to operate, which may limit the activity of our sales and financing professionals in engaging with our clients. We implemented measures such as increased sanitizing, physical distancing and remote work arrangements, with the goal of protecting our employees, sales and financing professionals and clients. We continue to follow the local guidelines in cities where our offices are located, and all of our offices have re-opened and are available to our employees and sales and financing professionals on an as needed basis.

We are closely monitoring the impact of COVID-19 pandemic on all aspects of our business and in the regions we operate. Since the start of the pandemic, we have taken multiple measures to support our investment sales and financing professionals’ ability to generate and execute business remotely. Such measures include multiple technological solutions, intensified internal training and education, as well as a significant increase in client outreach and investor education webcasts. The pandemic has caused a major market disruption, and we have seen significant slowing of our real estate brokerage and financing transaction activity, difficulty in pricing assets and, in certain cases, restrictions on the ability of borrowers to access the capital markets and other sources of financing. Our business was impacted during the third quarter of 2020, with the number of transactions and total revenues declining 12.2% and 20.0% in the three months ended September 30, 2020, respectively compared to the same period in 2019. During the third quarter of 2020, we saw some recovery in transaction activity and our total revenues from the initial impact of COVID-19, with the number of transactions and total revenues increasing 34.8% and 35.1%, respectively on a sequential basis compared to the second quarter. Given these circumstances, our financial results continue to be well-below prior levels, the reversal of which remains a major priority for us. We are also exploring extended use of technology and resource sharing measures adopted over the past six months as ways to achieve more efficiency on a long-term basis. For the foreseeable future, we believe that the effect of the COVID-19 restrictions, including the effects of preventative and precautionary health measures mandated to us by federal, state and local governments will likely continue to affect our ability to identify and close commercial real estate transactions.

The long-term impact of the disruption in financial markets, consumer spending, unemployment as well as other unanticipated consequences remain unknown. Additionally, we are unable to predict the extent of the negative impact that the COVID-19 pandemic will continue to have on our financial condition, results of operations and cash flows due to numerous uncertainties and the fluidity of this situation. Although the negative impact to our business has moderated to some extent, we anticipate that total revenues will be negatively impacted for at least the fourth quarter of 2020 and until more stable business conditions begin to resume in 2021. These uncertainties include the scope, severity and duration of the pandemic, expectation gaps among buyers and sellers on pricing and property operation vulnerability to further economic weakness and/or slow recovery, a more difficult market environment for new sales and financing professionals who are experiencing extended ramp-up time to reach production goals, the actions taken by state and local governments to contain the pandemic or mitigate its impact, the direct and indirect economic effects of the pandemic and containment measures and actions taken, and the impact of these and other factors on our employees, independent contractors and clients and potential clients.

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We continue to monitor the expected trends and related demand for our services and will continue to adjust our operations accordingly. In response to this ongoing period of business disruption, we assessed our cost structure and instituted various expense reduction initiatives, including but not limited to, compensation reductions, reductions in events and travel, suspension of company matching contributions in our 401(k) plan and layoffs to preserve our balance sheet and financial position. These reductions were strategically decided upon to ensure proper allocation of capital and human resources to support our sales force's ability to conduct business as well as develop strategic investments in tools, technology and infrastructure vital to our long-term competitiveness. We have reinstated some of our furloughs and compensation levels for certain employees; however, the compensation reductions of our senior executives remain in effect. We expect real estate sales and financing volumes to improve and eventually post solid growth after the market is able to assess the impact of the economic shut down on property occupancies, rent collections and values and when financing flows improve. Due to a high degree of uncertainty, the timing of this recovery in real estate transactions and therefore, our revenues are difficult to forecast. Our priority is to support our team's efforts to increase client contact, provide expanded content and advisory services to investors and clients and preserve our financial position through expense reductions. Given our significant liquidity, we expect our company to be well positioned to benefit from and contribute to the real estate transaction recovery when it emerges, including making accretive and synergistic acquisitions, which will help expand service offerings and market coverage.

Factors Affecting Our Business

Our business and our operating results, financial condition and liquidity are significantly affected by the number and size of commercial real estate investment sales and financing transactions that we close in any period. The number and size of these transactions are affected by our ability to recruit and retain investment sales and financing professionals, identify and contract properties for sale and identify those that need financing and refinancing. We principally monitor the commercial real estate market through four factors, which generally drive our business. The factors are the economy, commercial real estate supply and demand, capital markets and investor sentiment and investment activity.

The Economy

Our business is dependent on economic conditions within the markets in which we operate. Changes in the economy on a global, national, regional or local basis can have a positive or a negative impact on our business. Economic indicators and projections related to job growth, unemployment, interest rates, retail spending and confidence trends can have a positive or a negative impact on our business. Overall market conditions, including global trade, interest rate changes and job creation, can affect investor sentiment and, ultimately, the demand for our services from investors in real estate.

The U.S. economy continues to grapple with the impact of COVID-19, and although we believe some progress has been made, the pace of employment growth lost momentum over the course of the third quarter. The CARES Act stimulus package delivered in March offered the economy an important backstop, but many benefits including expanded federal unemployment and the Paycheck Protection Program ended in the third quarter. Numerous businesses that were closed in the second quarter lockdown have since reopened but are only operating at partial capacity. The hospitality and retail sectors have been particularly hard hit. As a result, total employment as of the end of September remained 10.7 million positions short of pre-pandemic levels. With COVID-19 infections once again rising in the U.S., we expect that economic growth in the fourth quarter to be moderate. Election-related uncertainty and financial market volatility also remain risks to the economy and commercial real estate investment sales and financing volumes. Additional stimulus remains in negotiation on Capitol Hill and could accelerate the economic recovery and boost consumer confidence in the short term. We believe that ultimately, vaccine and effective therapeutics are likely required for the economy to fully recover. We also believe that a significant level of business and consumer pent up demand will be released at some point, which could support a robust period of recovery; however, the timing of such recovery is very difficult to predict. At the same time, we observe that a broad range of unknowns, including health, economic and public policy have increased investor uncertainty, and many investors are continuing to wait on the sidelines for either increased economic clarity or for significant distressed asset buying opportunities to emerge.

Commercial Real Estate Supply and Demand

Our business is dependent on the willingness of investors to invest in or sell commercial real estate, which is affected by many factors beyond our control. These factors include the supply of commercial real estate coupled with user demand for these properties and the performance of real estate assets when compared with other investment alternatives, such as stocks and bonds.

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The apartment and single-tenant property types, which are a significant part of our business, have performed relatively well as they have been more stable than the other property types. The hotel sector and parts of the retail sector continue to face headwinds, although we believe segments of each of the sectors appear to have built some momentum. While large destination tourist hotels and those catering to conferences continue to face the severe impact of the pandemic, it appears smaller drivable vacation hotels have partially recovered. In the retail sector, older enclosed shopping malls, experiential retail, gyms, movie theaters and sit-down dining restaurants have faced extensive difficulties while restaurants with drive-thru facilities, necessity and discount retailers as well as pharmacies have in many cases partially recovered. Suburban office and apartment properties have generally outperformed their urban counterparts as home offices and need for more space outweighed the many closed amenities offered in the urban core. Industrial property performance, meanwhile, has generally remained stable, bolstered by the rapid ascension of eCommerce as a primary consumption channel. Rent collections for apartment, office and industrial properties remain above 90 percent, but collections could face increased pressure if another round of stimulus and/or a health solution is not delivered soon. We believe risks to apartment collections could be mitigated by the renewal of federal unemployment benefits or the addition of a rent assistance program. That said, asset performance varies significantly by locality as cities across the country have faced wide-ranging economic and health-related fallout. Some cities have only experienced a marginal rise in unemployment while other have been impacted more severely.

Capital Markets

Credit and liquidity issues in the financial markets have a direct impact on the flow of capital to the commercial real estate market. Real estate purchases are often financed with debt and, as a result, credit and liquidity impact transaction activity and prices. Changes in interest rates, as well as steady and protracted movements of interest rates in one direction, whether increases or decreases, could adversely or positively affect the operations and income potential of commercial real estate properties, as well as lender and equity underwriting for real estate investments. These changes influence the demand of investors for commercial real estate investments.

Following the second quarter uncertainty-driven financing slowdown, lenders have become more active. Led by local and regional banks, financing liquidity for most property types and locations is available at interest rates near all-time lows. Hotels and some retail centers, which are the property types grappling with the greatest levels of distress, still face limited access to debt capital. Other property types, particularly those that have maintained strong rent collections, have financing options. Speculative investment, including construction and value-add assets face closer lender scrutiny. The increased debt liquidity and particularly low interest rates have supported rising investor activity in the third quarter compared to the second quarter, but transaction activity remains well below pre-crisis levels. The Federal Reserve's commitment to low interest rates could support the low interest rate climate, and we believe market liquidity should remain strong barring a significant medical or financial market setback.

Investor Sentiment and Investment Activity

We rely on investors to buy and sell properties in order to generate commissions. Investors' desires to engage in real estate transactions are dependent on many factors that are beyond our control. The economy, supply and demand for properly positioned properties, available credit and market events impact investor sentiment and, therefore, transaction velocity. In addition, our private clients are often motivated to buy, sell and/or refinance properties due to personal circumstances such as death, divorce, partnership breakups and estate planning.

Investor activity gained ground in the third quarter despite uncertainties surrounding health, economic, policy and operational variables. Questions remain for substantially all facets of the near-term real estate sector outlook, but many investors are adapting to the new climate. Because the pandemic has affected each property type and each market differently, price discovery remains a hurdle in the transaction process. However, we believe low interest rates and generally broad capital availability have been positive forces supporting activity. We believe the many investors still on the sidelines have ample capital on-hand that could spur transaction activity once the uncertainties begin to abate or if a wave of distressed assets come to market. Looking forward, election uncertainty in the United States, particularly in relation to future tax policy, could be a concern for investors. Potential changes to capital gains and estate taxes could influence activity either to the upside or downside in the coming year. Nonetheless, a medical solution to the health crisis could remain the single most significant factor determining investor decisions.

Seasonality

Our real estate brokerage commissions and financing fees have tended to be seasonal and, combined with other factors, can affect an investor's ability to compare our financial condition and results of operations on a quarter-by-quarter basis. Historically, this seasonality has generally caused our revenue, operating income, net income and cash flows from operating activities to be lower in the first half of the year and higher in the second half of the year, particularly in the fourth quarter. The concentration of earnings and cash flows in the last nine months of the year, particularly in the fourth quarter, is generally due to an industry-wide focus of clients to complete transactions towards the end of the calendar year. This historical trend could be disrupted either positively or negatively by major economic, political events, natural disasters or pandemics such as the COVID-19 pandemic, which may impact, among other things, investor sentiment for a particular property type or location, volatility in financial markets, current and future projections of interest rates, attractiveness of other asset classes, market liquidity and the extent of limitations or availability of capital allocations for larger property buyers. Private client investors may also accelerate or delay transactions due to personal or business-related reasons unrelated to economic or political events. In addition, our operating margins are typically lower during the second half of each year due to our commission structure for some of our senior investment sales and financing professionals. These senior investment sales and financing professionals are on a graduated commission schedule that resets annually, pursuant to which higher commissions are paid for higher sales volumes. Our historical pattern of seasonality may be significantly disrupted by the COVID-19 pandemic due to uncertainties around substantially all aspects of the economy and may not continue to the same degree experienced in prior years.

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Operating Segments

We follow the guidance for segment reporting, which requires reporting information on operating segments in interim and annual financial statements. Substantially all of our operations involve the delivery of commercial real estate services to our customers including real estate investment sales, financing, consulting, advisory and other real estate related services. Management makes operating decisions, assesses performance and allocates resources based on an ongoing review of these integrated operations, which constitute only one operating segment for financial reporting purposes.

Key Financial Measures and Indicators

Revenues

Our revenues are primarily generated from our real estate investment sales business. In addition to real estate brokerage commissions, we generate revenues from financing fees and from other real estate related revenues, which are primarily comprised of consulting and advisory fees.

Because our business is transaction oriented, we rely on investment sales and financing professionals to continually develop leads, identify properties to sell and finance, market those properties and close the sale timely to generate a consistent flow of revenue. While our sales volume is impacted by seasonality factors, the timing of closings is also dependent on many market and personal factors unique to a particular client or transaction, particularly clients transacting in the \$1-\$10 million private client market segment. These factors can cause transactions to be accelerated or delayed beyond our control. Further, commission rates earned are generally inversely related to the value of the property sold. As a result of our expansion into the middle and larger transaction market segments, we have seen our overall commission rates fluctuate from period-to-period as a result of changes in the relative mix of the number and volume of investment sales transactions closed in the middle and larger transaction market segments as compared to the \$1-\$10 million private client market segment. These factors may result in period-to-period variations in our revenues that differ from historical patterns.

A small percentage of our transactions include retainer fees and/or breakage fees. Retainer fees are credited against a success-based fee paid upon the closing of a transaction or a breakage fee. Transactions that are terminated before completion will sometimes generate breakage fees, which are usually calculated as a set amount or a percentage of the fee we would have received had the transaction closed.

Real Estate Brokerage Commissions

We earn real estate brokerage commissions by acting as a broker for commercial real estate owners seeking to sell or investors seeking to buy properties. Revenues from real estate brokerage commissions are typically recognized at the close of escrow.

Financing Fees

We earn financing fees by securing financing on purchase transactions or by securing refinancing of our clients' existing mortgage debt. We recognize financing fee revenues at the time the loan closes, and we have no remaining significant obligations for performance in connection with the transaction. To a lesser extent, we also earn mortgage servicing revenue, mortgage servicing fees and ancillary fees associated with financing activities. We recognize mortgage servicing revenues upon the acquisition of a servicing obligation. We generate mortgage servicing fees through the provision of collection, remittance, recordkeeping, reporting and other related mortgage servicing functions, activities and services.

Other Revenues

Other revenues include fees generated from consulting, advisory and other real estate services performed by our investment sales professionals, as well as referral fees from other real estate brokers. Revenues from these services are recognized as they are performed and completed.

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Operating Expenses

Our operating expenses consist of cost of services, selling, general and administrative expenses and depreciation and amortization. The significant components of our expenses are further described below.

Cost of Services

The majority of our cost of services expense is variable commissions paid to our investment sales professionals and compensation-related costs related to our financing activities. Commission expenses are directly attributable to providing services to our clients for investment sales and financing services. Most of our investment sales and financing professionals are independent contractors and are paid commissions; however, because there are some who are initially paid a salary and certain of our financing professionals are employees, costs of services also include employee-related compensation, employer taxes and benefits for those employees. The commission rates we pay to our investment sales and financing professionals vary based on individual contracts negotiated and are generally higher for the more experienced professionals. Some of our most senior investment sales and financing professionals also have the ability to earn additional commissions after meeting certain annual revenue thresholds. These additional commissions are recognized as cost of services in the period in which they are earned. Payment of a portion of these additional commissions are generally deferred for a period of three years, at our election, and paid at the beginning of the fourth calendar year. Cost of services also includes referral fees paid to other real estate brokers where we are the principal service provider. Cost of services, therefore, can vary based on the commission structure of the independent contractors that closed transactions in any particular period.

Selling, General and Administrative Expenses

The largest expense component within selling, general and administrative expenses is personnel expenses for our management team and sales and support staff. In addition, these costs include facilities costs (excluding depreciation and amortization), staff related expenses, sales, marketing, legal, telecommunication, network, data sources, transaction costs related to acquisitions, changes in fair value for contingent consideration and other administrative expenses. Also included in selling, general and administrative are expenses for stock-based compensation to non-employee directors, employees and independent contractors (i.e. investment sales and financing professionals) under the Amended and Restated 2013 Omnibus Equity Incentive Plan ("2013 Plan") and the 2013 Employee Stock Purchase Plan ("ESPP").

Depreciation and Amortization Expense

Depreciation expense consists of depreciation recorded on our computer software and hardware and furniture, fixture and equipment. Depreciation is provided over estimated useful lives ranging from three to seven years for assets. Amortization expense consists of (i) amortization recorded on our mortgage servicing rights ("MSRs") using the interest method over the period that servicing income is expected to be received and (ii) amortization recorded on intangible assets amortized on a straight-line basis using a useful life between one and six years.

Other Income (Expense), Net

Other income (expense), net primarily consists of interest income, net gains or losses on our deferred compensation plan assets, realized gains and losses on our marketable debt securities, available-for-sale, foreign currency gains and losses and other non-operating gains and losses.

Interest Expense

Interest expense primarily consists of interest expense associated with the stock appreciation rights ("SARs") liability, notes payable to former stockholders and our credit agreement.

Provision for Income Taxes

We are subject to U.S. and Canadian federal taxes and individual state and local taxes based on the income generated in the jurisdictions in which we operate. Our effective tax rate fluctuates as a result of the change in the mix of our activities in the jurisdictions we operate due to differing tax rates in those jurisdictions and the impact of permanent items, including principally compensation charges, qualified transportation fringe benefits, reversal of uncertain tax positions, meals and entertainment and tax-exempt deferred compensation plan assets. Our provision for income taxes includes the windfall tax benefits and shortfall expense, net, from shares issued in connection with our 2013 Plan and ESPP.

We record deferred taxes, net based on the tax rate expected to be in effect at the time those items are expected to be recognized for tax purposes.

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Results of Operations

Following is a discussion of our results of operations for the three and nine months ended September 30, 2020 and 2019. The tables included in the period comparisons below provide summaries of our results of operations. The period-to-period comparisons of financial results are not necessarily indicative of future results.

Key Operating Metrics

We regularly review a number of key metrics to evaluate our business, measure our performance, identify trends affecting our business, formulate financial projections, and make strategic decisions. During the three months ended September 30, 2020 and 2019, we closed more than 2,100 and 2,400 investment sales, financing and other transactions, respectively, with total sales volume of approximately \$9.1 billion and \$12.1 billion, respectively. During the nine months ended September 30, 2020 and 2019, we closed more than 5,900 and 6,900 investment sales, financing and other transactions, respectively, with total sales volume of approximately \$27.8 billion and \$34.9 billion, respectively. Such key metrics for real estate brokerage and financing activities (excluding other transactions) are as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|-------------------------------------|-----------|------------------------------------|-----------|
| | 2020 | 2019 | 2020 | 2019 |
| <i>Real Estate Brokerage</i> | | | | |
| Average Number of Investment Sales Professionals | 1,917 | 1,837 | 1,911 | 1,829 |
| Average Number of Transactions per Investment Sales Professional | 0.80 | 0.95 | 2.21 | 2.73 |
| Average Commission per Transaction | \$92,236 | \$102,794 | \$98,659 | \$102,928 |
| Average Commission Rate | 2.01% | 1.88% | 1.99% | 1.98% |
| Average Transaction Size (in thousands) | \$ 4,581 | \$ 5,460 | \$ 4,947 | \$ 5,190 |
| Total Number of Transactions | 1,527 | 1,753 | 4,217 | 4,992 |
| Total Sales Volume (in millions) | \$ 6,995 | \$ 9,571 | \$20,861 | \$ 25,908 |
| | | | | |
| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| <i>Financing ⁽¹⁾</i> | | | | |
| Average Number of Financing Professionals | 82 | 98 | 86 | 103 |
| Average Number of Transactions per Financing Professional | 5.39 | 5.01 | 15.13 | 13.23 |
| Average Fee per Transaction | \$33,531 | \$ 31,203 | \$31,607 | \$ 33,361 |
| Average Fee Rate | 0.88% | 0.90% | 0.89% | 0.91% |
| Average Transaction Size (in thousands) | \$ 3,828 | \$ 3,460 | \$ 3,533 | \$ 3,685 |
| Total Number of Transactions | 442 | 491 | 1,301 | 1,363 |
| Total Financing Volume (in millions) | \$ 1,692 | \$ 1,699 | \$ 4,597 | \$ 5,023 |

⁽¹⁾ Operating metrics calculated excluding certain financing fees not directly associated to transactions.

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Comparison of Three Months Ended September 30, 2020 and 2019

Below are key operating results for the three months ended September 30, 2020 compared to the three months ended September 30, 2019 (dollars in thousands):

| | Three Months Ended | Percentage of | Three Months Ended | Percentage of | Change | |
|--|--------------------|---------------|--------------------|---------------|-------------------|----------------|
| | September 30, 2020 | Revenue | September 30, 2019 | Revenue | Dollar | Percentage |
| Revenues: | | | | | | |
| Real estate brokerage commissions | \$ 140,844 | 88.8% | \$ 180,198 | 90.9% | \$(39,354) | (21.8)% |
| Financing fees | 15,620 | 9.9 | 16,013 | 8.1 | (393) | (2.5)% |
| Other revenues | 2,111 | 1.3 | 2,009 | 1.0 | 102 | 5.1% |
| Total revenues | 158,575 | 100.0 | 198,220 | 100.0 | \$(39,645) | (20.0)% |
| Operating expenses: | | | | | | |
| Cost of services | 99,707 | 62.9 | 124,147 | 62.6 | (24,440) | (19.7)% |
| Selling, general and administrative | 49,722 | 31.4 | 48,091 | 24.3 | 1,631 | 3.4% |
| Depreciation and amortization | 2,606 | 1.6 | 1,910 | 1.0 | 696 | 36.4% |
| Total operating expenses | 152,035 | 95.9 | 174,148 | 87.9 | (22,113) | (12.7)% |
| Operating income | 6,540 | 4.1 | 24,072 | 12.1 | (17,532) | (72.8)% |
| Other income (expense), net | 1,615 | 1.0 | 2,573 | 1.4 | (958) | (37.2)% |
| Interest expense | (199) | (0.1) | (329) | (0.2) | 130 | (39.5)% |
| Income before provision for income taxes | 7,956 | 5.0 | 26,316 | 13.3 | (18,360) | (69.8)% |
| Provision for income taxes | 1,916 | 1.2 | 7,024 | 3.6 | (5,108) | (72.7)% |
| Net income | \$ 6,040 | 3.8% | \$ 19,292 | 9.7% | \$(13,252) | (68.7)% |
| Adjusted EBITDA ⁽¹⁾ | \$ 12,229 | 7.7% | \$ 27,865 | 14.1% | \$(15,636) | (56.1)% |

(1) Adjusted EBITDA is not a measurement of our financial performance under U.S. generally accepted accounting principles (“U.S. GAAP”) and should not be considered as an alternative to net income, operating income or any other measures derived in accordance with U.S. GAAP. For a definition of Adjusted EBITDA and a reconciliation of Adjusted EBITDA to net income, see “Non-GAAP Financial Measure.”

Revenues

Our total revenues were \$158.6 million for the three months ended September 30, 2020 compared to \$198.2 million for the same period in 2019, a decrease of \$39.6 million, or 20.0%. Total revenues decreased primarily as a result of decreases in real estate brokerage commissions as financing fees and other revenues were comparable, as described below.

Real estate brokerage commissions. Revenues from real estate brokerage commissions decreased to \$140.8 million for the three months ended September 30, 2020 from \$180.2 million for the same period in 2019, a decrease of \$39.4 million, or 21.8%. The decrease was primarily driven by a 26.9% reduction in sales volume, partially offset by a 13 basis points increase in average commission rates. Sales volume was primarily impacted by a 16.1% decrease in the average transaction size and a 12.9% decrease in the number of transactions, primarily as a result of the economic uncertainty and other transactional impediments surrounding the COVID-19 pandemic.

Financing fees. Revenues from financing fees of \$15.6 million for the three months ended September 30, 2020 were relatively comparable to the \$16.0 million for the same period in 2019. This was primarily the result of increased re-financings due to lower interest rates offset by decreased financings for purchases resulting primarily from the economic uncertainty and other transactional impediments surrounding the COVID-19 pandemic.

Other revenues. Other revenues of \$2.1 million for the three months ended September 30, 2020 were comparable to the \$2.0 million for the same period in 2019.

Operating expenses

Our total operating expenses were \$152.0 million for the three months ended September 30, 2020 compared to \$174.1 million for the same period in 2019, a decrease of \$22.1 million, or 12.7%. The decrease was primarily due to a decrease in cost of services, which are variable commissions paid to our investment sales professionals and compensation related costs in connection with our financing activities, partially offset by increases in selling, general and administrative costs and depreciation and amortization expense, as described below.

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Cost of services. Cost of services decreased to \$99.7 million for the three months ended September 30, 2020 from \$124.1 million for the same period in 2019, a decrease of \$24.4 million, or 19.7%. The decrease was primarily due to decreased commission expenses driven by the related decreased revenues noted above. Cost of services as a percent of total revenues increased to 62.9% compared to 62.6% for the same period in 2019 primarily due to a higher proportion of transactions closed by our more senior investment sales and financing professionals. Due to the uncertainty surrounding COVID-19, we expect cost of services as a percent of total revenues to remain elevated in the coming quarters as we expect the majority of the deals closed to be weighted towards senior investment sales and financing professionals.

Selling, general and administrative expense. Selling, general and administrative expense for the three months ended September 30, 2020 increased \$1.6 million, or 3.4%, to \$49.7 million from \$48.1 million for the same period in 2019. The increase was primarily due to (i) variable employee incentive compensation due to better than expected results in the third quarter of 2020, as well as additional accrual driven by the improved full-year financial performance outlook as compared to projections made at the onset of the COVID-19 pandemic; (ii) prior year's low accrual level for variable employee incentive compensation due to that period's performance shortfall from plan; and (iii) business development, marketing and other support related to the long-term retention of our sales and financing professionals, as well as recent additions of experienced professionals. These increases were partially offset by COVID-19 related (i) reductions in headcount, salaries and related benefits and (ii) decreases in sales events, travel and other related expenses.

Depreciation and amortization expense. Depreciation and amortization expense increased to \$2.6 million for the three months ended September 30, 2020 from \$1.9 million for the same period in 2019, an increase of \$0.7 million, or 36.4%. The increase was primarily driven by the increase in amortization of intangible assets resulting from the increase in intangible assets due to acquisitions.

Other Income (Expense), Net

Other income (expense), net decreased to \$1.6 million for the three months ended September 30, 2020 from \$2.6 million for the same period in 2019. The decrease was primarily driven by (i) a \$1.6 million reduction in interest income on our investments in marketable debt securities, available-for-sale due to overall decrease in interest rates and (ii) a \$0.3 million reduction in net other categories. The decrease was partially offset by (i) a \$0.5 million increase in foreign currency gain related to our Canadian operations; and (ii) a \$0.4 million favorable change in the value of our deferred compensation plan assets that are held in a rabbi trust.

Interest Expense

Interest Expense decreased to \$0.2 million for the three months ended September 30, 2020 from \$0.3 million for the same period in 2019. The decrease for the three months ended September 30, 2020 was primarily due to no interest expense related to notes payable to former stockholders, which was fully repaid during the second quarter of 2020, compared to the same period in 2019.

Provision for Income Taxes

The provision for income taxes was \$1.9 million for the three months ended September 30, 2020 compared to \$7.0 million in the same period in 2019, a decrease of \$5.1 million, or 72.7%, primarily due to the significant decline in income before provision for income taxes and a partial reversal of a reserve of uncertain tax positions. The effective income tax rate for the three months ended September 30, 2020 was 24.1% compared to 26.7% for the same period in 2019.

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Comparison of Nine Months Ended September 30, 2020 and 2019

Below are key operating results for the nine months ended September 30, 2020 compared to the nine months ended September 30, 2019 (dollars in thousands):

| | Nine Months Ended September 30, 2020 | Percentage of Revenue | Nine Months Ended September 30, 2019 | Percentage of Revenue | Change | |
|--|---|--------------------------|---|--------------------------|------------------|----------------|
| | | | | | Dollar | Percentage |
| Revenues: | | | | | | |
| Real estate brokerage commissions | \$ 416,044 | 89.1% | \$ 513,815 | 90.4% | \$ (97,771) | (19.0)% |
| Financing fees | 43,674 | 9.4 | 47,487 | 8.4 | (3,813) | (8.0)% |
| Other revenues | 6,974 | 1.5 | 7,218 | 1.2 | (244) | (3.4)% |
| Total revenues | 466,692 | 100.0 | 568,520 | 100.0 | (101,828) | (17.9)% |
| Operating expenses: | | | | | | |
| Cost of services | 287,207 | 61.5 | 343,682 | 60.5 | (56,475) | (16.4)% |
| Selling, general and administrative | 148,101 | 31.7 | 149,845 | 26.3 | (1,744) | (1.2)% |
| Depreciation and amortization | 7,822 | 1.8 | 5,674 | 1.0 | 2,148 | 37.9% |
| Total operating expenses | 443,130 | 95.0 | 499,201 | 87.8 | (56,071) | (11.2)% |
| Operating income | 23,562 | 5.0 | 69,319 | 12.2 | (45,757) | (66.0)% |
| Other income (expense), net | 4,224 | 0.9 | 9,067 | 1.6 | (4,843) | (53.4)% |
| Interest expense | (695) | (0.1) | (1,018) | (0.2) | 323 | (31.7)% |
| Income before provision for income taxes | 27,091 | 5.8 | 77,368 | 13.6 | (50,277) | (65.0)% |
| Provision for income taxes | 7,875 | 1.7 | 21,159 | 3.7 | (13,284) | (62.8)% |
| Net income | \$ 19,216 | 4.1% | \$ 56,209 | 9.9% | \$ (36,993) | (65.8)% |
| Adjusted EBITDA ⁽¹⁾ | \$ 38,757 | 8.3% | \$ 83,040 | 14.6% | \$ (44,283) | (53.3)% |

(1) Adjusted EBITDA is not a measurement of our financial performance under U.S. GAAP and should not be considered as an alternative to net income, operating income or any other measures derived in accordance with U.S. GAAP. For a definition of Adjusted EBITDA and a reconciliation of Adjusted EBITDA to net income, see “Non-GAAP Financial Measure.”

Revenues

Our total revenues were \$466.7 million for the nine months ended September 30, 2020 compared to \$568.5 million for the same period in 2019, a decrease of \$101.8 million, or 17.9%. Total revenues decreased primarily as a result of decreases in real estate brokerage commissions and to a lesser extent, financing fees, as described below.

Real estate brokerage commissions. Revenues from real estate brokerage commissions decreased to \$416.0 million for the nine months ended September 30, 2020 from \$513.8 million for the same period in 2019, a decrease of \$97.8 million, or 19.0%. The decrease was driven by a 19.5% reduction in sales volume. Sales volume was impacted by a 15.5% decrease in the number of transactions and a 4.7% decrease in the average transaction size, primarily as a result of the economic uncertainty and other transactional impediments surrounding the COVID-19 pandemic. The average commission rates remained comparable.

Financing fees. Revenues from financing fees decreased to \$43.7 million for the nine months ended September 30, 2020 from \$47.5 million for the same period in 2019, a decrease of \$3.8 million, or 8.0%. The decrease was driven by an 8.5% reduction in financing volume and a 2 basis points reduction in the average commission rates. Financing volume was impacted the economic uncertainty and other transactional impediments surrounding the COVID-19 pandemic.

Other revenues. Other revenues of \$7.0 million for the nine months ended September 30, 2020 were comparable to the \$7.2 million for the same period in 2019.

Operating expenses

Our total operating expenses were \$443.1 million for the nine months ended September 30, 2020 compared to \$499.2 million for the same period in 2019, a decrease of \$56.1 million, or 11.2%. The decrease was primarily due to a decrease in cost of services, which are variable commissions paid to our investment sales professionals and compensation related costs in connection with our financing activities, and a decrease in selling, general and administrative costs, partially offset by an increase in depreciation and amortization expense, as described below.

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Cost of services. Cost of services decreased to \$287.2 million for the nine months ended September 30, 2020 from \$343.7 million for the same period in 2019, a decrease of \$56.5 million, or 16.4%. The decrease was primarily due to decreased commission expenses driven by the related decreased revenues noted above. Cost of services as a percent of total revenues increased to 61.5% compared to 60.5% for the same period in 2019 primarily due to a higher proportion of transactions closed by our more senior investment sales and financing professionals.

Selling, general and administrative expense. Selling, general and administrative expense for the nine months ended September 30, 2020 decreased \$1.7 million, or 1.2%, to \$148.1 million from \$149.8 million for the same period in 2019. Decreases in our selling, general and administrative expense have been driven by our various expense reduction initiatives. The decrease was primarily due to reductions in (i) compensation related costs, primarily driven by decreases in variable employee incentive compensation, salaries and related benefits due to COVID-19, and deferred compensation obligations and (ii) sales events, travel and other related expenses due to COVID-19. These decreases were partially offset by increases in (i) business development, marketing and other support related to the long-term retention of our sales and financing professionals, as well as recent additions of experienced professionals; (ii) acquisition related costs; (iii) facilities expenses due to expansion of existing offices; and (iv) certain licensing fees.

Depreciation and amortization expense. Depreciation and amortization expense increased to \$7.8 million for the nine months ended September 30, 2020 from \$5.7 million for the same period in 2019, an increase of \$2.1 million, or 37.9%. The increase was primarily driven by the increase in amortization of intangible assets resulting from the increase in intangible assets due to acquisitions.

Other Income (Expense), Net

Other income (expense), net decreased to \$4.2 million for the nine months ended September 30, 2020 from \$9.1 million for the same period in 2019. The decrease was primarily driven by (i) a \$3.5 million reduction in interest income on our investments in marketable debt securities, available-for-sale due to overall decrease in interest rates; (ii) a \$0.8 million unfavorable change in the value of our deferred compensation plan assets that are held in a rabbi trust; and (iii) a \$0.5 million reduction in net other categories.

Interest expense

Interest Expense decreased to \$0.7 million for the nine months ended September 30, 2020 from \$1.0 million for the same period in 2019. The decrease was primarily due to a reduction in interest expense related to stock appreciations rights liability and notes payable to former stockholders, which were fully repaid during the second quarter of 2020.

Provision for income taxes

The provision for income taxes was \$7.9 million for the nine months ended September 30, 2020 compared to \$21.2 million in the same period in 2019, a decrease of \$13.3 million, or 62.8%, primarily due to the significant decline in income before provision for income taxes. The effective income tax rate for the nine months ended September 30, 2020 was 29.1% compared to 27.3% for the same period in 2019.

Non-GAAP Financial Measure

In this quarterly report on Form 10-Q, we include a non-GAAP financial measure, adjusted earnings before interest income/expense, taxes, depreciation and amortization, stock-based compensation and other non-cash items, or Adjusted EBITDA. We define Adjusted EBITDA as net income before (i) interest income and other, including net realized gains (losses) on marketable debt securities, available-for-sale and cash and cash equivalents, (ii) interest expense, (iii) provision for income taxes, (iv) depreciation and amortization, (v) stock-based compensation, and (vi) non-cash MSR activity. We use Adjusted EBITDA in our business operations to evaluate the performance of our business, develop budgets and measure our performance against those budgets, among other things. We also believe that analysts and investors use Adjusted EBITDA as a supplemental measure to evaluate our overall operating performance. However, Adjusted EBITDA has material limitations as an analytical tool and should not be considered in isolation, or as a substitute for analysis of our results as reported under U.S. GAAP. We find Adjusted EBITDA to be a useful tool to assist in evaluating performance, because Adjusted EBITDA eliminates items related to capital structure, taxes and non-cash items. In light of the foregoing limitations, we do not rely solely on Adjusted EBITDA as a performance measure and also consider our U.S. GAAP results. Adjusted EBITDA is not a measurement of our financial performance under U.S. GAAP and should not be considered as an alternative to net income, operating income or any other measures calculated in accordance with U.S. GAAP. Because Adjusted EBITDA is not calculated in the same manner by all companies, it may not be comparable to other similarly titled measures used by other companies.

A reconciliation of the most directly comparable U.S. GAAP financial measure, net income, to Adjusted EBITDA is as follows (in thousands):

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|-----------------|-------------------|-----------------|
| | September 30, | | September 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| Net income | \$ 6,040 | \$19,292 | \$19,216 | \$56,209 |
| Adjustments: | | | | |
| Interest income and other ⁽¹⁾ | (889) | (2,725) | (4,090) | (7,828) |
| Interest expense | 199 | 329 | 695 | 1,018 |
| Provision for income taxes | 1,916 | 7,024 | 7,875 | 21,159 |
| Depreciation and amortization | 2,606 | 1,910 | 7,822 | 5,674 |
| Stock-based compensation | 2,383 | 2,114 | 7,551 | 7,040 |
| Non-cash MSR activity ⁽²⁾ | (26) | (79) | (312) | (232) |
| Adjusted EBITDA ⁽³⁾ | <u>\$12,229</u> | <u>\$27,865</u> | <u>\$38,757</u> | <u>\$83,040</u> |

⁽¹⁾ Other includes net realized gains (losses) on marketable debt securities available-for-sale.

⁽²⁾ Non-cash MSR activity includes the assumption of servicing obligations.

⁽³⁾ The decrease in Adjusted EBITDA for the three and nine months ended September 30, 2020 compared to the same periods in 2019 is primarily due to a decrease in total revenues and a higher proportion of operating expenses compared to total revenues.

Liquidity and Capital Resources

Our primary sources of liquidity are cash and cash equivalents, cash flows from operations, marketable debt securities available-for-sale and, if necessary, borrowings under our credit agreement. In order to enhance yield to us, we have invested a portion of our cash in money market funds and fixed and variable income debt securities, in accordance with our investment policy approved by the board of directors. Certain of our investments in money market funds may not maintain a stable net asset value and may impose fees on redemptions and/or gating fees. To date, the Company has not experienced any restrictions or gating fees on its ability to redeem funds from money market funds. Although we have historically funded our operations through operating cash flows, there can be no assurance that we can continue to meet our cash requirements entirely through our operations, cash and cash equivalents, proceeds from the sale of marketable debt securities, available-for-sale or availability under our credit agreement.

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Cash Flows

Our total cash and cash equivalents balance decreased by \$59.6 million to \$173.1 million at September 30, 2020, compared to \$232.7 million at December 31, 2019. The following table sets forth our summary cash flows for the nine months ended September 30, 2020 and 2019 (in thousands):

| | Nine Months Ended September 30, | |
|---|------------------------------------|------------------|
| | 2020 | 2019 |
| Net cash used in operating activities | \$ (28,266) | \$ (6,053) |
| Net cash (used in) provided by investing activities | (21,381) | 21,079 |
| Net cash used in financing activities | (9,819) | (3,628) |
| Effect of currency exchange rate changes on cash and cash equivalents | (92) | — |
| Net (decrease) increase in cash and cash equivalents | (59,558) | 11,398 |
| Cash and cash equivalents at beginning of period | <u>232,670</u> | <u>214,683</u> |
| Cash and cash equivalents at end of period | <u>\$173,112</u> | <u>\$226,081</u> |

Operating Activities

Cash flows used in operating activities were \$28.3 million for the nine months ended September 30, 2020 compared to \$6.1 million for the same period in 2019. Net cash used in operating activities is driven by our net income adjusted for non-cash items and changes in operating assets and liabilities. The \$22.2 million increased usage in operating cash flows for the nine months ended September 30, 2020 compared to the same period in 2019 was primarily due to lower total revenues and a higher proportion of operating expenses compared to total revenues, differences in timing of certain payments and receipts, an increase in advances related to the acquisitions of teams, long-term retention of our investment sales and financing professionals and a reduction in deferral of certain discretionary commissions and commissions payable.

Investing Activities

Cash flows used in investing activities were \$21.4 million for the nine months ended September 30, 2020 compared to cash flows provided by investing activities of \$21.1 million for the same period in 2019. The \$42.5 million increase in cash flows used in investing activities for the nine months ended September 30, 2020 compared to the same period in 2019 was primarily due to a \$31.9 million reduction in net proceeds from sales and maturities of marketable debt securities and a net \$11.8 million outflow for acquisitions during the nine months ended September 30, 2020 with no such comparable outflow for the same period in 2019.

Financing Activities

Cash flows used in financing activities were \$9.8 million for the nine months ended September 30, 2020 compared to \$3.6 million for the same period in 2019. The change in cash flows used in financing activities for the nine months ended September 30, 2020 compared to the same period in 2019 was primarily impacted by principal payments on notes payable to former stockholders and payments related to stock appreciation rights liability, partially offset by lower taxes paid related to net share settlement of stock-based awards. See Note 12 – “Stock-Based Compensation Plans” of our Notes to Condensed Consolidated Financial Statements for additional information.

Liquidity

We believe that our existing balances of cash and cash equivalents, cash flows expected to be generated from our operations, proceeds from the sale of marketable debt securities, available-for-sale and borrowings available under the Credit Agreement (defined below) will be sufficient to satisfy our operating requirements for at least the next 12 months. As of September 30, 2020, cash on hand and core-cash investments aggregated \$342.8 million, and we had \$60.0 million of borrowing capacity under our credit agreement. In response to this period of business disruption, we assessed our cost structure and have instituted various expense reduction initiatives as discussed in “Overview – COVID-19” section above.

Credit Agreement

We have a Credit Agreement with Wells Fargo Bank, National Association for a \$60.0 million principal amount senior secured revolving credit facility that is guaranteed by all of our domestic subsidiaries and matures on June 1, 2022 (the “Credit Agreement”). See Note 15 – “Commitments and Contingencies” of our Notes to Condensed Consolidated Financial Statements for additional information on the Credit Agreement.

Contractual Obligations and Commitments

There have been no material changes in our commitments under contractual obligations, as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2019 through the date the condensed consolidated financial statements were issued other than (i) increases in contingent and deferred consideration in connection with acquisitions of \$5.2 million and (ii) increases in amounts that may be advanced to certain investment sales and financing professionals upon reaching time requirements of \$20.4 million.

Off Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

Inflation

Our commissions and other variable costs related to revenue are primarily affected by real estate market supply and demand, which may be affected by uncertain or changing economic and market conditions, including inflation/deflation arising in connection with and in response to the COVID-19 pandemic. The economic impacts from inflation/deflation to our business remain unknown at this time.

Critical Accounting Policies; Use of Estimates

We prepare our financial statements in accordance with U.S. GAAP. In applying many of these accounting principles, we make assumptions, estimates and/or judgments that affect the reported amounts of assets, liabilities, revenues and expenses in our condensed consolidated financial statements. We base our estimates and judgments on historical experience and other assumptions that we believe are reasonable under the circumstances. These assumptions, estimates and/or judgments, however, are often subjective and our actual results may change based on changing circumstances or changes in our analyses. If actual amounts are ultimately different from our estimates, the revisions are included in our results of operations for the period in which the actual amounts become known. There were no significant changes in our critical accounting policies, as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2019 except for the following:

Investments in Marketable Debt Securities, Available-for-Sale

We maintain a portfolio of investments in a variety of fixed and variable rate debt securities, including U.S. treasuries, U.S. government sponsored entities, corporate debt, asset-backed securities and other. We consider our investments in marketable debt securities to be available-for-sale, and accordingly are recorded at their fair values. We determine the appropriate classification of investments in marketable debt securities at the time of purchase. Interest along with accretion and amortization of purchase premiums and discounts from the purchase date through the estimated maturity date, including consideration of variable maturities and contractual call provisions, are included in other income (expense), net in the condensed consolidated statements of net and comprehensive income. We typically invest in highly-rated debt securities, and our investment policy generally limits the amount of credit exposure to any one issuer. The policy requires substantially all investments to be investment grade, with the primary objective of minimizing the potential risk of principal loss and matching long-term liabilities.

We review quarterly our investment portfolio of all securities in an unrealized loss position to determine if an impairment charge or credit reserve is required. We exclude accrued interest from both the fair value and the amortized cost basis of marketable debt securities, available-for-sale, for the purposes of identifying and measuring an impairment. An investment is impaired if the fair value is less than its amortized cost basis. Impairment relating to credit losses is recorded through a reduction in the amortized cost of the security or an allowance for credit losses and credit loss expense (included in selling, general and administrative expense), limited by the amount that the fair value is less than the amortized cost basis. Impairment that has not been recorded as a credit loss is recorded through other comprehensive income/loss, net of applicable taxes. We made an accounting policy election to not measure an allowance for credit losses for accrued interest receivables. We evaluate write-off of accrued interest receivable by the major security-type level at the time credit loss exists for the underlying security.

Determining whether a credit loss exists requires a high degree of judgment and we consider both qualitative and quantitative factors in making our determination. We evaluate our intent to sell, or whether we will more likely than not be required to sell, the security before recovery of its amortized cost basis. For all securities in an unrealized loss position, we evaluate, among other items, the extent and length of time the fair market value of a security is less than its amortized cost, time to maturity, duration, seniority, the financial condition of the issuer including credit ratings, any changes thereto and relative default rates, leverage ratios, availability of liquidity to make principle and interest payments, performance indicators of the underlying assets, analyst reports and recommendations and changes in base and market interest rates. If qualitative and quantitative analysis is sufficient to conclude that an impairment related to credit losses does not exist, we typically do not perform further quantitative analysis to estimate the present value of cash flows expected to be collected from the debt security. Estimates of expected future cash flows are our best estimate based on past events, current conditions and reasonable and supportable economic forecasts.

Recent Accounting Pronouncements

For information regarding recent accounting pronouncements, see Note 2 – “Accounting Policies and Recent Accounting Pronouncements” of our Notes to Condensed Consolidated Financial Statements. Other than changing certain accounting processes and disclosures, the accounting pronouncement related to Accounting Standards Update No. 2016-13, *Financial Instruments - Credit Losses* did not have a material impact on our condensed consolidated financial statements. Although we do not believe any of the other accounting pronouncements listed in that note will have a significant impact on our business, we are still in the process of determining the impact of the new pronouncements may have on our condensed consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We maintain a portfolio of investments in a variety of fixed and variable debt rate securities, including U.S. government and federal agency, corporate debt, asset-backed securities and other. As of September 30, 2020, the fair value of investments in marketable debt securities, available-for-sale was \$216.0 million. The primary objective of our investment activity is to maintain the safety of principal, and to provide for future liquidity requirements while maximizing yields without significantly increasing risk. While some investments may be securities of companies in foreign countries, all investments are denominated and payable in U.S. Dollars. We do not enter into investments for trading or speculative purposes. While our intent is not to sell these investment securities prior to their stated maturities, we may choose to sell any of the securities for strategic reasons including, but not limited to, anticipated capital requirements, anticipation of credit deterioration, duration management and because a security no longer meets the criteria of our investment policy. We do not use derivatives or similar instruments to manage our interest rate risk. We seek to invest in high quality investments. The weighted average rating (exclusive of cash and cash equivalents) was AA as of September 30, 2020. Maturities are maintained consistent with our short-, medium- and long-term liquidity objectives.

Currently, our portfolio of investments predominantly consists of fixed interest rate debt securities; however, a portion of our investment portfolio may consist of variable interest rate debt securities. Our investments in fixed interest rate debt securities are subject to various market risks. Changes in prevailing interest rates may adversely or positively impact their fair market value should interest rates generally rise or fall. Accordingly, we also may have interest rate risk with variable interest rate debt securities as the income produced may decrease if interest rates fall. Contraction in market liquidity may adversely affect the value of portions of our portfolio and affect our ability to sell securities in the time frames required and at acceptable prices. Uncertainty in future market conditions may raise market participant’s expectations of returns, thus impacting the value of securities in our portfolio as well. During the nine months ended September 30, 2020, increased demand for treasury securities caused a significant decrease in the yields on treasury securities and unbalanced demand and supply factors created significant liquidity shortfalls until the Federal Reserve initiated market intervention programs to stabilize the market. The following table sets forth the impact on the fair value of our investments as of September 30, 2020 from changes in interest rates based on the weighted average duration of the debt securities in our portfolio (in thousands):

| Change in Interest Rates | Approximate Change in Fair Value of Investments | |
|--------------------------|---|---------|
| | Increase (Decrease) | |
| 2% Decrease | \$ | 2,224 |
| 1% Decrease | \$ | 1,528 |
| 1% Increase | \$ | (2,383) |
| 2% Increase | \$ | (4,765) |

Due to the nature of our business and the manner in which we conduct our operations, we believe we do not face any material interest rate risk with respect to other assets and liabilities, equity price risk or other market risks. The functional currency of our Canadian operations is the Canadian dollar. We are exposed to foreign currency exchange rate risk for the settlement of transactions of the Canadian operations as well as unrealized translation adjustments. To date, realized foreign currency exchange rate gains and losses have not been material.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f), including maintenance of (i) records that in reasonable detail accurately and fairly reflect the transactions and dispositions of our assets, and (ii) policies and procedures that provide reasonable assurance that (a) transactions are recorded as necessary to permit preparation of financial statements in accordance with accounting principles generally accepted in the United States of America, (b) our receipts and expenditures are being made only in accordance with authorizations of management and our board of directors and (c) we will prevent or timely detect unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

Our management, with the supervision and participation of our chief executive officer (“CEO”) and chief financial officer (“CFO”), has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of the end of the period covered by this Form 10-Q, based on the criteria established under the Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) (2013 framework). Based on such evaluation, our management has concluded that as of September 30, 2020, our disclosure controls and procedures are designed at a reasonable assurance level and are effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the SEC, and that such information is accumulated and communicated to our management, including our CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There have not been any changes 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 quarter ended September 30, 2020 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. We have not experienced any significant impact to our internal controls over financial reporting despite the fact that most of our employees and independent contractors are working remotely due to the COVID-19 pandemic. The design of our processes and controls allow for remote execution with accessibility to secure data. We are continually monitoring and assessing the COVID-19 situation to minimize the impact, if any, on the design and operating effectiveness on our internal controls.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are involved in claims and legal actions arising in the ordinary course of our business, some of which involve claims for damages that are substantial in amount. Most of these litigation matters are covered by our insurance policies, which contain deductibles, exclusions, claim limits and aggregate policy limits. Such litigation and other proceedings may include, but are not limited to, actions relating to commercial relationships, standard brokerage disputes like the alleged failure to disclose physical or environmental defects or property expenses or contracts, the alleged inadequate disclosure of matters relating to the transaction like the relationships among the parties to the transaction, potential claims or losses pertaining to the asset, vicarious liability based upon conduct of individuals or entities outside of our control, general fraud claims, conflicts of interest claims, employment law claims, including claims challenging the classification of our sales professionals as independent contractors, claims alleging violations of state consumer fraud statutes and intellectual property. While the ultimate liability for these legal proceedings cannot be determined, we review the need for an accrual for loss contingencies quarterly and record an accrual for litigation related losses where the likelihood of loss is both probable and estimable. We do not believe, based on information currently available to us, that the final outcome of these proceedings will have a material adverse effect on our consolidated financial position, results of operations or cash flows.

Item 1A. Risk Factors

There have been no material changes from the risk factors described in our Annual Report on Form 10-K for the year ended December 31, 2019, other than the new risk factor below relating to the COVID-19 pandemic.

The COVID-19 pandemic has adversely affected and could continue to adversely affect how we operate our business, and the duration and extent to which it will impact our future results of operations and overall financial performance is unknown.

The COVID-19 pandemic is a prolonged widespread global health crisis that has adversely affected and could continue to adversely affect the broader economies, capital markets and overall demand for our services.

Government imposed restrictions, including social distancing and other prevention measures, intended to slow the community spread of COVID-19 have, and will likely continue to affect our clients or potential clients' ability or willingness to purchase properties with limited or no ability to view properties; delay the closing of real estate sales and financing transactions; increase the borrowing cost and reduce the availability of debt financing; impact our ability to provide or deliver services to our clients or potential clients; and/or temporarily delay our expansion efforts. In addition, the current COVID-19 pandemic, the reoccurrence of the COVID-19 pandemic or a future pandemic and the resumption of or any new state or local shelter-in-place orders, could materially affect our future sales, operating results, liquidity and overall financial performance due to, among other factors:

- Any impairment in value of our investments in marketable debt securities, available-for-sale, tangible or intangible assets, which could be recorded as a result of weaker economic conditions.
- A potential negative impact on the health of our employees and investment sales and financing professionals, particularly if a significant number of them are impacted, could result in a deterioration in our ability to ensure business continuity during a disruption.
- If significant portions of our workforce are unable to work effectively, including because of quarantines, facility closures, ineffective remote work arrangements or technology failures or limitations, our operations would be adversely impacted.
- If we need to raise additional capital through public or private debt or equity financings, strategic relationships or other arrangements, this capital might not be available to us in a timely manner, on acceptable terms, or at all due to various risks and uncertainties. Our failure to raise sufficient capital when needed could prevent us from, among other factors, to fund acquisitions or to otherwise finance our growth or operations. If we are not able to respond to and manage the impact of such events effectively, our business will be harmed.

The long-term potential economic impact of a pandemic may be difficult to assess or predict. The COVID-19 pandemic has resulted in significant disruption of global financial markets, and on June 8, 2020, the National Bureau of Economic Research announced that the United States was in a recession. A long-term recession or long-term market correction could have a long-term impact on the flow of capital to the commercial real estate market and/or the willingness of investors to invest in or sell commercial real estate. This may adversely impact the demand for our services as well as the value of our common stock and our access to capital.

While we did not incur significant disruptions during the three months ended March 31, 2020 from the COVID-19 pandemic, our business was materially adversely impacted during the three months ended June 30, 2020. During the three months ended June 30, 2020, we saw a significant increase in closing timelines, a dramatic slowing of our real estate brokerage and financing transaction activity, difficulty in pricing assets and, in certain cases, restricted ability of borrowers to access the capital markets and other sources of financing. During the three months ended September 30, 2020, we have seen some improvement in transaction activity and availability of capital. However, the effect of the government imposed restrictions, including social distancing and other prevention measures related to COVID-19 as mandated by federal, state and local governments, continues to restrict our operations and will likely continue to affect our ability to identify and close commercial real estate transactions.

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Please see “Management’s Discussion and Analysis of Financial Position and Results of Operations” for a more detailed discussions of the potential impact of the COVID-19 pandemic and associated economic disruptions.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not Applicable.

Item 5. Other Information

None.

Item 6. Exhibits

| <u>Exhibit No.</u> | <u>Description</u> |
|--------------------|---|
| 10.1*+ | Employment Agreement between the Company and Steven F. DeGennaro effective as of August 4, 2020 |
| 31.1* | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) under the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2* | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) under the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1** | Certifications of Chief Executive Officer and Chief Financial Officer pursuant to Rule 13a-14(b) under the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101* | The following financial statements from the Company’s Quarterly Report on Form 10-Q for the quarter ended September 30, 2020, formatted in Inline XBRL: (i) Condensed Consolidated Balance Sheets, (ii) Condensed Consolidated Statements of Net and Comprehensive Income, (iii) Condensed Consolidated Statements of Stockholders’ Equity, (iv) Condensed Consolidated Statements of Cash Flows, and (v) Notes to Condensed Consolidated Financial Statements, tagged as blocks of text and including detailed tags. |
| 104* | Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101) |

* Filed herewith.

** Furnished, not filed.

+ Indicates management contract or compensatory plan.

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.

Marcus & Millichap, Inc.

Date: November 9, 2020 By: /s/ Hessam Nadji
Hessam Nadji
President and Chief Executive Officer
(Principal Executive Officer)

Date: November 9, 2020 By: /s/ Steven F. DeGennaro
Steven F. DeGennaro
Chief Financial Officer
(Principal Financial Officer)

EMPLOYMENT AGREEMENT

This Agreement is made effective the 4th day of August, 2020 (“Effective Date”) by and between Marcus & Millichap, Inc. (the “Company”) and Steven F. DeGennaro (“Employee”) with respect to the following:

- A. The Parties desire to enter into an at-will Employment Agreement whereby the Employee will serve in the capacity of Executive Vice President and Chief Financial Officer, based in the Company’s Headquarters, which is currently located in Calabasas, CA.
- B. The Parties agree that Employee’s employment shall be governed by the terms set forth herein, including the arbitration provision, the Employee Manual, and the Company’s policies and procedures.

THEREFORE, the Parties agree as follows:

1. **Term of At-Will Employment.** This Agreement shall be in effect commencing on August 4, 2020. The Company and Employee hereby agree that Employee’s employment with the Company is at-will. Either party may terminate this Agreement with or without cause. Such termination shall not prejudice any remedy which either party may have against the other at law, in equity, or under this Agreement.
2. **Designation and Duties.** Commencing on August 17, 2020, Employee shall have the title of Executive Vice President and Chief Financial Officer. Subject to the control and direction of the Chief Executive Officer and/or the Board of Directors (or one of its Committees), Employee shall serve as an officer of the Company, and shall be responsible for oversight of the Company’s financial and accounting departments and activities, and other responsibilities as from time-to-time may be assigned by the Chief Executive Officer. Employee is not guaranteed, has not been promised, and has no expectation of any promotion or any other position with the Company other than the one stated in this Agreement. Employee shall serve the Company diligently and according to Employee’s best abilities in all respects, and generally do all things for the best interest of the Company as are usually done by persons occupying similar positions in similar businesses.
3. **Manner of Performance.** Employee shall at all times faithfully, industriously, and to the best of Employee’s ability, experience, and talent, perform all duties that may be required of and from Employee, pursuant to the express and implicit terms hereof, to the reasonable satisfaction of the Company. Such duties shall be rendered at the above-mentioned premises and at such other place or places as the Company shall require or as the interests, needs, business, and opportunities of the Company shall require or make advisable. Employee acknowledges that Employee has received and has read a copy of the Company’s Employee Policy Manual and Code of Ethics and agrees to abide by all terms and conditions, including all future amendments or modifications thereto. The Company reserves the right to amend and revise its policies at any time and from time to time. The Company will notify Employee of all such material changes. Employee agrees to read, comply with, and be bound by all such amendments, revisions and/or modifications.

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4. **Compensation and Fringe Benefits.** The compensation and fringe benefits to be received by Employee in consideration of the services to be rendered by Employee are set forth in Exhibit "A" attached hereto. The provisions of Exhibit "A" are incorporated into this Agreement by reference as if fully set forth herein. The Company reserves the right to cancel or change the employee benefit plans and programs it offers to employees.
 5. **Effect of Termination on Compensation.** Employee shall be entitled to the base salary earned by Employee prior to the date of termination, computed pro rata up to the date of termination. Employee shall not be entitled to any further salary or other compensation after the date of termination. Except as expressly modified in Exhibit A, on termination of this Agreement, Employee shall not be deemed to have earned any incentive compensation not already declared and paid by the Company because such compensation is not for services rendered and employment on the date of payment is an express requirement to be deemed to have earned any such compensation. Unless otherwise agreed-to in writing, Employee shall be obligated to return to the Company within ten (10) days after the termination of Employee's employment any draws or other advance payments (of incentive compensation or otherwise) made to him during the annual period in which such termination occurs. Unless otherwise agreed-to in writing, interest shall accrue on the sum of any such advances at the rate of ten percent (10%) per annum after said ten-day period.
 6. **Business Expenses.** The Company will promptly reimburse Employee for reasonable business expenses incurred by Employee in promoting the business of the Company, including expenditures for entertainment, gifts and travel, provided that: (i) Each such expenditure is of a nature qualifying it as a proper deduction on the Federal and State income tax returns of the Company; and (ii) Employee furnishes to the Company, in accordance with the Company's established policy, adequate records and other documentary evidence required by Federal and State statutes and regulations issued by the appropriate taxing authorities for the substantiation of such expenditures as income tax deductions.
 7. **Non-Solicitation and Confidential Information.**
 - (i) During the term of this Agreement, Employee shall not directly or indirectly, either as an employee, employer, consultant, agent, principal, owner, partner, stockholder, corporate officer, director, or in any other individual or representative capacity, engage or participate in any business that is in competition in any manner whatsoever with the business of the Company or the Company's affiliates, assigns or successors.
 - (ii) Employee acknowledges that the Company has devoted substantial resources to develop proprietary computer systems and software, and to obtain and organize information to be utilized by its agents in connection with their business activities on behalf of the Company and its clients. Employee is eligible to utilize, subject to the terms and conditions set forth in this Agreement, certain computer systems, software and data developed by or on behalf of the Company. Employee agrees that unauthorized use or disclosure of such systems, software or data would cause irreparable damage to the Company, and would lessen the value of the services it provides to its agents and clients.

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- (iii) Employee acknowledges that he serves in a position of trust with the Company and its affiliates and that he owes a fiduciary duty of loyalty to the Company and its affiliates, and that as a result of that position, that Company has entrusted Employee with Confidential Information. Employee understands and agrees that during Employee's employment Employee is provided with valuable "Confidential Information" regarding: (i) the business, present or future, of the Company; (ii) research, inventions, products and services of the Company and its affiliates; (iii) clients, Employees, and Salespersons of the Company and its affiliates; and (iv) operations, skills, and capabilities of the Company and its affiliates and its employees and Salespersons. Such "Confidential Information" includes, but is not limited to: (a) earnings, finances, projections, business plans, strategies, techniques, deployment, and business models, and business-related data relating to the Company and its affiliates and its clients, Employees and Salespersons; (b) manuals, research, data, reports or other information as stored on, input to or downloaded from the Company's software, system or network; (c) business processes, strategies, and endeavors, business plans and models, customer and Salesperson lists and procuring and retention methodology, and all proprietary information regarding the operations of the Company and its affiliates and its departments; (d) client strategies, listings, past/present/future transactions and information related thereto, non-public client contact, ownership, transactional history, or financial information; and (e) salesperson or employee strategies, listings, past/present/future transactions and information related thereto, transactional history, and contact, ownership, and financial information.
- (iv) For the purpose of protecting legitimate business interests of the Company, including Confidential Information and trade secrets, Employee agrees that, during the term of Employee's employment with the Company or with any of its affiliates, and for a **two (2) year period** thereafter, Employee will not (a) induce, convince, recruit, cause, or solicit any employees, contractors, or sales personnel of the Company or its affiliates to terminate his/her employment with the Company; or (b) induce, recruit, converse with, convince, cause, or solicit any employees, contractors, or sales personnel of the Company or its affiliates to terminate his/her employment with the Company to join Employee in a business operation or venture competitive to the business of the Company or its affiliates. For the purpose of this Agreement, the affiliates of the Company consist of the Company and all entities which are subsidiaries or related parties of M&M and/or the Company, or its assigns, or successors of M&M and/or the Company. This prohibition shall include, but not be limited to, activity done personally, directly, or indirectly by Employee, or through agents or employees acting on behalf of Employee, or for Employee's direct or indirect benefit. It shall not be a violation of this paragraph to hire an individual who was not induced, convinced, or otherwise solicited in violation of this paragraph.

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- (v) Both during and after Employee's association with the Company, Employee shall not disclose to anyone, or use in any manner (except as such disclosure or use is specifically authorized by the Company) any Confidential Information. Employee shall not during the term of this Agreement or at any time thereafter use to Employee's own advantage, or the advantage of any other person, firm or entity, any information gained from the files or business of the Company or its affiliates, including, but not necessarily limited to, information training materials, the IC Policy Manual, Employee Manual, customer lists, computer operations, financial and business information, and any other confidential aspects of the Company's operations or of its affiliates. All such information shall be treated by Employee in a confidential manner. Nothing in this Agreement shall prohibit the disclosure of information as required by law.
- (vi) If Employee leaves the Company's employment, Employee shall promptly return to the Company all manuals, disks, programs, documents, papers and other materials in Employee's possession or under Employee's control that may contain or be derived from Confidential Information, regardless of the medium in which they are contained; and Employee shall retain no copies of any of the foregoing.
- (vii) Employee agrees that the restrictive covenants set forth herein are separate and independent agreements, are reasonable and are necessary to protect the Company's legitimate business interests given Employee's high level and confidential access to such proprietary information and interests. Because of the unique nature of the Confidential Information and other proprietary information described herein, Employee understands and agrees that the Company will suffer irreparable harm if Employee fails to comply with the obligations contained herein, and that monetary damages will be inadequate to compensate the Company for said breach. Accordingly, Employee agrees that the Company will, in addition to any other remedies available to it at law or in equity, be entitled to injunctive relief to enforce the terms of this Agreement.
8. **Employee's Representations**. Employee shall never use any Confidential Information belonging to any of the Employee's former employers in the course of Employee's duties for the Company.
9. **Ownership of Records**. All documents and other materials relating to the Company's or its affiliates' accounts, customers, real estate listings, employees, sales personnel, computer programs, investments, finances, strategies and business plans, financial statements, training programs or any other type of Confidential Information, and all copies thereof, whether prepared by Employee or otherwise coming into Employee's possession, are the exclusive property of the Company. All such documents shall be immediately returned by Employee to the Company upon termination of Employee's employment.

10. **Mutual Arbitration Agreement**

- (i) Employee and the Company (which is inclusive of all parent, related, and subsidiary entities) agree that all past, present, or future disputes or claims arising from or relating to this Agreement or Employee's affiliation with the Company, including disputes or claims relating to any contract between the Company and Employee, shall be decided exclusively through mutual, binding arbitration before a single arbitrator of the American Arbitration Association ("AAA") in accordance with its commercial rules and procedures ("Rules"), except where modified herein. AAA's Expedited Procedures shall not apply. A copy of the Rules may be found on AAA's website at www.adr.org, and shall be provided by the Company upon request.
- (ii) The Parties understand and agree that all claims, disputes, or controversies between Employee and the Company (including owners, directors, managers, employees, parent or subsidiary entities) shall be resolved exclusively through binding arbitration in conformance with the Federal Arbitration Act ("FAA") and the procedures of any applicable State arbitration act. The Parties agree their relationship and work relates to and substantially affects interstate commerce, and that the FAA governs the enforcement and interpretation of this arbitration provision.
- (iii) The Agreement applies to all claims arising from or relating in any fashion to Employee's affiliation with the Company, including claims asserted under statute, equitable law, common law, regulations, ordinances, tort or contract law, or any other basis, and includes, but is not limited to, claims for breach of contract, unpaid commissions, unfair business practices, discrimination, harassment, retaliation, unpaid wages, unpaid benefits, failure to reimburse business expenses, wage statement violations, misclassification, wrongful discharge, defamation, misrepresentation, fraud, assault/battery, and infliction of emotional distress, as well as any claims under the California Labor Code and the California Fair Employment and Housing Act. This Agreement excludes claims arising under the National Labor Relations Act that are brought before the National Labor Relations Board, State medical and disability benefits, State workers compensation benefits, State unemployment benefits, claims under California's Private Attorney General Act (Cal. Labor Code § 2698, et seq. ("PAGA")) and any other claim excluded from arbitration under State or Federal law.

- (iv) The Parties understand and agree that they hereby waive their rights to a jury trial on any covered claim. The Parties further understand and agree that they may bring claims on behalf of themselves, and themselves only. The Parties hereby waive the right to bring, or otherwise participate in any fashion in, a claim or action on a class, collective or representative basis to the fullest extent allowed by law. The Parties understand and agree that this Agreement shall not be construed to allow or permit, and the arbitrator shall have no authority to allow or permit, the consolidation or joinder of other claims or controversies involving other individuals, or to order any action to proceed on a class, collective, or representative basis. Notwithstanding the foregoing, if a court or arbitrator determines a certain matter may proceed by law as a class, representative, or collective action, that action shall proceed in court only, and shall be stayed until the final disposition of all arbitrable claims.
- (v) The arbitrator shall have the authority to make orders regarding discovery, including depositions, written discovery, and document production, consistent with State law and as necessary for fair disposition of claims. The arbitrator shall apply all rules of evidence that would apply to an action brought in a State court. The arbitrator shall hear and issue written rulings on all dispositive motions, including, but not limited to demurrers, motions for summary judgment or adjudication, or motions for terminating sanctions. The arbitrator shall extend times for notices or hearings as required for the Parties full use and benefit of this Agreement. The arbitrator may award any type of relief that would otherwise be available in court. Issues of arbitrability shall be determined in conformity with the FAA. On all other issues of substantive law, the arbitrator shall apply the law that would apply to the claims and defenses if they were brought in court, and shall issue a written, reasoned opinion/award. The Company shall pay all costs unique to arbitration that Employee would not otherwise be required to pay if the matter were litigated in court, including the cost of the arbitrator.
- (vi) The arbitration shall occur in the county where the Company's office from which Employee is or was based is located. This is the entire agreement regarding the resolution of disputes. It supersedes any and all other agreements, either oral or in writing, between the parties hereto with respect to arbitration or the resolution of disputes or claims. Any modification to this Agreement will be effective only if it is in writing signed by the party to be charged. The Parties intend that this Agreement be enforced to the fullest extent allowed by law, and the Parties therefore agree the Court or arbitrator should construe it in a manner that renders it enforceable.

By initialing below, the Parties acknowledge that they have read, considered, and understand the foregoing arbitration agreement, and agree to be bound by it.

Initials:



Company



Employee

- 11. **Notices.** Any notices to be given hereunder by either party to the other may be effected either by personal delivery in writing or by certified mail. Mailed notices shall be addressed to the parties at the addresses appearing just under their signature on the execution page of this Agreement, but each party may change their address by giving written notice thereof to the other party.

12. **Entire Agreement.** This Agreement supersedes any and all other agreements, either oral or in writing, between the parties hereto with respect to the employment of Employee by the Company, and contains all of the covenants and agreements between the parties with respect to such employment in any manner whatsoever. Any modification of this Agreement will be effective only if it is in writing signed by all parties. This Agreement does not however modify the terms of the equity agreements provided under the Company's Omnibus Equity Incentive Plan.
13. **Partial Invalidity.** The Parties intend that this Agreement be interpreted to render it enforceable. If any part of this Agreement is held by a court of competent jurisdiction to be invalid, void, or unenforceable, it shall be severed or where possible modified by the court or arbitrator and the remaining provisions shall nevertheless continue in full force without being impaired or invalidated in any way.
14. **Attorneys' Fees.** Where not disallowed by state laws, in the event litigation is instituted by either party concerning any aspect of this Agreement, the prevailing party shall be entitled to receive from the other party all costs and reasonable attorneys' fees in addition to any other appropriate relief in accordance with state law.
15. **Additional Terms.** Electronic, or electronically transmitted, signatures shall be deemed to be originals. The Parties have been advised to seek counsel regarding the terms of this Agreement, and having had that opportunity now knowingly and voluntarily wish to enter into it. Both parties have participated in the negotiation and drafting of this Agreement, such that it will not be construed more strictly against the drafting party.
16. **Applicable Law.** This Agreement shall be construed in accordance with and governed by the laws of the State of California. As used herein, "State" refers to California.

IN WITNESS WHEREOF, the Parties understand and agree to the foregoing terms.

EMPLOYEE

MARCUS & MILLICHAP, INC.



STEVEN F. DEGENNARO

Date: 8/4/20



By:

HESSAM NADJI
President / CEO
23975 Park Sorrento, Suite 400
Calabasas, CA 91302

Date: 8/4/20

EMPLOYMENT AGREEMENT

EXHIBIT A

This document is Exhibit A of the Employment Agreement (hereinafter called the “Agreement”) between Marcus & Millichap, Inc. (the “Company”) and Steven F. DeGennaro (“Employee”). The provisions hereof are an integral part of said Agreement and are fully incorporated into the Agreement.

Compensation and Fringe Benefits of Employee.

The compensation and fringe benefits to be paid to Employee are as follows:

1. **Compensation and Special Conditions.**

- i. **Salary.** Employee shall be entitled to receive from the Company a base monthly salary of \$33,333.33, payable in semi-monthly installments, prorated for less than a full year of service. This amount will be reduced by twenty percent (20%) until written further notice by the President as part of the Company’s COVID-19-related cost reduction measures. In the event employment is terminated, the base salary amount will be paid on a pro-rata basis up to the date of termination in accordance with state law, with no salary due or earned after the date of termination.
- ii. **Signing Advance Bonus:** Employee will be provided a signing bonus of two hundred and fifty thousand dollars (\$250,000), less all required payroll withholdings and applicable deductions (“Signing Advance Bonus”). The Signing Advance Bonus will be paid as an advance in February 2021 so long as Employee remains employed in good standing with the Company on such date. It will be deemed earned on, and not before, the end of the service period ending December 31, 2022 (“Advance Earning Date”) if Employee is employed in good standing on the Advance Earning Date. In the event Employee voluntarily departs without “Good Reason” (as defined below) or is terminated for “Cause” (as defined below) prior to the Advance Earning Date, the Signing Advance Bonus is subject to claw-back and must be immediately repaid by Employee to the Company in its entirety.
 - a. For purposes of the Agreement, “Good Reason” shall be defined as: (i) material reduction in position or compensation without Cause; or (ii) relocation is required to an office location in excess of fifty (50) miles from the Company’s current Headquarters.

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- b. For purposes of the Agreement, "Cause" shall be defined as: (i) material violation of Company's policies or the Agreement following notice and thirty (30) days opportunity to cure where such breach is capable of cure; (ii) material violation of Company's policies or this Agreement where such breach is not capable of cure; (iii) failure to perform Employees' duties in a manner equal to or exceeding that which is reasonable and customary for individuals holding the same or similar title for public companies in the United States; (iv) failure to comply with the reasonable requests and directives of Employee's supervisor; (v) commission of, plea of guilt or no-contest to, or conviction for any felony or crime of moral turpitude; (vi) commission of fraud; (vii) commission of any conduct for which punitive damages are awarded; or (viii) commission of any act which materially and negatively affects the Company's brand, reputation, standing, or licensure.
- iii. **Bonus Potential:** Employee will be eligible to receive an annual discretionary incentive bonus targeted at six hundred thousand dollars (\$600,000) per calendar year starting for 2021 (with eligible bonus paid by the end of February 2022) and continuing annually thereafter. This bonus will be 50% based on Company financial and non-financial performance against goals, and 50% based on personal goals that will be set with Employee's input. It will be determined based on Employee's performance review with the Chief Executive Officer and paid, if appropriate, in February after the Compensation Committee meeting and approval process. If in any given year, the Company does not meet a minimum of 50% of its pre-tax income goal, no bonuses will be paid to executives for that year, unless special considerations are determined by the Compensation Committee.
- iv. **Restricted Stock Units:** Subject to approval by the Compensation Committee, as a senior leader of the Company, as set forth below contingent upon Employee's continued employment and good standing, Employee will be eligible for long term incentive compensation in the form of restricted stock units ("RSUs"). All RSUs require the approval of the Compensation Committee and shall be governed by the Company's Omnibus Equity Incentive Plan Restricted Stock Unit Award Agreement, except as modified and approved by the Compensation Committee.
- a. **Initial RSU Awards:** Subject to approval of the Compensation Committee, Employee will receive a grant of seventy five hundred (7,500) RSUs with a 5-year vesting schedule in August 2020 and an additional seventy five hundred (7,500) RSUs with 5-year vesting in August 2021 if Employee is in good standing with the Company.
- b. **LTP1 and LTP2 RSU Grant:** Subject to approval of the Compensation Committee, and Employee being in good standing, beginning with any discretionary cash bonus paid in 2022, Employee will be eligible in the Company's discretion to receive an RSU grant potential equivalent of up to fifty percent (50%) of Employee's actual discretionary cash bonus earned and paid each year. Twenty-five percent (25%) will be based on the year's overall results including the Company's performance and Employee's individual performance ("LTP1"). Twenty-five percent (25%) will be based on progress toward achieving the Company's long-term goals and Employee's contribution toward them ("LTP2"). Beginning in 2022, these RSU grants will be part of the annual review process, with amounts determined by the Company, in its discretion, in February based on the prior calendar year. The RSU grants will be subject to a 5-year vesting schedule. There is no LTP1 or LTP2 eligibility based on 2020.

v. **Severance Program:**

- a. Change of Control. In the event of a Change of Control as defined below, and as a result of such Change of Control and within one year of such event the Company terminates Employee's employment or Employee resigns for Good Reason, then: (a) the Company will provide Employee a severance payment equal to six (6) months of base salary and one-half (1/2) the amount of Employee's last annual cash discretionary bonus ("Severance Payment"); and (b) Employee will receive accelerated vesting of any unvested RSUs or other awarded unvested equity. If a Change of Control occurs in 2021, Employee will receive \$200,000 in base salary (one half of one year) and \$300,000 in bonus (one half of target bonus). For purposes of this Agreement, "Change in Control" shall be defined as the sale or merger of the Company wherein the other transacting entity to such sale or merger takes a controlling ownership interest in the Company.
- b. Termination Without Cause or Departure for Good Reason. In the event the Company terminates Employee's employment without Cause or Employee terminates Employee's employment for Good Reason, then the Company will provide Employee a severance payment equal to six (6) months of base salary and one-half (1/2) the amount of Employee's last annual cash discretionary bonus ("Severance Payment").
- c. Paragraphs 1(v)(a) and 1(v)(b) are collectively referred to herein as the "Severance Program." The Severance Program is only applicable to the circumstances expressly stated herein and Employee, when and if eligible, will receive the Severance Payment under either Paragraph 1(v)(a) or 1(v)(b), as applicable, not under both paragraphs. Amounts provided for in the Severance Payments are not compensation or otherwise earned in any respect until actually paid. There is no eligibility for or expectation of the Severance Program or any other severance benefits for any other circumstance, including, but not limited to, voluntary termination of employment by Employee, termination not triggered by a Change of Control, termination for Cause by the Company, or termination by Employee without Good Reason. Unless otherwise determined by the Company in its sole discretion, all Severance Payments made under the Severance Program shall be paid at such times and in such manner (including the withholding of required payroll withholdings and applicable deductions) as the amounts would have otherwise been paid to the Employee had Employee remained employed. Notwithstanding any term to the contrary, eligibility for and receipt of all Severance Payments and advanced RSU vesting is also expressly conditioned upon: (1) Employee's compliance with all post-termination obligations under the Agreement, including but not limited to those in Paragraph 7, and no Severance Payment of any kind shall be due or payable in the event Employee fails to comply with such obligations; and (2) Employee's execution of a severance agreement consistent with Employee's obligations under this Agreement and which shall be inclusive of a general release by Employee.

2. **Performance-Based Compensation Clawback.** Employee acknowledges and agrees that the Company will be entitled, pursuant to any policy it adopts to comply with the clawback rules implemented by the Securities and Exchange Commission and/or our exchange listing standards, to recover from Employee, regardless of fault, that portion of performance-based compensation which was based on financial information required to be reported under securities laws that would not have been paid in the three completed fiscal years preceding the year(s) in which an accounting restatement is required to be filed to correct a material error. Subject to applicable law, the Compensation Committee may seek to recoup such performance-based compensation by requiring Employee to repay such amount to the Company; by set-off; by reducing future compensation; or by such other means or combination of means as the Compensation Committee, in its sole discretion, determines to be appropriate.
3. **Cellular Phone Allowance.** Employee shall be entitled to a monthly cellular phone allowance in the amount of one hundred dollars (\$100.00), reimbursed through regular and timely Expense Report submittal.
4. **Insurance and Retirement.** Employee shall be entitled to participate in insurance packages (medical, dental, and life) in accordance with the terms of Company Insurance Plan(s) available to eligible Company employees. Additionally, Employee shall be entitled to participate in a retirement savings plan in accordance with the terms of Company 401(K) Plan(s) available to eligible Company employees.
5. **Paid Time Off (PTO):** Upon employment, Employee will begin accruing paid time off equal to 15 days (120 hours) per anniversary year. Any unused PTO will carry over from year to year, to the maximum limits of the Company's policy.

EMPLOYEE

MARCUS & MILLICHAP, INC



STEVEN F. DEGENNARO

Date: 8/4/20



By:

HESSAM NADJI
President / CEO
23975 Park Sorrento, Suite 400
Calabasas, CA 91302

Date: 8/4/20

**Certification of Chief Executive Officer of Marcus & Millichap, Inc. pursuant to
Rule 13a-14(a) under the Exchange Act,
as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Hessam Nadji, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Marcus & Millichap, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2020

/s/ Hessam Nadji
Hessam Nadji
President and Chief Executive Officer

**Certification of Chief Financial Officer of Marcus & Millichap, Inc. pursuant to
Rule 13a-14(a) under the Exchange Act,
as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002**

I, Steven F. DeGennaro, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Marcus & Millichap, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2020

/s/ Steven F. DeGennaro

Steven F. DeGennaro
Chief Financial Officer

**Certifications of Chief Executive Officer and Chief Financial Officer of Marcus & Millichap, Inc. Pursuant to
Rule 13a-14(b) under the Exchange Act and 18 U.S.C. Section 1350, as Adopted Pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002**

In connection with the quarterly report of Marcus & Millichap, Inc. on Form 10-Q for the period ended September 30, 2020 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), we, Hessam Nadji, President and Chief Executive Officer of the Company, and Steven F. DeGennaro, Chief Financial Officer of the Company, certify, to the best of our knowledge, pursuant to Rule 13a-14(b) under the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 9, 2020

/s/ Hessam Nadji
Hessam Nadji
President and Chief Executive Officer
(Principal Executive Officer)

Date: November 9, 2020

/s/ Steven F. DeGennaro
Steven F. DeGennaro
Chief Financial Officer
(Principal Financial Officer)