WEST BANCORPORATION INC
Form 10-Q
April 28, 2016

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

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2016

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from __________ to __________

Commission File Number: 0-49677

WEST BANCORPORATION, INC.
(Exact Name of Registrant as Specified in its Charter)

IOWA	42-1230603
(State of Incorporation)	(I.R.S. Employer Identification No.)

1601 22nd Street, West Des Moines, Iowa	50266
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (515) 222-2300

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

Yes x No o

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

Yes x No o

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

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

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

Yes o No x

As of April 27, 2016, there were 16,132,540 shares of common stock, no par value, outstanding.

WEST BANCORPORATION, INC.

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PART I - FINANCIAL INFORMATION
Item 1. Financial Statements
West Bancorporation, Inc. and Subsidiary
Consolidated Balance Sheets
(unaudited)

(dollars in thousands)	March 31, 2016	December 31, 2015
ASSETS		
Cash and due from banks	$48,919	$57,329
Federal funds sold	7,804	15,322
Cash and cash equivalents	56,723	72,651
Investment securities available for sale, at fair value	311,335	320,714
Investment securities held to maturity, at amortized cost (fair value of $51,455 and $51,918 at March 31, 2016 and December 31, 2015, respectively)	50,526	51,259
Federal Home Loan Bank stock, at cost	12,353	12,447
Loans	1,274,929	1,246,688
Allowance for loan losses	(15,280)	(14,967)
Loans, net	1,259,649	1,231,721
Premises and equipment, net	17,298	11,562
Accrued interest receivable	5,273	4,688
Bank-owned life insurance	32,688	32,834
Deferred tax assets, net	5,457	6,670
Other assets	3,817	3,850
Total assets	$1,755,119	$1,748,396
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
Deposits:		
Noninterest-bearing demand	$457,409	$486,707
Interest-bearing demand	247,300	267,824
Savings	632,934	570,391
Time of $250,000 or more	13,248	14,749
Other time	94,856	101,058
Total deposits	1,445,747	1,440,729
Federal funds purchased	1,685	2,760
Short-term borrowings	17,000	19,000
Subordinated notes, net of discount	20,388	20,385
Federal Home Loan Bank advances, net of discount	98,758	98,385
Long-term debt, net of discount	7,592	8,405
Accrued expenses and other liabilities	7,023	6,355
Total liabilities	1,598,193	1,596,019
COMMITMENTS AND CONTINGENCIES (NOTE 8)		
STOCKHOLDERS' EQUITY		
Preferred stock, $0.01 par value; authorized 50,000,000 shares; no shares issued and outstanding at March 31, 2016 and December 31, 2015	—	—
Common stock, no par value; authorized 50,000,000 shares; 16,106,540 and 16,064,435 shares issued and outstanding at March 31, 2016 and December 31, 2015, respectively	3,000	3,000

Additional paid-in capital	20,262	20,067
Retained earnings	132,865	129,740
Accumulated other comprehensive income (loss)	799	(430)
Total stockholders' equity	156,926	152,377
Total liabilities and stockholders' equity	$ 1,755,119	$ 1,748,396

See Notes to Consolidated Financial Statements.

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West Bancorporation, Inc. and Subsidiary
Consolidated Statements of Income
(unaudited)

	Three Months Ended March 31,	
(dollars in thousands, except per share data)	2016	2015
Interest income:		
Loans, including fees	$13,466	$12,622
Investment securities:		
Taxable	1,155	1,125
Tax-exempt	883	764
Federal funds sold	20	10
Total interest income	15,524	14,521
Interest expense:		
Deposits	705	571
Federal funds purchased	2	2
Short-term borrowings	14	26
Subordinated notes	187	171
Federal Home Loan Bank advances	872	724
Long-term debt	45	64
Total interest expense	1,825	1,558
Net interest income	13,699	12,963
Provision for loan losses	200	—
Net interest income after provision for loan losses	13,499	12,963
Noninterest income:		
Service charges on deposit accounts	596	620
Debit card usage fees	447	435
Trust services	297	325
Increase in cash value of bank-owned life insurance	168	189
Gain from bank-owned life insurance	443	—
Realized investment securities gains, net	—	11
Other income	279	280
Total noninterest income	2,230	1,860
Noninterest expense:		
Salaries and employee benefits	4,256	3,990
Occupancy	951	1,049
Data processing	579	574
FDIC insurance	218	202
Professional fees	234	204
Director fees	240	188
Other expenses	1,321	1,239
Total noninterest expense	7,799	7,446
Income before income taxes	7,930	7,377
Income taxes	2,234	2,274
Net income	$5,696	$5,103
Basic earnings per common share	$0.35	$0.32
Diluted earnings per common share	$0.35	$0.32

Cash dividends declared per common share	$0.16	$0.14

See Notes to Consolidated Financial Statements.

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West Bancorporation, Inc. and Subsidiary
Consolidated Statements of Comprehensive Income
(unaudited)

	Three Months Ended March 31,	
(dollars in thousands)	2016	2015
Net income	$5,696	$5,103
Other comprehensive income (loss):		
Unrealized gains on available for sale securities:		
Unrealized holding gains arising during the period	2,685	2,029
Less: reclassification adjustment for net gains realized in net income	—	(11)
Less: reclassification adjustment for amortization of net unrealized gains to interest income on securities transferred from available for sale to held to maturity	(24)	(10)
Income tax (expense)	(1,011)	(763)
Other comprehensive income on available for sale securities	1,650	1,245
Unrealized (losses) on derivatives arising during the period:	(830)	(1,113)
Less: reclassification adjustment for net loss on derivatives realized in net income	124	74
Less: reclassification adjustment for amortization of derivative termination costs	27	2
Income tax benefit	258	394
Other comprehensive (loss) on derivatives	(421)	(643)
Total other comprehensive income	1,229	602
Comprehensive income	$6,925	$5,705

See Notes to Consolidated Financial Statements.

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West Bancorporation, Inc. and Subsidiary
Consolidated Statements of Stockholders' Equity
(unaudited)

(in thousands, except share and per share data)	Preferred Stock	Common Stock Shares	Common Stock Amount	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2014	$ —	16,018,734	$ 3,000	$ 18,971	$ 117,950	$ 254	$ 140,175
Net income	—	—	—	—	5,103	—	5,103
Other comprehensive income, net of tax	—	—	—	—	—	602	602
Cash dividends declared, $0.14 per common share	—	—	—	—	(2,242)	—	(2,242)
Stock-based compensation costs	—	—	—	178	—	—	178
Issuance of common stock upon vesting of restricted stock units, net of shares withheld for payroll taxes	—	20,535	—	(179)	—	—	(179)
Excess tax benefits from vesting of restricted stock units	—	—	—	84	—	—	84
Balance, March 31, 2015	$ —	16,039,269	$ 3,000	$ 19,054	$ 120,811	$ 856	$ 143,721
Balance, December 31, 2015	$ —	16,064,435	$ 3,000	$ 20,067	$ 129,740	$ (430)	$ 152,377
Net income	—	—	—	—	5,696	—	5,696
Other comprehensive income, net of tax	—	—	—	—	—	1,229	1,229
Cash dividends declared, $0.16 per common share	—	—	—	—	(2,571)	—	(2,571)
Stock-based compensation costs	—	—	—	461	—	—	461
Issuance of common stock upon vesting of restricted stock units, net of shares withheld for payroll taxes	—	42,105	—	(348)	—	—	(348)
Excess tax benefits from vesting of restricted stock units	—	—	—	82	—	—	82
Balance, March 31, 2016	$ —	16,106,540	$ 3,000	$ 20,262	$ 132,865	$ 799	$ 156,926

See Notes to Consolidated Financial Statements.

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West Bancorporation, Inc. and Subsidiary
Consolidated Statements of Cash Flows
(unaudited)

(dollars in thousands)	Three Months Ended March 31, 2016	2015
Cash Flows from Operating Activities:		
Net income	$5,696	$5,103
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	200	—
Net amortization and accretion	1,106	898
Loss on disposition of premises and equipment	—	1
Investment securities gains, net	—	(11)
Stock-based compensation	461	178
Increase in cash value of bank-owned life insurance	(168)	(189)
Gain from bank-owned life insurance	(443)	—
Depreciation	241	230
Deferred income taxes	460	165
Excess tax benefits from vesting of restricted stock units	(82)	(84)
Change in assets and liabilities:		
Increase in accrued interest receivable	(585)	(689)
Decrease in other assets	252	2,697
Decrease in accrued expenses and other liabilities	(39)	(971)
Net cash provided by operating activities	7,099	7,328
Cash Flows from Investing Activities:		
Proceeds from sales of securities available for sale	—	10,057
Proceeds from maturities and calls of investment securities	12,072	10,146
Purchases of securities available for sale	—	(10,107)
Purchases of Federal Home Loan Bank stock	(7,527)	(8,187)
Proceeds from redemption of Federal Home Loan Bank stock	7,621	10,747
Net increase in loans	(28,128)	(131)
Purchases of premises and equipment	(5,977)	(1,041)
Proceeds of principal and earnings from bank-owned life insurance	621	—
Proceeds from settlement of other assets	—	3,593
Net cash provided by (used in) investing activities	(21,318)	15,077
Cash Flows from Financing Activities:		
Net increase in deposits	5,018	94,958
Net increase (decrease) in federal funds purchased	(1,075)	1,125
Net decrease in short-term borrowings	(2,000)	(66,000)
Principal payments on long-term debt	(815)	(815)
Interest rate swap termination costs paid	—	(158)
Common stock dividends paid	(2,571)	(2,242)
Restricted stock units withheld for payroll taxes	(348)	(179)
Excess tax benefits from vesting of restricted stock units	82	84
Net cash provided by (used in) financing activities	(1,709)	26,773
Net increase (decrease) in cash and cash equivalents	(15,928)	49,178
Cash and Cash Equivalents:		
Beginning	72,651	39,781

Ending	$56,723	$88,959
Supplemental Disclosures of Cash Flow Information:		
Cash payments for:		
Interest	$1,811	$1,569
Income taxes	—	40

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West Bancorporation, Inc. and Subsidiary
Notes to Consolidated Financial Statements
(unaudited)
(in thousands, except per share data)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared by West Bancorporation, Inc. (the Company) pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements have been condensed or omitted pursuant to such rules and regulations. Although management believes that the disclosures are adequate to make the information presented understandable, it is suggested that these interim consolidated financial statements be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2015. In the opinion of management, the accompanying consolidated financial statements contain all adjustments necessary to fairly present the financial position of the Company as of March 31, 2016 and December 31, 2015, and net income, comprehensive income and cash flows of the Company for the three months ended March 31, 2016 and 2015. The results for these interim periods may not be indicative of results for the entire year or for any other period.

The consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) established by the Financial Accounting Standards Board (FASB). References to GAAP issued by the FASB in these footnotes are to the FASB Accounting Standards Codification™, sometimes referred to as the Codification or ASC. In preparing the consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses for the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term are the fair value and other than temporary impairment (OTTI) of financial instruments and the allowance for loan losses.

The accompanying unaudited consolidated financial statements include the accounts of the Company, West Bank and West Bank's wholly-owned subsidiary WB Funding Corporation (which owned an interest in a limited liability company that was sold in the fourth quarter of 2015). All significant intercompany transactions and balances have been eliminated in consolidation. In accordance with GAAP, West Bancorporation Capital Trust I is recorded on the books of the Company using the equity method of accounting and is not consolidated.

Reclassification: Certain amounts in prior year consolidated financial statements have been reclassified, with no effect on net income, comprehensive income or stockholders' equity, to conform with current period presentation.

Current accounting developments: In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606): Summary and Amendments that Create Revenue from Contracts with Customers (Topic 606) and Other Assets and Deferred Costs—Contracts with Customers (Subtopic 340-40). The guidance in this update supersedes the revenue recognition requirements in ASC Topic 605, Revenue Recognition, and most industry-specific guidance throughout the industry topics of the Codification. For public companies, this update will be effective for interim and annual periods beginning after December 15, 2017. The Company is currently assessing the impact that this guidance will have on its consolidated financial statements, but does not expect the guidance to have a material impact on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-03, Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The update simplifies the presentation of debt issuance costs by requiring that debt issuance costs be presented in the balance sheet as a direct deduction from the carrying amount of debt liability, consistent with debt discounts or premiums. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this update. For public companies, this update was effective for interim and annual periods beginning after December 15, 2015, and was applied retrospectively. The adoption of this guidance required a balance sheet reclassification of unamortized debt issuance costs, which did not have a material impact on the Company's consolidated financial statements.

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(dollars in thousands, except per share data)

In January 2016, the FASB issued ASU No. 2016-01, Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities. The update enhances the reporting model for financial instruments to provide users of financial statements with more decision-useful information by updating certain aspects of recognition, measurement, presentation and disclosure of financial instruments. Among other changes, the update includes requiring changes in fair value of equity securities with readily determinable fair value to be recognized in net income and clarifies that entities should evaluate the need for a valuation allowance on a deferred tax asset related to available for sale securities in combination with the entities' other deferred tax assets. For public companies, this update will be effective for interim and annual periods beginning after December 15, 2017, and is to be applied on a modified retrospective basis. The Company is currently assessing the impact that this guidance will have on its consolidated financial statements, but does not expect the guidance to have a material impact on the Company's consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). The guidance in the update supersedes the requirements in ASC Topic 840, Leases. The update will require business entities to recognize lease assets and liabilities on the balance sheet and to disclose key information about leasing arrangements. A lessee would recognize a liability to make lease payments and a right-of-use asset representing its right to use the leased asset for the lease term. For public companies, this update will be effective for interim and annual periods beginning after December 15, 2018, and is to be applied on a modified retrospective basis. The Company is currently assessing the impact that this guidance will have on its consolidated financial statements, but does not expect the guidance to have a material impact on the Company's consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, Compensation—Stock Compensation (Topic 718). The update simplifies several aspects of accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The guidance also allows an entity to make an entity-wide accounting policy election to either estimate expected forfeitures or account for forfeitures as they occur. For public companies, the update is effective for annual periods beginning after December 15, 2016. Portions of the amended guidance are to be applied using a modified retrospective transition method and others require prospective application. The Company is currently assessing the impact that this guidance will have on its consolidated financial statements, but does not expect the guidance to have a material impact on the Company's consolidated financial statements.

2. Earnings per Common Share

Basic earnings per common share are computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted earnings per common share reflect the potential dilution that could occur if the Company's outstanding restricted stock units were vested. The dilutive effect was computed using the treasury stock method, which assumes all stock-based awards were exercised and the hypothetical proceeds from exercise were used by the Company to purchase common stock at the average market price during the period. The incremental shares, to the extent they would have been dilutive, were included in the denominator of the diluted earnings per common share calculation. The calculations of earnings per common share and diluted earnings per common share for the three months ended March 31, 2016 and 2015 are presented in the following table.

(in thousands, except per share data)	Three Months Ended March 31, 2016	2015
Net income	$5,696	$5,103
Weighted average common shares outstanding	16,070	16,020
Weighted average effect of restricted stock units outstanding	41	65
Diluted weighted average common shares outstanding	16,111	16,085
Basic earnings per common share	$0.35	$0.32
Diluted earnings per common share	$0.35	$0.32

Restricted stock units totaling 151,630 were anti-dilutive and therefore excluded from the computation of diluted earnings per common share for the three months ended March 31, 2016. No restricted stock units were anti-dilutive for the three months ended March 31, 2015.

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West Bancorporation, Inc. and Subsidiary
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(unaudited)
(dollars in thousands, except per share data)

3. Investment Securities

The following tables show the amortized cost, gross unrealized gains and losses, and fair value of investment securities, by investment security type as of March 31, 2016 and December 31, 2015.

	March 31, 2016			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
Securities available for sale:				
U.S. government agencies and corporations	$2,545	$128	$—	$ 2,673
State and political subdivisions	71,390	1,926	(7)	73,309
Collateralized mortgage obligations [1]	126,142	819	(318)	126,643
Mortgage-backed securities [1]	96,568	924	(13)	97,479
Trust preferred security	1,776	—	(701)	1,075
Corporate notes and equity securities	10,113	68	(25)	10,156
	$308,534	$3,865	$(1,064)	$ 311,335

Securities held to maturity:					
State and political subdivisions	$50,526	$1,154	$ 323,560	44,130	13.6
Eurobond	34,538	36,933	(2,395)	(6.5)	
Emerging markets, high-yield and other	187,368	164,514	22,854	13.9	
Total	$ 589,596	$ 525,007	$ 64,589	12.3%	
Number of U.S. Trading Days	248	250			
Number of U.K. Trading Days	252	251			

For volume reporting purposes, transactions in foreign currencies are converted to U.S. dollars at average monthly rates. The 13.6% increase in U.S. high-grade volume was principally due to an increase in the Company s estimated market share of total U.S. high-grade corporate bond volume as reported by TRACE from 11.1% for the year ended December 31, 2011 to 12.4% for the year ended December 31, 2012. Estimated TRACE U.S. high-grade volume for the year ended December 31, 2012 was $3.0 trillion, an increase of approximately 1.6% from the year ended December 31, 2011. Our Eurobond volumes decreased by 6.5% for the year ended December 31, 2012 compared to the year ended December 31, 2011 due, in part, to unfavorable market conditions in the European region. Emerging markets, high-yield and other volume increased by 13.9% for the year ended December 31, 2012 compared to the year ended December 31, 2011, primarily due to higher emerging markets and high-yield bond volumes.

Our average variable transaction fee per million for the years ended December 31, 2012 and 2011 was as follows:

	Year Ended December 31, 2012	2011
Average Variable Transaction Fee Per Million		
U.S. high-grade fixed rate	$ 202	$ 190

U.S. high-grade floating rate	34	22
Total U.S. high-grade	197	183
Eurobond	73	99
Emerging markets, high-yield and other	214	175
Total	195	175

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The U.S. high-grade average variable transaction fee per million increased to $197 per million for the year ended December 31, 2012 from $183 per million for the year ended December 31, 2011. The change was primarily due to an increase in the duration of bonds traded. Eurobond average variable transaction fee per million decreased to $73 per million for the year ended December 31, 2012 from $99 per million for the year ended December 31, 2011. Emerging markets, high-yield and other average variable transaction fee per million increased to $214 per million for the year ended December 31, 2012 from $175 per million for the year ended December 31, 2011, primarily due to a larger percentage of volume in products that carry higher fees per million, principally emerging markets and high-yield bonds.

Technology Products and Services. Technology products and services revenues decreased by $2.0 million or 13.7% to $12.4 million for the year ended December 31, 2012 from $14.3 million for the year ended December 31, 2011. The decrease was primarily a result of lower technology integration consulting services and lower software license sales primarily due to a shift to a rental software license model.

Information and User Access Fees. Information and user access fees increased by $0.2 million or 3.3% to $7.4 million for the year ended December 31, 2012 from $7.2 million for the year ended December 31, 2011.

Investment Income. Investment income decreased by $0.1 million or 13.9% to $1.1 million for the year ended December 31, 2012 from $1.2 million for the year ended December 31, 2011.

Other. Other revenues increased by $0.2 million or 8.4% to $3.2 million for the year ended December 31, 2012 from $2.9 million for the year ended December 31, 2011.

Expenses

Our expenses for the years ended December 31, 2012 and 2011, and the resulting dollar and percentage changes, were as follows:

	Year Ended December 31,					
	2012		2011			
	$	% of Revenues	$	% of Revenues	$ Change	% Change
	($ in thousands)					
Expenses						
Employee compensation and benefits	$ 60,361	30.5%	$ 58,786	32.5%	$ 1,575	2.7%
Depreciation and amortization	8,233	4.2	6,781	3.7	$ 1,452	21.4
Technology and communications	12,766	6.4	10,912	6.0	$ 1,854	17.0
Professional and consulting fees	13,081	6.6	10,138	5.6	$ 2,943	29.0
Occupancy	3,012	1.5	2,921	1.6	$ 91	3.1
Marketing and advertising	5,470	2.8	4,882	2.7	$ 588	12.0
General and administrative	8,595	4.3	7,946	4.4	$ 649	8.2
Total expenses	$ 111,518	56.3%	$ 102,366	56.5%	$ 9,152	8.9%

Employee Compensation and Benefits. Employee compensation and benefits increased by $1.6 million or 2.7% to $60.4 million for the year ended December 31, 2012 from $58.8 million for the year ended December 31, 2011. This increase was primarily attributable to higher wages and employment taxes and benefits aggregating $1.8 million and higher stock-based compensation expense of $1.5 million, offset by increased wage capitalization related to software development of $1.3 million. The increase in stock-based compensation expense was principally due to the cancelation of unvested stock options, restricted stock and performance shares related to the June 2011 resignation of the Company s president. The total number of employees increased to 240 as of December 31, 2012 from 232 as of December 31, 2011. As a percentage of total revenues, employee compensation and benefits expense decreased to 30.5% for the year ended December 31, 2012 from 32.5% for the year ended December 31, 2011.

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Depreciation and Amortization. Depreciation and amortization expense increased by $1.5 million or 21.4% to $8.2 million for the year ended December 31, 2012 from $6.8 million for the year ended December 31, 2011. The increase was primarily due to an increase in amortization of software development costs of $0.9 million and an increase in depreciation for production hardware equipment of $0.4 million. For the years ended December 31, 2012 and 2011, we capitalized $5.2 million and $4.1 million, respectively, of software development costs. For the years ended December 31, 2012 and 2011, we capitalized $5.2 million and $3.2 million, respectively, of equipment and leasehold improvements. The higher equipment purchases were primarily due to the build-out of a replacement disaster recovery data center.

Technology and Communications. Technology and communications expense increased by $1.9 million or 17.0% to $12.8 million for the year ended December 31, 2012 from $10.9 million for the year ended December 31, 2011. The increase was primarily attributable to higher expenses associated with our new data center and increased market data, production data and telecommunication costs.

Professional and Consulting Fees. Professional and consulting fees increased by $2.9 million or 29.0% to $13.1 million for the year ended December 31, 2012 from $10.1 million for the year ended December 31, 2011. The increase was principally due to higher legal expense of $0.8 million, audit and tax services of $0.6 million and IT consulting of $0.6 million. Transaction costs related to the Xtrakter acquisition, mainly legal, audit and tax fees, amounted to approximately $1.1 million in 2012.

Occupancy. Occupancy costs increased by $0.1 million or 3.1% to $3.0 million for the year ended December 31, 2012 from $2.9 million for the year ended December 31, 2011.

Marketing and Advertising. Marketing and advertising expense increased by $0.6 million or 12% to $5.5 million for the year ended December 31, 2012 from $4.9 million for the year ended December 31, 2011. The increase was principally due to higher advertising costs of $0.2 million and public relations of $0.3 million.

General and Administrative. General and administrative expense increased by $0.6 million or 8.2% to $8.6 million for the year ended December 31, 2012 from $7.9 million for the year ended December 31, 2011. The increase was due to an increase in state and local sales tax and VAT tax of $1.3 million, offset by a decrease of $0.7 million in charges for doubtful accounts. In 2011, we recognized a credit of $1.0 million resulting from the settlement of a reimbursement claim on a previously paid sales tax. In 2011, we also recorded a charge for doubtful accounts of $0.9 million relating to the MF Global Inc. liquidation proceeding and a write-off of a minority investment of $0.6 million.

Provision for Income Tax

We recorded an income tax provision of $26.6 million and $31.0 million for the years ended December 31, 2012 and 2011, respectively. The decrease in the 2012 tax provision was primarily attributable to a non-recurring favorable income tax adjustment of $6.7 million, offset by an increase in pre-tax income.

Our consolidated effective tax rate for the twelve months ended December 31, 2012 was 30.7%, compared to 39.4% for the twelve months ended December 31, 2011. The 2012 provision includes a favorable income tax adjustment of $6.7 million relating to certain previously unrecognized tax benefits. We updated the recognition of certain acquired net operating loss carryforwards in response to a private letter ruling received from the Internal Revenue Service. Our consolidated effective tax rate can vary from period to period depending on, among other factors, the geographic and business mix of our earnings and changes in tax legislation and tax rates.

As of December 31, 2012, we had restricted U.S. federal net operating loss carryforwards of approximately $17.1 million. The utilization of our U.S. net operating loss carryforwards is subject to an annual limitation as determined by Section 382 of the Internal Revenue Code.

Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Overview

Total revenues increased by $34.9 million or 23.8% to $181.1 million for the year ended December 31, 2011 from $146.2 million for the year ended December 31, 2010. This increase in total revenues was primarily due to an increase in commissions of $33.3 million.

Total expenses increased by $7.0 million or 7.4% to $102.4 million for the year ended December 31, 2011 from $95.3 million for the year ended December 31, 2010. The increase was primarily due to higher employee compensation and benefits of $2.3 million, professional and consulting fees of $1.6 million and marketing and advertising costs of $1.8 million.

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Income before taxes increased by $27.8 million or 54.7% to $78.7 million for the year ended December 31, 2011 from $50.9 million for the year ended December 31, 2010. Net income increased by $16.3 million or 51.8% to $47.7 million for the year ended December 31, 2011 from $31.4 million for the year ended December 31, 2010.

Revenues

Our revenues for the years ended December 31, 2011 and 2010, and the resulting dollar and percentage changes, were as follows:

	Year Ended December 31, 2011		2010			
	$	% of Revenues	$	% of Revenues	$ Change	% Change
	($ in thousands)					
Commissions	$ 155,444	85.8%	$ 122,180	83.6%	$ 33,264	27.2%
Technology products and services	14,310	7.9	13,648	9.3	662	4.9
Information and user access fees	7,199	4.0	6,681	4.6	518	7.8
Investment income	1,229	0.7	1,192	0.8	37	3.1
Other	2,917	1.6	2,527	1.7	390	15.4
Total revenues	$ 181,099	100.0%	$ 146,228	100.0%	$ 34,871	23.8%

Commissions. Our commission revenues for the years ended December 31, 2011 and 2010, and the resulting dollar and percentage changes, were as follows:

	Year Ended December 31,			
	2011	2010	$ Change	% Change
	($ in thousands)			
Variable transaction fees				
U.S. high-grade	$ 59,351	$ 46,329	$ 13,022	28.1%
Eurobond	3,650	5,963	(2,313)	(38.8)
Emerging markets, high-yield and other	28,714	19,728	8,986	45.5
Total variable transaction fees	91,715	72,020	19,695	27.3
Distribution fees				
U.S. high-grade	49,580	37,467	12,113	32.3
Eurobond	14,149	12,693	1,456	11.5
Total distribution fees	63,729	50,160	13,569	27.1
Total commissions	$ 155,444	$ 122,180	$ 33,264	27.2%

The $13.6 million increase in distribution fees for the year ended December 31, 2011 compared to the year ended December 31, 2010 was due principally to the migration of seven U.S. broker-dealer market makers in the prior 15 months from an all-variable fee plan to a plan that incorporates a combination of a monthly distribution fee and variable transaction fees and the addition of several new U.S. and European broker-dealer market makers to the platform.

The following table shows the extent to which the increase in commissions for the year ended December 31, 2011 was attributable to changes in transaction volumes, variable transaction fees per million and distribution fees:

	Change from Year Ended December 31, 2010			
	U.S. High-Grade	Eurobond	Emerging Markets, High-Yield and Other	Total
	(In thousands)			
Volume increase (decrease)	$ 15,259	$ (1,580)	$ 10,154	$ 23,833
Variable transaction fee per million (decrease)	(2,237)	(733)	(1,168)	(4,138)
Monthly distribution fees increase	12,113	1,456		13,569
Total commissions increase (decrease)	$ 25,135	$ (857)	$ 8,986	$ 33,264

Our trading volume for each of the years presented was as follows:

	Year Ended December 31,			
	2011	2010	$ Change	% Change
Trading Volume Data (in millions)				
U.S. high-grade fixed rate	$ 311,758	$ 235,698	$ 76,060	32.3%
U.S. high-grade floating rate	11,802	7,698	4,104	53.3
Total U.S. high-grade	323,560	243,396	80,164	32.9
Eurobond	36,933	50,251	(13,318)	(26.5)
Emerging markets, high-yield and other	164,514	108,610	55,904	51.5
Total	$ 525,007	$ 402,257	$ 122,750	30.5%
Number of U.S. Trading Days	250	250		
Number of U.K. Trading Days	251	253		

For volume reporting purposes, transactions in foreign currencies are converted to U.S. dollars at average monthly rates. The 32.3% increase in U.S. high-grade volume was principally due to an increase in the Company s estimated market share of total U.S. high-grade corporate bond volume as reported by TRACE from 8.4% for the year ended December 31, 2010 to 11.1% for the year ended December 31, 2011. Estimated TRACE U.S. high-grade volume for the year ended December 31, 2011 was $2.9 trillion and increased approximately 1.0% from the year ended December 31, 2010. Our Eurobond volumes decreased by 26.5% for the year ended December 31, 2011 compared to the year ended December 31, 2010. We believe that the decline in Eurobond volumes was due, in part, to continuing sovereign debt concerns which negatively impacted market conditions and the competitive environment in Europe. Emerging markets, high-yield and other volume increased by 51.5% for the year ended December 31, 2011 compared to the year ended December 31, 2010, primarily due to higher agency volumes.

Our average variable transaction fee per million for the years ended December 31, 2011 and 2010 was as follows:

	Year Ended December 31,	
	2011	2010
Average Variable Transaction Fee Per Million		
U.S. high-grade fixed rate	$ 190	$ 196
U.S. high-grade floating rate	22	28
Total U.S. high-grade	183	190
Eurobond	99	119
Emerging markets, high-yield and other	175	182
Total	175	179

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The U.S. high-grade average variable transaction fee per million decreased to $183 per million for the year ended December 31, 2011 from $190 per million for the year ended December 31, 2010. The decline was primarily due to the migration of seven U.S. broker-dealer market makers from an all-variable plan to a plan that incorporates a combination of a monthly distribution fee and variable transaction fees. The decline was partially offset from an increase in the percentage of volume derived from broker-dealer clients on an all-variable plan. Eurobond average variable transaction fee per million decreased to $99 per million for the year ended December 31, 2011 from $119 per million for the year ended December 31, 2010. In June 2010, we launched a click-to-trade protocol in the European market. In connection with the launch, the Eurobond fee plan was generally revised downward. Emerging markets, high-yield and other average variable transaction fee per million decreased to $175 per million for the year ended December 31, 2011 from $182 per million for the year ended December 31, 2010, primarily due to a higher percentage of volume in products that carry lower fees per million, principally agency bonds.

Technology Products and Services. Technology products and services revenues increased by $0.7 million or 4.9% to $14.3 million for the year ended December 31, 2011 from $13.6 million for the year ended December 31, 2010. The increase was primarily a result of higher technology integration consulting services.

Information and User Access Fees. Information and user access fees increased by $0.5 million or 7.8% to $7.2 million for the year ended December 31, 2011 from $6.7 million for the year ended December 31, 2010.

Investment Income. Investment income was $1.2 million for each of the years ended December 31, 2011 and December 31, 2010.

Other. Other revenues increased by $0.4 million or 15.4% to $2.9 million for the year ended December 31, 2011 from $2.5 million for the year ended December 31, 2010. The increase was primarily a result of higher initial set-up fees from broker-dealer clients.

Expenses

Our expenses for the years ended December 31, 2011 and 2010, and the resulting dollar and percentage changes, were as follows:

	Year Ended December 31,					
	2011		2010			
	$	% of Revenues	$	% of Revenues	$ Change	% Change
	($ in thousands)					
Expenses						
Employee compensation and benefits	$ 58,786	32.5%	$ 56,446	38.6%	$ 2,340	4.1%
Depreciation and amortization	6,781	3.7	6,350	4.3	431	6.8
Technology and communications	10,912	6.0	9,982	6.8	930	9.3
Professional and consulting fees	10,138	5.6	8,503	5.8	1,635	19.2
Occupancy	2,921	1.6	2,997	2.0	(76)	(2.5)
Marketing and advertising	4,882	2.7	3,075	2.1	1,807	58.8
General and administrative	7,946	4.4	7,965	5.4	(19)	(0.2)
Total expenses	$ 102,366	56.5%	$ 95,318	65.2%	$ 7,048	7.4%

Employee Compensation and Benefits. Employee compensation and benefits increased by $2.3 million or 4.1% to $58.8 million for the year ended December 31, 2011 from $56.4 million for the year ended December 31, 2010. This increase was primarily attributable to higher incentive compensation of $2.3 million due to improved operating performance and higher wages and employment taxes and benefits aggregating $2.2 million, offset by a decline in stock-based compensation expense of $2.1 million. The lower stock-based compensation expense was principally due to the cancelation of unvested stock options, restricted stock and performance shares related to the June 2011 resignation of the Company s President. The total number of employees increased to 232 as of December 31, 2011 from 227 as of December 31, 2010. As a percentage of total revenues, employee compensation and benefits expense decreased to 32.5% for the year ended December 31, 2011 from 38.6% for the year ended December 31, 2010.

Depreciation and Amortization. Depreciation and amortization expense increased by $0.4 million or 6.8% to $6.8 million for the year ended December 31, 2011 from $6.4 million for the year ended December 31, 2010. The increase was primarily due to higher depreciation of production and office hardware costs of $0.4 million. For the years ended December 31, 2011 and 2010, we capitalized $4.1 million and $1.9

million, respectively, of software development costs, and $3.2 million and $5.2 million, respectively, of equipment and leasehold improvements. The 2010 equipment and leasehold improvement expenditures included $3.0 million associated with the move of our corporate offices to new premises in New York City in the first quarter of 2010.

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Technology and Communications. Technology and communications expense increased by $0.9 million or 9.3% to $10.9 million for the year ended December 31, 2011 from $10.0 million for the year ended December 31, 2010. The increase was primarily attributable to higher expenses associated with production data and telecommunication costs.

Professional and Consulting Fees. Professional and consulting fees increased by $1.6 million or 19.2% to $10.1 million for the year ended December 31, 2011 from $8.5 million for the year ended December 31, 2010. The increase was principally due to higher technology consulting costs of $1.2 million and legal expense, principally in connection with proposed swap execution facility-related regulation, of $0.9 million.

Occupancy. Occupancy costs decreased by $0.1 million or 2.5% to $2.9 million for the year ended December 31, 2011 from $3.0 million for the year ended December 31, 2010.

Marketing and Advertising. Marketing and advertising expense increased by $1.8 million or 58.8% to $4.9 million for the year ended December 31, 2011 from $3.1 million for the year ended December 31, 2010. The increase was principally due to higher advertising costs of $0.9 million associated with our credit default swaps trading capabilities and travel and entertainment expenses related to sales activities of $0.6 million.

General and Administrative. General and administrative expense was $7.9 million for each of the years ended December 31, 2011 and 2010. During 2011, a credit of $1.0 million resulting from the settlement of a reimbursement claim on a previously paid sales tax was offset by a higher charge for doubtful accounts of $0.6 million and a write-off of a minority investment of $0.6 million. During the fourth quarter of 2011, MF Global Inc., a broker-dealer market maker on our platform, entered a liquidation proceeding. In connection with the proceeding, we recorded a 100% allowance against outstanding receivables amounting to $0.9 million.

Provision for Income Tax

We recorded an income tax provision of $31.0 million and $19.5 million for the years ended December 31, 2011 and 2010, respectively. The increase in the tax provision was primarily attributable to the $27.8 million increase in pre-tax income. With the exception of certain foreign and state and local taxes, the provision for income taxes was largely a non-cash expense since we had net operating loss and tax credit carryforwards available to offset the majority of U.S. taxable income. We fully utilized the balance of our unrestricted U.S. federal net operating loss carryforward during 2011, which we expect will result in an increase in cash paid for income taxes in subsequent years.

Our consolidated effective tax rate for the year ended December 31, 2011 was 39.4% compared to 38.3% for the year ended December 31, 2010. Our consolidated effective tax rate can vary from period to period depending on, among other factors, the geographic and business mix of our earnings and changes in tax legislation and tax rates.

As of December 31, 2011, we had restricted U.S. federal net operating loss carryforwards of approximately $12.3 million. The utilization of our U.S. net operating loss carryforwards is subject to an annual limitation of approximately $2.1 million as determined by Section 382 of the Internal Revenue Code.

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Quarterly Results of Operations

Our quarterly results have varied significantly as a result of:

- changes in trading volume due to market conditions, changes in the number of trading days in certain quarters, and seasonality effects caused by slow-downs in trading activity during certain periods;

- changes in the number of broker-dealers and institutional investors using our trading platform as well as variation in usage by existing clients;

- expansion of the products we offer to our clients; and

- variance in our expenses, particularly employee compensation and benefits.

The following table sets forth certain unaudited consolidated quarterly income statement data for the eight quarters ended December 31, 2012. In our opinion, this unaudited information has been prepared on a basis consistent with our annual financial statements and includes all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of the unaudited quarterly data. This information should be read in conjunction with our Consolidated Financial Statements and related Notes included in this Annual Report on Form 10-K. The results of operations for any quarter are not necessarily indicative of results that we may achieve for any subsequent periods.

	Three Months Ended							
	Dec 31, 2012	Sep 30, 2012	Jun 30, 2012	Mar 31, 2012	Dec 31, 2011	Sep 30, 2011	Jun 30, 2011	Mar 31, 2011
	(In thousands, except per share data) (unaudited)							
Revenues								
Commissions	$ 44,228	$ 42,379	$ 42,690	$ 44,902	$ 38,761	$ 39,822	$ 39,076	$ 37,785
Technology products and services	3,244	2,979	3,220	2,908	3,439	3,779	3,984	3,108
Information and user access fees	1,878	1,896	1,790	1,871	1,960	1,831	1,719	1,689
Interest income	236	251	268	303	317	303	310	299
Other	801	752	857	751	658	829	702	728
Total revenues	50,387	48,257	48,825	50,735	45,135	46,564	45,791	43,609
Expenses								
Employee compensation and benefits	14,579	14,636	15,305	15,841	13,707	13,707	15,104	16,268
Depreciation and amortization	2,337	2,081	1,961	1,854	1,793	1,799	1,627	1,562
Technology and communications	3,534	3,262	3,015	2,955	2,916	2,772	2,724	2,500
Professional and consulting fees	4,018	3,202	2,837	3,024	2,354	2,247	2,665	2,872
Occupancy	764	732	757	759	726	721	708	766
Marketing and advertising	1,224	1,067	1,732	1,447	1,380	1,280	1,248	974
General and administrative	2,402	2,068	2,018	2,107	3,393	1,742	1,810	1,001
Total expenses	28,858	27,048	27,625	27,987	26,269	24,268	25,886	25,943
Income before income taxes	21,529	21,209	21,200	22,748	18,866	22,296	19,905	17,666
Provision for income taxes (1)	1,064	7,727	8,571	9,255	7,323	8,852	7,968	6,886
Net income	$ 20,465	$ 13,482	$ 12,629	$ 13,493	$ 11,543	$ 13,444	$ 11,937	$ 10,780

Net income per common share:								
Basic	$ 0.56	$ 0.37	$ 0.35	$ 0.37	$ 0.31	$ 0.36	$ 0.32	$ 0.30
Diluted (1)	$ 0.54	$ 0.36	$ 0.34	$ 0.35	$ 0.29	$ 0.34	$ 0.30	$ 0.27

(1) In the fourth quarter of 2012, the Company recognized a favorable income tax adjustment of $6.7 million, or $0.18 per share, relating to certain previously unrecognized tax benefits.

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The following tables set forth trading volume and average variable transaction fee per million traded for the eight quarters ended December 31, 2012.

	Three Months Ended							
	Dec 31, 2012	Sep 30, 2012	Jun 30, 2012	Mar 31, 2012	Dec 31, 2011	Sep 30, 2011	Jun 30, 2011	Mar 31, 2011
	(In millions)							
Trading Volume Data								
U.S. high-grade fixed rate	$ 89,211	$ 83,193	$ 87,686	$ 94,997	$ 73,181	$ 79,233	$ 77,077	$ 82,267
U.S. high-grade floating rate	3,499	2,795	2,984	3,325	2,278	2,761	3,825	2,938
Total U.S. high-grade	92,710	85,988	90,670	98,322	75,459	81,994	80,902	85,205
Eurobond	7,995	6,016	7,793	12,734	8,042	7,580	9,998	11,313
Emerging markets, high-yield and other	48,373	45,748	46,313	146,934	41,699	42,092	42,061	38,661
Total	$ 149,078	$ 137,752	$ 144,776	$ 157,990	$ 125,200	$ 131,666	$ 132,961	$ 135,179

	Three Months Ended							
	Dec 31, 2012	Sep 30, 2012	Jun 30, 2012	Mar 31, 2012	Dec 31, 2011	Sep 30, 2011	Jun 30, 2011	Mar 31, 2011
Average Variable Transaction Fee Per Million								
U.S. high-grade fixed rate	$ 200	$ 209	$ 208	$ 194	$ 195	$ 195	$ 192	$ 178
U.S. high-grade floating rate	45	37	28	25	27	24	22	17
Total U.S. high-grade	193	203	202	188	190	189	184	172
Eurobond	80	79	74	65	92	108	95	101
Emerging markets, high-yield and other	232	216	205	202	166	175	182	176
Total	200	202	196	183	175	180	177	167
Number of U.S. trading days	60	63	63	62	61	64	63	62
Number of U.K. trading days	64	64	60	64	63	65	60	63

Liquidity and Capital Resources

During the past three years, we have met our funding requirements through cash on hand and internally generated funds. Cash and cash equivalents and securities available-for-sale totaled $180.1 million at December 31, 2012.

On January 14, 2013, we entered into a three-year credit agreement that provides for revolving loans and letters of credit up to an aggregate of $50.0 million. Subject to satisfaction of certain specified conditions, we are permitted to upsize the credit facility by an additional $50.0 million in total.

Our cash flows were as follows:

	Year Ended December 31,		
	2012	2011	2010
	(In thousands)		
Net cash provided by operating activities	$ 81,582	$ 65,478	$ 64,146
Net cash provided by (used in) investing activities	15,030	(8,576)	(7,720)
Net cash (used in) financing activities	(136,175)	(11,199)	(33,849)
Effect of exchange rate changes on cash and cash equivalents	(1,149)	(1,077)	(924)
Net (decrease) increase for the period	$ (40,712)	$ 44,626	$ 21,653

We define free cash flow as cash flow from operating activities less expenditures for furniture, equipment and leasehold improvements and capitalized software development costs. For the years ended December 31, 2012, 2011 and 2010, free cash flow was $71.2 million, $58.3 million and $57.0 million, respectively. Free cash flow is a non-GAAP financial measure. We believe that this non-GAAP financial measure, when taken into consideration with the corresponding GAAP financial measures, is important in gaining an understanding of our financial strength and cash flow generation.

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Cash Flows for the Year Ended December 31, 2012 Compared to Year Ended December 31, 2011

Net cash provided by operating activities was $81.6 million for the year ended December 31, 2012 compared to $65.5 million for the year ended December 31, 2011. The $16.1 million increase was due to higher net income of $12.4 million and an increase in cash provided by working capital of $17.5 million, offset by a decrease in deferred taxes of $16.8 million. We fully utilized the balance of our unrestricted U.S. federal net operating loss carryforward during 2011, which resulted in an increase in cash paid for income taxes in 2012. During 2012, cash paid for income taxes was $15.1 million compared to $10.2 million in 2011.

Net cash provided by investing activities was $15.0 million for the year ended December 31, 2012 compared to net cash used in investing activities of $8.6 million for the year ended December 31, 2011. The $23.6 million increase was primarily due to net sales and maturities of securities available-for-sale of $25.4 million in 2012 compared to net purchases of securities available-for-sale of $4.9 million for the year ended December 31, 2011. Capital expenditures were $10.4 million and $7.2 million for the years ended December 31, 2012 and 2011, respectively. The increase in capital expenditures was primarily due to the build-out of a replacement disaster recovery data center in 2012.

Net cash used in financing activities was $136.2 million for the year ended December 31, 2012 compared to $11.2 million for the year ended December 31, 2011. The $125.0 million increase in net cash used in financing activities was principally due to an increase in repurchases of our common stock of $68.2 million, which included $52.8 million acquired from JPMorgan Chase & Co. (JPM), an increase in withholding tax payments on restricted stock vesting and stock option exercises of $15.6 million and an increase in cash dividends paid in 2012 on our common stock of $50.4 million, offset by an increase in excess tax benefits from stock-based compensation of $7.5 million and the exercise of stock options of $1.7 million. We paid a special dividend on our common stock in December 2012 of $47.6 million.

Cash Flows for the Year Ended December 31, 2011 Compared to Year Ended December 31, 2010

Net cash provided by operating activities was $65.5 million for the year ended December 31, 2011 compared to $64.1 million for the year ended December 31, 2010. The $1.3 million increase in net cash provided by operating activities was primarily due to an increase in net income of $16.3 million, offset by a decrease in cash used for working capital of $14.6 million and lower non-cash stock based compensation expense of $2.1 million. We fully utilized the balance of our unrestricted U.S. federal net operating loss carryforward during 2011, which resulted in an increase in cash paid for income taxes in 2011. During 2011, cash paid for income taxes was $10.2 million compared to $2.2 million in 2010.

Net cash used in investing activities was $8.6 million for the year ended December 31, 2011 compared to $7.7 million for the year ended December 31, 2010. Net purchases of securities available-for-sale were $4.9 million in 2011 compared to $0.6 million in December 31, 2010. Capital expenditures were $7.2 million and $7.1 million for the years ended December 31, 2011 and 2010, respectively. Securities and cash provided as collateral decreased by $3.5 million in 2011.

Net cash used in financing activities was $11.2 million for the year ended December 31, 2011 compared to $33.8 million for the year ended December 31, 2010. The $22.7 million decrease in net cash used in financing activities was principally due to a reduction in repurchases of our common stock of $23.1 million and an increase in windfall tax benefits on stock-based compensation of $5.7 million, offset by an increase of $2.4 million in withholding tax payments on restricted stock vesting and stock option exercises and an increase of $3.1 million in cash dividends paid in 2011 on common stock.

Other Factors Relating to Liquidity and Capital Resources

We are dependent on our broker-dealer clients who are not restricted from buying and selling fixed-income securities with institutional investors, either directly or through their own proprietary or third-party platforms. None of our broker-dealer clients is contractually or otherwise obligated to continue to use our electronic trading platform. The loss of, or a significant reduction in the use of our electronic platform by, our broker-dealer clients could reduce our cash flows, affect our liquidity and have a material adverse effect on our business, financial condition and results of operations.

We believe that our current cash resources and borrowing capacity under our credit facility are adequate to meet our liquidity needs and capital expenditure requirements for at least the next 12 months. However, our future liquidity and capital requirements will depend on a number of factors, including expenses associated with product development and expansion and new business opportunities that are intended to further diversify our revenue stream. We may also acquire or invest in technologies, business ventures or products that are complementary to our business. In addition, we fully utilized the balance of our unrestricted U.S. federal net operating loss carryforward during 2011, which resulted in an increase in cash paid for income taxes in 2012, and we expect further increases in subsequent years. In the event we require any additional financing, it will take the form of equity or debt financing. Any additional equity offerings may result in dilution to our stockholders. Any debt financings, if available at all, would likely be pursuant to the terms of our credit facility with JPM, which includes restrictive covenants with respect to dividends, issuances of additional capital and other financial and operational matters related to our business.

We have three regulated subsidiaries, MarketAxess Corporation, MarketAxess Europe Limited and MarketAxess Canada Ltd. MarketAxess Corporation is a registered broker-dealer in the U.S., MarketAxess Europe Limited is a registered multilateral trading facility dealer in the U.K. and MarketAxess Canada Ltd. is a registered Alternative Trading System dealer in the Province of Ontario. As such, they are subject to minimum regulatory capital requirements imposed by their respective market regulators that are intended to ensure general financial soundness and liquidity based on certain minimum capital requirements. The relevant regulations prohibit a registrant from repaying borrowings from its parent or affiliates, paying cash dividends, making loans to its parent or affiliates or otherwise entering into transactions that result in a significant reduction in its regulatory net capital position without prior notification to or approval from its principal regulator. The capital structures of our subsidiaries are designed to provide each with capital and liquidity consistent with its business and regulatory requirements. Subject to rulemaking pursuant to the Dodd-Frank Act, we currently expect to establish and operate a swap execution facility and/or a security-based swap execution facility and we will be required to maintain an additional amount of minimum net capital in connection with such facilities. The following table sets forth the capital requirements, as defined, that the Company s subsidiaries were required to maintain as of December 31, 2012:

	MarketAxess Corporation	MarketAxess Europe Limited (In thousands)	MarketAxess Canada Limited
Net capital	$ 63,624	$ 13,151	$ 479
Minimum net capital required	2,266	2,943	277
Excess net capital	$ 61,358	$ 10,208	$ 202

We execute certain bond transactions between and among institutional investor and broker-dealer clients on a riskless principal basis by serving as counterparty to both the buyer and the seller in matching back-to-back trades, which are then settled through a third-party clearing organization. We act as intermediary on a riskless principal basis in these bond transactions by serving as counterparty to the two clients involved. Settlement typically occurs within one to three trading days after the trade date. Cash settlement of the transaction occurs upon receipt or delivery of the underlying instrument that was traded. Under securities clearing agreements with the independent third party, we maintain collateral deposits with the clearing broker in the form of cash. As of December 31, 2012, the amount of the collateral deposits included in prepaid expenses and other assets in the Consolidated Statements of Financial Condition was $0.9 million. We are exposed to credit risk in the event a counterparty does not fulfill its obligation to complete a transaction. Pursuant to the terms of the securities clearing agreements between us and the independent clearing broker, the clearing broker has the right to charge us for losses resulting from a counterparty s failure to fulfill its contractual obligations. The losses are not capped at a maximum amount and apply to all trades executed through the clearing broker. At December 31, 2012, we had not recorded any liabilities with regard to this right.

In the ordinary course of business, we enter into contracts that contain a variety of representations, warranties and general indemnifications. Our maximum exposure from any claims under these arrangements is unknown, as this would involve claims that have not yet occurred. However, based on past experience, we expect the risk of loss to be remote.

In October 2011, our Board of Directors authorized a share repurchase program for up to $35.0 million of our common stock. As of December 31, 2012, a total of 955,342 shares were repurchased at an aggregate cost of $29.2 million. Shares repurchased under the program are held in treasury for future use. Through February 20, 2013, no additional shares have been repurchased under this plan.

In January 2013, our Board of Directors approved a quarterly cash dividend of $0.13 per share payable on February 28, 2013 to stockholders of record as of the close of business on February 14, 2013. Any future declaration and payment of dividends will be at the sole discretion of our Board of Directors. The Board of Directors may take into account such matters as general business conditions, our financial results, capital requirements, contractual, legal, and regulatory restrictions on the payment of dividends to our stockholders or by our subsidiaries to the parent and any such other factors as the Board of Directors may deem relevant.

On October 26, 2012, we entered into an agreement to acquire all of the outstanding shares of Xtrakter from Euroclear S.A./N.V. The aggregate purchase price is £26.0 million (approximately $40.5 million) in cash, plus transaction costs, and is subject to a post-closing adjustment based on the net working capital of Xtrakter on the closing date. The purchase price will be funded from available cash on hand. We received FSA approval of the change in control on February 18, 2013 and expect to complete the acquisition of Xtrakter on or about February 28, 2013.

Effects of Inflation

Because the majority of our assets are liquid in nature, they are not significantly affected by inflation. However, the rate of inflation may affect our expenses, such as employee compensation, office leasing costs and communications expenses, which may not be readily recoverable in the prices of our services. To the extent inflation results in rising interest rates and has other adverse effects on the securities markets, it may adversely affect our financial position and results of operations.

Contractual Obligations and Commitments

As of December 31, 2012, we had the following contractual obligations and commitments:

	Payments due by period				
	Total	Less than 1 year	1 - 3 years	3 - 5 years	More than 5 years
			(In thousands)		
Operating leases	$ 17,831	$ 1,796	$ 3,789	$ 4,991	$ 7,255
Capital leases	364	322	42		
Foreign currency forward contract	15,809	15,809			
	$ 34,004	$ 17,927	$ 3,831	$ 4,991	$ 7,255

We enter into foreign currency forward contracts to hedge the exposure to variability in foreign currency cash flows resulting from the net investment in our U.K. subsidiary. As of December 31, 2012, the notional value of the foreign currency forward contract outstanding was $15.8 million and the gross and net fair value liability was $17,000.

In January 2013, our Board of Directors approved a quarterly dividend to be paid to the holders of the outstanding shares of capital stock. A cash dividend of $0.13 per share of voting and non-voting common stock outstanding will be payable on February 28, 2013 to stockholders of record as of the close of business on February 14, 2013. We expect the total amount payable to be approximately $4.9 million.

On January 14, 2013, we entered into a three-year credit agreement that provides for revolving loans and letters of credit up to an aggregate of $50.0 million. Subject to satisfaction of certain specified conditions, we are permitted to upsize the credit facility by an additional $50.0 million in total.

Recent Accounting Pronouncements

See Note 2 to the Consolidated Financial Statements included in Item 8 of this Annual Report on Form 10-K for a discussion of recent accounting pronouncements.

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Item 7A. ***Quantitative and Qualitative Disclosures About Market Risk.***

Market risk is the risk of the loss resulting from adverse changes in market rates and prices, such as interest rates and foreign currency exchange rates.

Market Risk

The global financial services business is, by its nature, risky and volatile and is directly affected by many national and international factors that are beyond our control. Any one of these factors may cause a substantial decline in the U.S. and global financial services markets, resulting in reduced trading volume and revenues. These events could have a material adverse effect on our business, financial condition and results of operations.

As of December 31, 2012, we had a $51.2 million investment in securities available-for-sale. Adverse movements, such as a 10% decrease in the value of these securities or a downturn or disruption in the markets for these securities, could result in a substantial loss. In addition, principal gains and losses resulting from these securities could on occasion have a disproportionate effect, positive or negative, on our financial condition and results of operations for any particular reporting period.

See also Item 1A. *Risk Factors*, Risks Related to Our Industry *Economic, political and market factors beyond our control could reduce demand for our services and harm our business, and our profitability could suffer.*

Interest Rate Risk

Interest rate risk represents our exposure to interest rate changes with respect to the money market instruments, U.S. Treasury obligations and fixed-income securities in which we invest. As of December 31, 2012, our cash and cash equivalents and securities available-for-sale amounted to $180.1 million and were primarily invested in money market instruments, U.S. government obligations and municipal securities. We do not maintain an inventory of bonds that are traded on our platform.

Derivative Risk

Our limited derivative risk stems from our activities in the foreign currency forward contract market. We use this market to mitigate our U.S. dollar versus Pound Sterling exposure that arises from the activities of our U.K. subsidiary. As of December 31, 2012, the notional value of our foreign currency forward contract was $15.8 million. In October 2012, we purchased a foreign exchange call option to economically hedge the Xtrakter purchase price of £26.0 million. We do not speculate in any derivative instruments.

Credit Risk

We act as a riskless principal through MarketAxess Corporation and MarketAxess Europe Limited in certain transactions that we execute between clients. We act as an intermediary in these transactions by serving as counterparty to both the buyer and the seller in matching back-to-back bond trades, which are then settled through a third-party clearing organization. Settlement typically occurs within one to three trading days after the trade date. Cash settlement of the transaction occurs upon receipt or delivery of the underlying instrument that was traded.

We are exposed to credit risk in our role as trading counterparty to our clients. We are exposed to the risk that third parties that owe us money, securities or other assets will not perform their obligations. These parties may default on their obligations to us due to bankruptcy, lack of liquidity, operational failure or other reasons. Adverse movements in the prices of securities that are the subject of these transactions can increase our risk. Where the unmatched position or failure to deliver is prolonged, there may also be regulatory capital charges required to be taken by us. There can be no assurance that the policies and procedures we use to manage this credit risk will effectively mitigate our credit risk exposure.

Cash and cash equivalents includes cash and money market instruments that are primarily maintained at one major global bank. Given this concentration we are exposed to certain credit risk.

Item 8. ***Financial Statements and Supplementary Data.***

MARKETAXESS HOLDINGS INC.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

The unaudited supplementary data regarding consolidated quarterly income statement data are incorporated by reference to the information set forth in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, in the section captioned Quarterly Results of Operations.

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MANAGEMENT S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of MarketAxess Holdings Inc. is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934. The Company s internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. The Company s internal control over financial reporting includes those policies and procedures that:

(i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;

(ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and

(iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management assessed the effectiveness of the Company s internal control over financial reporting as of December 31, 2012. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control Integrated Framework*.

Based on our assessment and those criteria, management concluded that the Company maintained effective internal control over financial reporting as of December 31, 2012.

The effectiveness of our internal control over financial reporting as of December 31, 2012 has been audited by PricewaterhouseCoopers LLP, an independent registered public accounting firm, as stated in their report which appears herein.

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Report of Independent Registered Public Accounting Firm

To Board of Directors and Stockholders of MarketAxess Holdings Inc.:

In our opinion, the accompanying consolidated statements of financial condition and related consolidated statements of operations, consolidated statements of other comprehensive income, consolidated statements of changes in stockholders equity, and consolidated statements of cash flows, present fairly, in all material respects, the financial position of MarketAxess Holdings Inc. and its subsidiaries at December 31, 2012 and December 31, 2011, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2012 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2012, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Report on Internal Control over Financial Reporting. Our responsibility is to express opinions on these financial statements and on the Company s internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed 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. A company s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

New York, New York

February 21, 2013

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MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

	As of December 31 2012	2011
	(In thousands, except share and per share amounts)	
ASSETS		
Cash and cash equivalents	$ 128,908	$ 169,620
Securities available-for-sale	51,208	78,110
Accounts receivable, net of allowance of $75 and $1,086 as of December 31, 2012 and 2011, respectively	31,044	36,170
Deferred tax assets, net	9,442	8,089
Goodwill and intangible assets, net of accumulated amortization	33,134	34,544
Capitalized software, furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization	18,009	14,460
Prepaid expenses and other assets	8,096	8,465
Total assets	$ 279,841	$ 349,458
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities		
Accrued employee compensation	$ 19,916	$ 19,425
Deferred revenue	4,864	5,326
Accounts payable, accrued expenses and other liabilities	12,344	12,268
Total liabilities	37,124	37,019
Commitments and Contingencies (Note 12)		
Stockholders equity		
Preferred stock, $0.001 par value, 4,855,000 shares authorized, no shares issued and outstanding as of December 31, 2012 and 2011		
Series A Preferred Stock, $0.001 par value, 110,000 shares authorized, no shares issued and outstanding as of December 31, 2012 and 2011		
Common stock voting, $0.003 par value, 110,000,000 shares authorized, 38,902,294 shares and 37,725,394 shares issued and 37,407,135 shares and 36,183,655 shares outstanding as of December 31, 2012 and 2011, respectively	118	113
Common stock non-voting, $0.003 par value, 10,000,000 shares authorized, no shares and 2,585,654 shares issued and outstanding as of December 31, 2012 and 2011, respectively		9
Additional paid-in capital	283,609	340,716
Treasury stock Common stock voting, at cost, 1,495,159 shares and 1,541,739 shares as of December 31, 2012 and 2011, respectively	(32,273)	(25,933)
Accumulated deficit	(5,644)	(584)
Accumulated other comprehensive loss	(3,093)	(1,882)
Total stockholders equity	242,717	312,439
Total liabilities and stockholders equity	$ 279,841	$ 349,458

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

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MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended December 31,		
	2012	**2011**	**2010**
	(In thousands, except per share amounts)		
Revenues			
Commissions	$ 174,199	$ 155,444	$ 122,180
Technology products and services	12,351	14,310	13,648
Information and user access fees	7,435	7,199	6,681
Investment income	1,058	1,229	1,192
Other	3,161	2,917	2,527
Total revenues	198,204	181,099	146,228
Expenses			
Employee compensation and benefits	60,361	58,786	56,446
Depreciation and amortization	8,233	6,781	6,350
Technology and communications	12,766	10,912	9,982
Professional and consulting fees	13,081	10,138	8,503
Occupancy	3,012	2,921	2,997
Marketing and advertising	5,470	4,882	3,075
General and administrative	8,595	7,946	7,965
Total expenses	111,518	102,366	95,318
Income before income taxes	86,686	78,733	50,910
Provision for income taxes	26,617	31,029	19,482
Net income	$ 60,069	$ 47,704	$ 31,428
Net income per common share			
Basic	$ 1.65	$ 1.29	$ 0.86
Diluted	$ 1.59	$ 1.20	$ 0.80
Cash dividends declared per common share	$ 1.74	$ 0.36	$ 0.28
Weighted average shares outstanding			
Basic	36,516	37,006	33,159
Diluted	37,816	39,608	39,051

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

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MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

	Year Ended December 31,		
	2012	2011	2010
	(In thousands)		
Net income	$ 60,069	$ 47,704	$ 31,428
Cumulative translation adjustment and foreign currency exchange hedge, net of tax	(748)	(634)	(564)
Unrealized net (loss) gain on securities available-for-sale, net of tax	(463)	403	304
Comprehensive Income	$ 58,858	$ 47,473	$ 31,168

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

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MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY

	Commo Stock Voting	Commo Stock Non - Voting	Additional Paid-In Capital	Receivable for Common Stock Subscribed	Treasury Stock - Commo Stock Voting	Accumulated Deficit	Accumulated Other Comprehen-sive Loss	Total Stockholders Equity
					(In thousands)			
Balance at December 31, 2009	$ 104	$ 9	$ 313,896	$ (713)	$ (40,000)	$ (55,403)	$ (1,391)	$ 216,502
Net income						31,428		31,428
Cumulative translation adjustment and foreign currency exchange hedge, net of tax							(564)	(564)
Unrealized net gain on securities available-for-sale, net of tax							304	304
Stock-based compensation			8,969					8,969
Exercise of stock options	4		6,757					6,761
Withholding tax payments on restricted stock vesting and stock option exercises			(2,055)					(2,055)
Tax benefit from the exercise of warrants in prior years			11,429					11,429
Excess tax benefits from stock-based compensation			1,619					1,619
Repayment of promissory notes				713				713
Purchase of treasury stock					(30,000)			(30,000)
Cash dividend on common stock and Series B Preferred Stock						(10,630)		(10,630)
Balance at December 31, 2010	108	9	340,615		(70,000)	(34,605)	(1,651)	234,476
Net income						47,704		47,704
Cumulative translation adjustment and foreign currency exchange hedge, net of tax							(634)	(634)
Unrealized net gain on securities available-for-sale, net of tax							403	403
Stock-based compensation			6,859					6,859
Exercise of stock options	4		6,803					6,807
Withholding tax payments on restricted stock vesting and stock option exercises			(4,415)					(4,415)
Conversion of Series B Preferred stock to common stock voting	1		(20,688)		51,002			30,315
Tax benefit from the exercise of warrants in prior years			4,237					4,237
Excess tax benefits from stock-based compensation			7,305					7,305
Purchase of treasury stock					(6,935)			(6,935)
Cash dividend on common stock						(13,683)		(13,683)
Balance at December 31, 2011	113	9	340,716		(25,933)	(584)	(1,882)	312,439
Net income						60,069		60,069
Cumulative translation adjustment and foreign currency exchange hedge, net of tax							(748)	(748)
Unrealized net (loss) on securities available-for-sale, net of tax							(463)	(463)
Stock-based compensation			8,385					8,385
Exercise of stock options	3		8,522					8,525
			(20,003)					(20,003)

Withholding tax payments on restricted stock vesting and stock option exercises								
Excess tax benefits from stock-based compensation			14,775					14,775
Conversion of common stock non-voting to common stock voting	2	(2)	(15,878)		15,878			
Repurchases of common stock		(7)	(52,908)		(22,218)			(75,133)
Cash dividend on common stock						(65,129)		(65,129)
Balance at December 31, 2012	$ 118	$	$ 283,609	$	$ (32,273)	$ (5,644)	$ (3,093)	$ 242,717

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

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MARKETAXESS HOLDINGS INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31,		
	2012	2011	2010
	(In thousands)		
Cash flows from operating activities			
Net income	$ 60,069	$ 47,704	$ 31,428
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	8,233	6,781	6,350
Stock-based compensation expense	8,385	6,859	8,969
Deferred taxes	(643)	16,129	15,767
Provision for bad debts	519	1,177	602
Other	685		(411)
Changes in operating assets and liabilities:			
Decrease (increase) in accounts receivable	4,607	(11,665)	(3,134)
Decrease (increase) in prepaid expenses and other assets	412	(4,074)	57
Increase in accrued employee compensation	491	1,634	2,634
(Decrease) increase in deferred revenue	(462)	755	309
(Decrease) increase in accounts payable, accrued expenses and other liabilities	(714)	178	1,575
Net cash provided by operating activities	81,582	65,478	64,146
Cash flows from investing activities			
Securities available-for-sale:			
Proceeds from sales	23,663		15,377
Proceeds from maturities	18,313	27,419	49,988
Purchases	(16,543)	(32,302)	(66,008)
Securities and cash (provided) received as collateral	(43)	3,532	32
Purchases of furniture, equipment and leasehold improvements	(5,153)	(3,160)	(5,205)
Capitalization of software development costs	(5,207)	(4,065)	(1,904)
Net cash provided by (used in) investing activities	15,030	(8,576)	(7,720)
Cash flows from financing activities			
Cash dividend on common stock and Series B Preferred Stock	(64,041)	(13,683)	(10,630)
Exercise of stock options	8,525	6,807	6,761
Excess tax benefits from stock-based compensation	14,775	7,305	1,619
Withholding tax payments on restricted stock vesting and stock option exercises	(20,003)	(4,415)	(2,055)
Repurchase of common stock	(75,133)	(6,935)	(30,000)
Other	(298)	(278)	456
Net cash (used in) financing activities	(136,175)	(11,199)	(33,849)
Effect of exchange rate changes on cash and cash equivalents	(1,149)	(1,077)	(924)
Cash and cash equivalents			
Net (decrease) increase for the period	(40,712)	44,626	21,653
Beginning of period	169,620	124,994	103,341
End of period	$ 128,908	$ 169,620	$ 124,994

Supplemental cash flow information:

Cash paid during the year						
Cash paid for income taxes	$	15,102	$	10,177	$	2,228
Non-cash activity						
Conversion of Series B Preferred Stock to common stock	$		$	30,315	$	
Conversion of common stock non-voting to common stock voting		15,880				

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

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Principal Business Activity

MarketAxess Holdings Inc. (the Company) was incorporated in the State of Delaware on April 11, 2000. Through its subsidiaries, the Company operates an electronic trading platform for corporate bonds and other types of fixed-income instruments through which the Company s institutional investor clients can access the liquidity provided by its broker-dealer clients. The Company s multi-dealer trading platform allows its institutional investor clients to simultaneously request competitive, executable bids or offers from multiple broker-dealers, and to execute trades with the broker-dealer of their choice. The Company offers its clients the ability to trade U.S. high-grade corporate bonds, European high-grade corporate bonds, credit default swaps, agencies, high-yield and emerging markets bonds and asset-backed and preferred securities. The Company also executes certain bond transactions between and among institutional investor and broker-dealer clients on a riskless principal basis by serving as counterparty to both the buyer and the seller in matching back-to-back trades, which then settle through a third-party clearing organization. Through its Corporate BondTicker service, the Company provides fixed-income market data, analytics and compliance tools that help its clients make trading decisions. In addition, the Company provides FIX (Financial Information eXchange) message management tools, connectivity solutions and ancillary technology services that facilitate the electronic communication of order information between trading counterparties.

For 2011 and 2010, JPMorgan Chase & Co. (JPM) was the Company s sole stockholder broker-dealer client. During the first quarter of 2012, JPM sold its shares of the Company s common stock and is no longer considered a related party. See Note 8, Related Parties.

2. Significant Accounting Policies

Basis of Presentation

The consolidated financial statements include the accounts of the Company and its subsidiaries. All intercompany transactions and balances have been eliminated.

Cash and Cash Equivalents

Cash and cash equivalents includes cash and money market instruments that are primarily maintained at one major global bank. Given this concentration, the Company is exposed to certain credit risk. The Company defines cash equivalents as short-term interest-bearing investments with maturities at the time of purchase of three months or less.

Securities Available-for-Sale

The Company classifies its marketable securities as available-for-sale securities. Unrealized marketable securities gains and losses, net of taxes, are reflected as a net amount under the caption of accumulated other comprehensive loss on the Consolidated Statements of Financial Condition. Realized gains and losses are recorded in the Consolidated Statements of Operations in other revenues. For the purpose of computing realized gains and losses, cost is determined on a specific identification basis.

The Company assesses whether an other-than-temporary impairment loss on the investments has occurred due to declines in fair value or other market conditions. The portion of an other-than-temporary impairment related to credit loss is recorded as a charge in the Consolidated Statements of Operations. The remainder is recognized in other comprehensive loss if the Company does not intend to sell the security and it is more likely than not that the Company will not be required to sell the security prior to recovery. No charges for other-than-temporary losses were recorded during 2012, 2011 or 2010.

Fair Value Financial Instruments

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. A three-tiered hierarchy for determining fair value has been established that prioritizes inputs to valuation techniques used in fair value calculations. The three levels of inputs are defined as Level 1 (unadjusted quoted prices for identical assets or liabilities in active markets), Level 2 (inputs that are observable in the marketplace other than those inputs classified in Level 1) and Level 3 (inputs that are unobservable in the marketplace). The Company s financial assets and liabilities measured at fair value on a recurring basis consist of its money market funds, securities available-for-sale portfolio, one foreign currency forward contract and one foreign currency option contract.

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Allowance for Doubtful Accounts

All accounts receivable have contractual maturities of less than one year and are derived from trading-related fees and commissions and revenues from products and services. The Company continually monitors collections and payments from its customers and maintains an allowance for doubtful accounts. The allowance for doubtful accounts is based upon the historical collection experience and specific collection issues that have been identified. Additions to the allowance for doubtful accounts are charged to bad debt expense, which is included in general and administrative expense in the Company s Consolidated Statements of Operations.

The allowance for doubtful accounts was $0.1 million, $1.1 million and $0.4 million as of December 31, 2012, 2011 and 2010, respectively. The provision for bad debts was $0.5 million, $1.2 million and $0.6 million for the years ended December 31, 2012, 2011 and 2010, respectively. During the fourth quarter of 2011, MF Global Inc., a broker-dealer market maker on the Company s platform, entered a liquidation proceeding. In connection with the proceeding, the Company recorded a 100% allowance against outstanding receivables amounting to $0.9 million. Write-offs and other charges against the allowance for doubtful accounts were $1.4 million, $0.2 million and $0.7 million for the years ended December 31, 2012, 2011 and 2010, respectively.

Depreciation and Amortization

Fixed assets are carried at cost less accumulated depreciation. The Company uses the straight-line method of depreciation over three to seven years. Leasehold improvements are stated at cost and are amortized using the straight-line method over the lesser of the life of the improvement or the remaining term of the lease.

Software Development Costs

The Company capitalizes certain costs associated with the development of internal use software at the point at which the conceptual formulation, design and testing of possible software project alternatives have been completed. The Company capitalizes employee compensation and related benefits and third party consulting costs incurred during the preliminary software project stage. Once the product is ready for its intended use, such costs are amortized on a straight-line basis over three years. The Company reviews the amounts capitalized for impairment whenever events or changes in circumstances indicate that the carrying amounts of the assets may not be recoverable.

Cash Provided as Collateral

Cash is provided as collateral for electronic bank settlements and broker-dealer clearance accounts. Cash provided as collateral is included in prepaid expenses and other assets in the Consolidated Statements of Financial Condition.

Foreign Currency Translation and Forward Contracts

Assets and liabilities denominated in foreign currencies are translated using exchange rates at the end of the period; revenues and expenses are translated at average monthly rates. Gains and losses on foreign currency translation are a component of accumulated other comprehensive loss in the Consolidated Statements of Financial Condition. Transaction gains and losses are recorded in general and administrative expense in the Consolidated Statements of Operations.

The Company enters into foreign currency forward contracts to hedge its net investment in its U.K. subsidiary. Gains and losses on these transactions are included in accumulated other comprehensive loss on the Consolidated Statements of Financial Condition.

Revenue Recognition

The majority of the Company s revenues are derived from monthly distribution fees and commissions for trades executed on its platform that are billed to its broker-dealer clients on a monthly basis. The Company also derives revenues from technology products and services, information and user access fees, investment income and other income.

Commission revenue. Commissions are generally calculated as a percentage of the notional dollar volume of bonds traded on the platform and vary based on the type and maturity of the bond traded. Under the Company s transaction fee plans, bonds that are more actively traded or that have shorter maturities are generally charged lower commissions, while bonds that are less actively traded or that have longer maturities generally command higher commissions. For trades that the Company executes between and among institutional investor and broker-dealer clients on a riskless principal basis by serving as counterparty to both the buyer and the seller, the Company earns the commission through the difference in price between the two back-to-back trades. Fee programs for certain products include distribution fees which are recognized monthly.

MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Technology products and services. The Company generates revenues from technology software licenses, maintenance and support services (referred to as post-contract technical support or PCS) and professional consulting services. Revenue is generally recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable and collection is considered probable. The Company generally sells software licenses and PCS together as part of multiple-element arrangements. The Company also enters into contracts for technology integration consulting services unrelated to any software product.

For arrangements that include multiple elements, generally software licenses and PCS, the Company allocates and defers revenue for the undelivered items based on vendor specific objective evidence (VSOE) of the fair value of the undelivered elements and recognizes the difference between the total arrangement fee and the amount deferred for the undelivered items as license revenue. The Company s VSOE of each element is based on historical evidence of stand-alone sales of these elements to third parties or the stated renewal rate for the undelivered elements. When VSOE does not exist for undelivered items, the entire arrangement fee is recognized ratably over the performance period. For PCS, the term is typically one year and revenue is recognized over the duration of the arrangement on a straight-line basis.

Professional consulting services are generally separately priced and are typically not essential to the functionality of the Company s software products. Revenues from these services are recognized separately from the license fee. Generally, revenue from time-and-materials consulting contracts is recognized as services are performed.

Revenues from contracts for technology integration consulting services are recognized on the percentage-of-completion method. Percentage-of-completion accounting involves calculating the percentage of services provided during the reporting period compared to the total estimated services to be provided over the duration of the contract. If estimates indicate that a contract loss will occur, a loss provision is recorded in the period in which the loss first becomes probable and reasonably estimable. Contract losses are determined to be the amount by which the estimated direct and indirect costs of the contract exceed the estimated total revenues that will be generated by the contract. There were no contract loss provisions recorded as of December 31, 2012, 2011 and 2010. Revenues recognized in excess of billings are recorded as unbilled services within other assets. Billings in excess of revenues recognized are recorded as deferred revenues until revenue recognition criteria are met.

Initial set-up fees. The Company enters into agreements with its broker-dealer clients pursuant to which the Company provides access to its platform through a non-exclusive and non-transferable license. Broker-dealer clients may pay an initial set-up fee, which is typically due and payable upon execution of the broker-dealer agreement. The initial set-up fee, if any, varies by agreement. Revenue is recognized over the initial term of the agreement, which is generally two years. Initial set-up fees are reported in other income in the Consolidated Statements of Operations.

Stock-Based Compensation

The Company measures and recognizes compensation expense for all share-based payment awards based on their estimated fair values measured as of the grant date. These costs are recognized as an expense in the Consolidated Statements of Operations over the requisite service period, which is typically the vesting period, with an offsetting increase to additional paid-in capital.

Income Taxes

Income taxes are accounted for using the asset and liability method. Deferred income taxes reflect the net tax effects of temporary differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when such differences are expected to reverse. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is recognized against deferred tax assets if it is more likely than not that such assets will not be realized in future years. The Company recognizes interest and penalties related to unrecognized tax benefits in general and administrative expenses in the Consolidated Statements of Operations.

Business Combinations, Goodwill and Intangible Assets

Business acquisitions are accounted for under the purchase method of accounting. The total cost of an acquisition is allocated to the underlying net assets based on their respective estimated fair values. The excess of the purchase price over the estimated fair values of the net assets acquired is recorded as goodwill. Determining the fair value of certain assets acquired and liabilities assumed is judgmental in nature and often involves the use of significant estimates and assumptions, including assumptions with respect to future cash flows, discount rates, growth rates and asset lives.

MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

An impairment review of goodwill is performed on an annual basis and more frequently if circumstances change. Intangible assets with definite lives, including purchased technologies, customer relationships and other intangible assets, are amortized on a straight-line basis over their estimated useful lives, ranging from five to ten years. Intangible assets are assessed for impairment when events or circumstances indicate the existence of a possible impairment.

Earnings Per Share

For 2010, earnings per share (EPS) was calculated using the two-class method. Basic EPS is computed by dividing the net income attributable to common stock by the weighted-average number of shares of common stock outstanding for the period, including consideration of the two-class method to the extent that participating securities were outstanding during the period. Under the two-class method, undistributed net income is allocated to common stock and participating securities based on their respective right to share in dividends. The Series B Preferred Stock was convertible into shares of common stock and also included a right whereby, upon the declaration or payment of a dividend or distribution on the common stock, a dividend or distribution must also be declared or paid on the Series B Preferred Stock based on the number of shares of common stock into which such securities were convertible at the time. Due to these rights, the Series B Preferred Stock was considered a participating security requiring the use of the two-class method for the computation of basic EPS.

In January 2011, all of the shares of the Series B Preferred Stock were mandatorily and automatically converted into shares of common stock. For 2011 and 2012, basic EPS is computed by dividing the net income attributable to common stock by the weighted-average number of shares of common stock outstanding during the period.

Diluted EPS is computed using the more dilutive of the (a) if-converted method or (b) two-class method. Since the Series B Preferred Stock participated equally with the common stock in dividends and unallocated income, diluted EPS under the if-converted method was and is equivalent to the two-class method. The weighted-average shares outstanding of common stock reflects the dilutive effect that could occur if convertible securities or other contracts to issue common stock were converted into or exercised for common stock.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Recent Accounting Pronouncements

In 2011, the Financial Accounting Standards Board (FASB) issued new accounting guidance that simplifies goodwill impairment tests. The new guidance states that a qualitative assessment may be performed to determine whether further impairment testing is necessary. This accounting standard is effective for fiscal years beginning on or after December 15, 2011. The Company adopted the new guidance effective January 1, 2012 and there was no material impact on the Company s Consolidated Financial Statements.

In 2011, the FASB issued new disclosure guidance related to the presentation of the Statement of Comprehensive Income. This guidance eliminates the current option to report other comprehensive income and its components in the Consolidated Statement of Changes in Stockholders Equity. The requirement to present reclassification adjustments out of accumulated other comprehensive income on the face of the Consolidated Statement of Operations has been deferred. This accounting standard is effective for fiscal years beginning on or after December 15, 2011. The Company adopted the new guidance effective January 1, 2012 and has presented a separate Statement of Comprehensive Income in the Company s Consolidated Financial Statements.

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Net Capital Requirements and Customer Protection Requirements

MarketAxess Corporation, a U.S. subsidiary, is a registered broker-dealer with the Securities and Exchange Commission (SEC) and is a member of the Financial Industry Regulatory Authority (FINRA). MarketAxess Corporation claims exemption from SEC Rule 15c3-3, as it does not hold customer securities or funds on account, as defined. Pursuant to the Uniform Net Capital Rule under the Securities Exchange Act of 1934, MarketAxess Corporation is required to maintain minimum net capital, as defined, equal to the greater of $100,000 or 6 2/3% of aggregate indebtedness. MarketAxess Europe Limited, a U.K. subsidiary, is registered as a Multilateral Trading Facility dealer with the Financial Services Authority (FSA) in the U.K. MarketAxess Canada Limited, a Canadian subsidiary, is registered as an Alternative Trading System dealer under the Securities Act of Ontario and is a member of the Investment Industry Regulatory Organization of Canada. MarketAxess Europe Limited and MarketAxess Canada Limited are subject to certain financial resource requirements of the FSA and the Ontario Securities Commission, respectively. The following table sets forth the capital requirements, as defined, that the Company s subsidiaries were required to maintain as of December 31, 2012:

	MarketAxess Corporation	MarketAxess Europe Limited (In thousands)	MarketAxess Canada Limited
Net capital	$ 63,624	$ 13,151	$ 479
Minimum net capital required	2,266	2,943	277
Excess net capital	$ 61,358	$ 10,208	$ 202

The Company s regulated subsidiaries are subject to U.S., U.K. and Canadian regulations which prohibit repayment of borrowings from the Company or affiliates, paying cash dividends, making loans to the Company or affiliates or otherwise entering into transactions that result in a significant reduction in regulatory net capital or financial resources, respectively, without prior notification to or approval from such regulated entity s principal regulator.

4. Fair Value Measurements

The following table summarizes the valuation of the Company s assets and liabilities measured at fair value as categorized based on the hierarchy described in Note 2.

	Level 1	Level 2 (In thousands)	Level 3	Total
As of December 31, 2012				
Money market funds	$ 83,519	$	$	$ 83,519
Securities available-for-sale				
U.S. government obligations		31,104		31,104
Municipal securities		17,947		17,947
Corporate bonds		2,157		2,157
Foreign currency forward and option contracts		15		15
	$ 83,519	$ 51,223	$	$ 134,742
As of December 31, 2011				

Money market funds	$ 111,256	$	$	$ 111,256
Securities available-for-sale				
U.S. government obligations		55,460		55,460
Municipal securities		20,612		20,612
Corporate bonds		2,038		2,038
Foreign currency forward contract		155		155
	$ 111,256	$ 78,265	$	$ 189,521

Securities classified within Level 2 were valued using a market approach utilizing prices and other relevant information generated by market transactions involving comparable assets. The foreign currency forward and options contracts are classified within Level 2 as the valuation inputs are based on quoted market prices. There were no financial assets classified within Level 3 during 2012 and 2011.

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company enters into foreign currency forward contracts to hedge the exposure to variability in foreign currency cash flows resulting from the net investment in the Company s U.K. subsidiary. The Company assesses each foreign currency forward contract to ensure that it is highly effective at reducing the exposure being hedged. The Company designates each foreign currency forward contract as a hedge, assesses the risk management objective and strategy, including identification of the hedging instrument, the hedged item and the risk exposure and how effectiveness is to be assessed prospectively and retrospectively. These hedges are for a one-month period and are used to limit exposure to foreign currency exchange rate fluctuations. Gains or losses on foreign currency forward contracts designated as hedges are included in accumulated other comprehensive loss in the Consolidated Statements of Financial Condition. The gross and net fair value liability as of December 31, 2012 is included in accounts payable and the gross and net fair value asset as of December 31, 2011 is included in accounts receivable, in the Consolidated Statements of Financial Condition.

A summary of the foreign currency forward contracts is as follows:

	As of December 31, 2012	As of December 31, 2011
	(In thousands)	
Notional value	$ 15,792	$ 28,671
Fair value of notional	15,809	28,516
Gross and net fair value (liability) asset	$ (17)	$ 155

In October 2012, the Company purchased a foreign exchange call option to economically hedge the £26.0 million purchase price of Xtrakter Limited (Xtrakter) (See Note 16, Acquisition). As of December 31, 2012, the fair value of the call option was $32,000. A mark-to-market loss of $0.3 million was included in general and administrative expense in the Consolidated Statement of Operations for the year ended December 31, 2012.

The following is a summary of the Company s securities available-for-sale:

	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
As of December 31, 2012				
U.S. government obligations	$ 30,255	$ 849	$	$ 31,104
Municipal securities	17,941	10	(4)	17,947
Corporate bonds	2,159		(2)	2,157
Total securities available-for-sale	$ 50,355	$ 859	$ (6)	$ 51,208
As of December 31, 2011				
U.S. government obligations	$ 53,832	$ 1,628	$	$ 55,460
Municipal securities	20,613	7	(8)	20,612
Corporate bonds	2,028	10		2,038
Total securities available-for-sale	$ 76,473	$ 1,645	$ (8)	$ 78,110

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table summarizes the contractual maturities of securities available-for-sale:

	As of December 31, 2012	As of December 31, 2011
	(In thousands)	
Less than one year	$ 10,870	$ 31,554
Due in 1 5 years	40,338	46,556
Total securities available-for-sale	$ 51,208	$ 78,110

Proceeds from the sales and maturities of securities available-for-sale during 2012, 2011 and 2010 were $42.0 million, $27.4 million and $65.4 million, respectively.

The following table provides fair values and unrealized losses on securities available-for-sale and by the aging of the securities continuous unrealized loss position:

	Less than Twelve Months		Twelve Months or More		Total	
	Estimated fair value	Gross unrealized losses	Estimated fair value	Gross unrealized losses	Estimated fair value	Gross unrealized losses
			(In thousands)			
As of December 31, 2012						
U.S. government obligations	$	$	$	$	$	$
Municipal securities	2,780	(4)			2,780	(4)
Corporate bonds	2,157	(2)			2,157	(2)
Total	$ 4,937	$ (6)	$	$	$ 4,937	$ (6)
As of December 31, 2011						
U.S. government obligations	$	$	$	$	$	$
Municipal securities	9,529	(8)			9,529	(8)
Corporate bonds						
Total	$ 9,529	$ (8)	$	$	$ 9,529	$ (8)

5. Goodwill and Intangible Assets

Goodwill and intangible assets principally relate to the acquisitions of Greenline Financial Technologies, Inc. (Greenline) in 2008 and Trade West Systems, LLC in 2007. Goodwill was $31.8 million as of both December 31, 2012 and December 31, 2011. Intangible assets that are subject to amortization, including the related accumulated amortization, are comprised of the following:

December 31, 2012		December 31, 2011	
Accumulated	Net Carrying	Accumulated	Net Carrying

	Cost	Amortization	Amount	Cost	Amortization	Amount
			(In thousands)			
Technology	$ 4,010	$ (3,892)	$ 118	$ 4,010	$ (3,202)	$ 808
Customer relationships	3,530	(2,364)	1,166	3,530	(1,999)	1,531
Non-competition agreements	1,260	(1,214)	46	1,260	(962)	298
Tradenames	590	(570)	20	590	(467)	123
Total	$ 9,390	$ (8,040)	$ 1,350	$ 9,390	$ (6,630)	$ 2,760

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Amortization expense associated with identifiable intangible assets was $1.4 million and $1.5 million, respectively, for the years ended December 31, 2012 and 2011. Estimated total amortization expense is $0.5 million for 2013, $0.3 million for 2014, $0.2 million for each of 2015 and 2016 and $0.1 million for 2017.

6. Capitalized Software, Furniture, Equipment and Leasehold Improvements

Capitalized software development costs, furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization, are comprised of the following:

	As of December 31,	
	2012	2011
	(In thousands)	
Software development costs	$ 29,662	$ 24,440
Computer hardware and related software	15,702	11,126
Office hardware	2,125	1,832
Furniture and fixtures	1,479	1,446
Leasehold improvements	4,709	4,667
Computer hardware under capital lease	1,419	1,419
Accumulated depreciation and amortization	(37,087)	(30,470)
Total capitalized software, furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization	$ 18,009	$ 14,460

During the years ended December 31, 2012, 2011 and 2010, software development costs totaling $5.2 million, $4.1 million and $1.9 million, respectively, were capitalized. Non-capitalized software costs and routine maintenance costs are expensed as incurred and are included in employee compensation and benefits and professional and consulting fees in the Consolidated Statements of Operations.

7. Income Taxes

The provision for income taxes consists of the following:

	Year Ended December 31,		
	2012	2011	2010
		(In thousands)	
Current:			
Federal	$ 12,981	$ 3,605	$
State and local	2,138	2,793	355
Foreign	1,315	1,194	1,348
Total current provision	16,434	7,592	1,703
Deferred:			
Federal	8,951	20,531	14,494
State and local	1,238	2,890	3,170
Foreign	(6)	16	115

Total deferred provision	10,183	23,437	17,779
Provision for income taxes	$ 26,617	$ 31,029	$ 19,482

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Pre-tax income from U.S. operations was $82.0 million, $74.3 million and $46.1 million for the years ended December 31, 2012, 2011 and 2010, respectively. Pre-tax income from foreign operations was $4.7 million, $4.4 million and $4.8 million for the years ended December 31, 2012, 2011 and 2010, respectively.

The difference between the Company s reported provision for income taxes and the U.S. federal statutory rate of 35% is as follows:

	Year Ended December 31,		
	2012	2011	2010
U.S. federal tax at statutory rate	35.0%	35.0%	35.0%
State and local taxes net of federal benefit	2.4	5.2	4.6
Release of previously unrecognized tax benefits	(7.8)		
Other, net	1.1	(0.8)	(1.4)
Provision for income taxes	30.7%	39.4%	38.3%

The following is a summary of the Company s net deferred tax assets:

	As of December 31,	
	2012	2011
	(In thousands)	
Deferred tax assets		
U.S net operating loss carryforwards	$ 7,175	$ 4,589
Foreign net operating loss carryforwards	160	165
Stock compensation expense	5,296	5,312
Other	2,839	3,280
Total deferred tax assets	15,470	13,346
Valuation allowance	(727)	(287)
Net deferred tax assets	14,743	13,059
Deferred tax liabilities		
Depreciation and amortization	(2,025)	(1,905)
Capitalized software development costs	(2,752)	(1,980)
Intangible assets	(524)	(1,085)
Deferred tax assets, net	$ 9,442	$ 8,089

As of December 31, 2012, the Company had deferred tax assets associated with stock-based compensation of approximately $5.3 million. There is a risk that the ultimate tax benefit realized upon the exercise of stock options or vesting of restricted stock could be less than the tax benefit previously recognized and exhaust the additional-paid-in-capital pool. If this should occur, any excess tax benefit previously recognized would be reversed, resulting in an increase in tax expense. Since the tax benefit to be realized in the future is unknown, it is not currently possible to estimate the impact on the deferred tax balance. As of December 31, 2012, the additional paid-in-capital pool, which is determined under a one pool approach for employee and non-employee awards, was approximately $42.9 million. The additional paid-in-capital pool is currently sufficient to absorb a complete write-off of the stock-based compensation deferred tax asset.

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

As of December 31, 2012, the Company had restricted U.S. federal net operating loss carryforwards of approximately $17.1 million, which begin to expire in 2021, and $0.7 million of foreign loss carryforwards, which begin to expire in 2025. In 2001 and 2000, MarketAxess Holdings Inc. and MarketAxess Corporation had an ownership change within the meaning of Section 382 of the Internal Revenue Code. Net operating loss carryforwards relating to this ownership change were $25.6 million as of December 31, 2012 of which $10.6 million is deemed utilizable and recognized as a net operating loss carryforward. Greenline experienced an ownership change within the meaning of Section 382 of the Internal Revenue Code in 2008. The Company does not believe that this ownership change significantly impacts the ability to utilize acquired net operating loss carryforwards, which amounted to $6.5 million as of December 31, 2012. In addition, the Company s net operating loss carryforwards may be subject to additional annual limitations if there is a 50% or greater change in the Company s ownership, as determined over a rolling three-year period.

The Company issued warrants to certain broker-dealer stockholders at the time that they made an equity investment in the Company. All of the warrants were exercised prior to 2008. Through December 31, 2009, the tax benefit on a portion of the tax deduction generated on the exercise of the warrants had not yet been recorded. During 2010, the Company recognized a portion of the tax benefits amounting to $11.4 million as an increase to additional paid-in-capital due to the utilization of the related tax loss carryforwards of $31.0 million. During the first quarter of 2011, the Company recognized the remaining portion of the tax benefit, amounting to $4.2 million, as an increase to additional paid-in-capital due to the expected utilization of the related tax loss carryforwards of $10.4 million.

The ultimate realization of deferred income tax assets is dependent upon the generation of future taxable income during the periods in which the temporary differences become deductible. If it is not more likely than not that some portion or all of the gross deferred income tax assets will be realized in future years, a valuation allowance is recorded. As of December 31, 2012, the valuation allowance relates to certain foreign and state tax loss carryforwards that are not expected to be realized. A summary of the changes in the valuation allowance follows:

	Year Ended December 31,		
	2012	2011	2010
	(In thousands)		
Valuation allowance at beginning of year	$ 287	$ 249	$ 666
Increase (decrease) to valuation allowance attributable to:			
Net operating losses	440	38	(132)
Tax credits			(285)
Valuation allowance at end of year	$ 727	$ 287	$ 249

The Company or one of its subsidiaries files U.S. federal, state and foreign income tax returns. No income tax returns have been audited, with the exception of New York city (through 2003) and state (through 2006) and Connecticut state (through 2003) tax returns. An examination of the Company s New York state franchise tax returns for 2007 through 2009 is currently underway. The Company cannot estimate when the examination will conclude.

In the fourth quarter of 2012, the Company recorded a reduction to the income tax provision of $6.7 million. The Company updated the recognition of certain acquired net operating loss carryforwards in response to a private letter ruling received from the Internal Revenue Service. As a result, the reserve for unrecognized tax benefits amounting to $3.6 million was reversed and deferred tax assets were increased by $3.1 million to recognize additional tax loss carryforwards. A reconciliation of the unrecognized tax benefits is as follows (in thousands):

	Year Ended December 31,		
	2012	2011	2010
	(In thousands)		
Balance at beginning of year	$ 3,647	$ 3,329	$ 2,924

Additions for tax positions of prior years		366	277
Additions for tax positions of current year			128
Reductions for tax positions of prior years	(3,598)	(48)	
Balance at end of year	$ 49	$ 3,647	$ 3,329

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

8. Related Parties

On February 28, 2012, the Company completed a registered underwritten secondary public offering of 3,597,333 shares of common stock held by JPM. The Company did not receive any of the proceeds of the offering. In addition, the Company repurchased 1,821,730 shares of non-voting common stock held by JPM (see Note 9, Stockholders Equity). After February 28, 2012, JPM no longer holds shares of common stock in the Company and is not considered a related party.

The Company generates commissions, technology products and services revenues, information and user access fees, investment income and other income and related accounts receivable balances from JPM and its affiliates. In addition, JPM acts in a custodial and cash management capacity for the Company. The Company also maintains an account with and paid commissions to JPM in connection with the Company s share repurchase program. The Company also incurs bank fees in connection with these arrangements. As of the dates and for the periods indicated below, the Company had the following balances and transactions with JPM and its affiliates:

	As of December 31, 2011 (In thousands)
Cash and cash equivalents	$ 156,982
Securities and cash provided as collateral	550
Accounts receivable	2,255
Accounts payable	86

	Year Ended December 31,		
	2012	2011	2010
	(In thousands)		
Commissions	$ 1,480	$ 7,045	$ 5,541
Technology products and services	35	167	16
Information and user access fees	24	176	132
Investment income	20	90	113
Other income	11	66	63
General and administrative	7	73	27

9. Stockholders Equity

Common Stock

As of December 31, 2012 and 2011, the Company had 110,000,000 authorized shares of common stock and 10,000,000 authorized shares of non-voting common stock. Common stock entitles the holder to one vote per share of common stock held.

In June 2010, the Board of Directors of the Company authorized a share repurchase program for up to $30.0 million of the Company s common stock. The share repurchase program was completed in December 2010. A total of 1,939,620 shares were repurchased at an aggregate cost of $30.0 million over the life of the repurchase program. Shares repurchased under the program are held in treasury for future use.

In October 2011, the Board of Directors of the Company authorized a share repurchase program for up to $35.0 million of the Company s common stock. As of December 31, 2012, a total of 955,342 shares were repurchased at an aggregate cost of $29.2 million, including 717,344 shares repurchased in 2012. Shares repurchased under the program will be held in treasury for future use. The share repurchase program has an expiration date of January 1, 2014.

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

On February 28, 2012, the Company repurchased 1,821,730 shares of the Company s non-voting common stock from JPM at a cost of $52.9 million. Shares repurchased from JPM were cancelled by the Company. JPM also converted 763,924 shares of non-voting common stock to voting common stock on February 28, 2012.

Series B Preferred Stock Conversion

In 2008, the Company entered into a Securities Purchase Agreement (the Purchase Agreement) with two funds managed by Technology Crossover Ventures (the Purchasers), pursuant to which the Company sold to the Purchasers (i) 35,000 shares of the Company s Series B Preferred Stock, which shares were convertible into an aggregate of 3,500,000 shares of common stock, and (ii) warrants (the Warrants and, together with the Series B Preferred Stock, the Securities) to purchase an aggregate of 700,000 shares of common stock at an exercise price of $10.00 per share, for an aggregate purchase price of $35.0 million. The net proceeds, after the placement agent fee and legal fees, were $33.5 million. The Warrants were exercisable for cash or on a net exercise basis. The Warrants were to expire on the tenth anniversary of the date they were first issued and were subject to customary anti-dilution adjustments in the event of stock splits, reverse stock splits, stock dividends and similar transactions.

The shares of Series B Preferred Stock were convertible at any time by the holders thereof at a conversion price of $10.00 per share, subject to certain anti-dilution adjustments and also were subject to automatic conversion into shares of common stock if the closing price of the common stock was at least $17.50 on each trading day for a period of 65 consecutive trading days. In January 2011, all of the shares of the Series B Preferred Stock were mandatorily and automatically converted into 3,499,999 shares of common stock. In November 2011, a total of 455,465 shares of common stock were issued upon the exercise of the Warrants on a net exercise basis.

Dividends

The Company initiated a regular quarterly dividend in the fourth quarter of 2009. In January 2013, the Company s Board of Directors approved a quarterly cash dividend of $0.13 per share payable on February 28, 2013 to stockholders of record as of the close of business on February 14, 2013. On December 27, 2012, the Company paid a special dividend of $1.30 per share. Any future declaration and payment of dividends will be at the sole discretion of the Company s Board of Directors. The Board of Directors may take into account such matters as general business conditions, the Company s financial results, capital requirements, contractual, legal, and regulatory restrictions on the payment of dividends to the Company s stockholders or by the Company s subsidiaries to the parent and any such other factors as the Board of Directors may deem relevant.

10. Stock-Based Compensation Plans

The Company has two stock incentive plans which provide for the grant of stock options, stock appreciation rights, restricted stock, performance shares, performance units, or other stock-based awards as incentives and rewards to encourage employees, consultants and non-employee directors to participate in the long-term success of the Company. As of December 31, 2012, there were 5,116,163 shares available for grant under the stock incentive plans.

Total stock-based compensation expense was as follows:

	Year Ended December 31,		
	2012	2011	2010
		(In thousands)	
Employee:			
Restricted stock and performance shares	$ 7,046	$ 5,856	$ 6,588
Stock options	668	324	1,728

	7,714	6,180	8,316
Non-employee directors:			
Restricted stock	671	679	570
Stock options			83
	671	679	653
Total stock-based compensation	$ 8,385	$ 6,859	$ 8,969

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company records stock-based compensation expense for employees in employee compensation and benefits and for non-employee directors in general and administrative expenses in the Consolidated Statements of Operations.

Stock Options

The exercise price of each option granted is equal to the market price of the Company s common stock on the date of grant. Generally, option grants have provided for vesting over a three or five-year period. Options expire ten years from the date of grant. The fair value of each option award is estimated on the date of grant using the Black-Scholes option-pricing model. The determination of fair value of share-based payment awards on the date of grant using an option-pricing model is affected by the Company s stock price as well as assumptions regarding a number of highly complex and subjective variables, including the expected stock price volatility over the term of the awards, the risk-free interest rate and the expected term. Expected volatilities are based on historical volatility of the Company s stock and a peer group. The risk-free interest rate is based on U.S. Treasury securities with a maturity value approximating the expected term of the option. The expected term represents the period of time that options granted are expected to be outstanding based on actual and projected employee stock option exercise behavior.

The weighted-average fair value for options granted during 2012, 2011 and 2010 was $12.26, $11.29 and $5.45, respectively. The following table represents the assumptions used for the Black-Scholes option-pricing model to determine the per share weighted-average fair value for options granted for the three years ended December 31, 2012:

	2012	2011	2010
Expected life (years)	5.0	9.9	5.0
Risk-free interest rate	0.7%	3.3%	2.2%
Expected volatility	48.2%	48.0%	50.0%
Expected dividend yield	1.2%	1.3%	2.0%

The following table reports stock option activity during the three years ended December 31, 2012 and the intrinsic value as of December 31, 2012:

	Number of Shares	Weighted-Average Exercise Price	Remaining Contractual Term	Intrinsic Value (In thousands)
Outstanding at December 31, 2009	5,166,558	$ 9.10		
Granted	8,239	$ 14.10		
Canceled	(12,575)	$ 13.85		
Exercised	(758,660)	$ 9.17		
Outstanding at December 31, 2010	4,403,562	$ 9.09		
Granted	340,771	$ 21.60		
Canceled	(211,323)	$ 16.16		
Exercised	(1,605,273)	$ 10.21		
Outstanding at December 31, 2011	2,927,737	$ 9.42	8.1	
Granted	13,292	$ 32.45		
Canceled		$		
Exercised	(1,511,207)	$ 5.64		$ 41,310

Outstanding at December 31, 2012	1,429,822	$	13.62	4.5	$	31,002
Exercisable at December 31, 2012	1,214,099	$	12.10	4.0	$	28,172

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The intrinsic value is the amount by which the closing price of the Company s common stock on December 31, 2012 of $35.30 or the price on the day of exercise exceeds the exercise price of the stock options multiplied by the number of shares. As of December 31, 2012, there was $1.8 million of total unrecognized compensation cost related to non-vested stock options. That cost is expected to be recognized over a weighted-average period of 3.0 years.

Restricted Stock and Performance Shares

Shares of restricted stock generally vest over a period of three years. Compensation expense is measured at the grant date and recognized ratably over the vesting period. Performance share awards are granted to certain senior managers. Each performance share award is earned or forfeited based on the level of achievement by the Company of pre-tax operating income on a per share basis before performance share and cash bonus expense. The pay-out ranges from zero to 150% of the performance share award. For each performance share earned, a participant is awarded an equal number of shares of restricted stock. Any restricted stock awarded to a participant vests and ceases to be restricted stock in two equal installments on each of the second and third anniversaries of the date of grant of the applicable performance share award. Compensation expense for performance shares is measured at the grant date and recognized on a graded basis over the vesting period. The pay-out achievement was 92.5%, 146% and 150% of the performance award for 2012, 2011 and 2010, respectively. The following table reports performance share activity for the three years ended December 31, 2012:

	2012	2011	2010
Performance year			
Share pay-out at plan, net of forfeitures of 14,563 for 2011	44,843	63,102	87,035
Actual share pay-out in following year	41,481	94,653	130,552
Fair value per share on grant date	$ 30.64	$ 21.56	$ 14.29

The following table reports restricted stock and performance share activity during the three years ended December 31, 2012:

	Number of Restricted Shares	Weighted-Average Grant Date Fair Value
Outstanding at December 31, 2009	1,034,139	$ 9.64
Granted	549,264	
Performance share pay-out	206,664	
Canceled	(71,152)	
Vested	(474,051)	
Outstanding at December 31, 2010	1,244,864	$ 11.23
Granted	435,548	
Performance share pay-out	130,552	
Canceled	(279,081)	
Vested	(574,172)	
Outstanding at December 31, 2011	957,711	$ 15.69
Granted	206,965	
Performance share pay-out	91,498	
Canceled	(7,390)	
Vested	(459,474)	

Outstanding at December 31, 2012	789,310	$	21.88

As of December 31, 2012, there was $9.7 million of total unrecognized compensation expense related to non-vested restricted stock and performance shares. That cost is expected to be recognized over a weighted-average period of 1.7 years.

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

11. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per common share:

	Year Ended December 31,		
	2012	2011	2010
	(In thousands, except per share amounts)		
Basic EPS			
Net income	$ 60,069	$ 47,704	$ 31,428
Amount allocable to common shareholders	100.0%	100.0%	90.5%
Net income applicable to common stock	$ 60,069	$ 47,704	$ 28,427
Common stock voting	36,101	34,420	30,573
Common stock non-voting	415	2,586	2,586
Basic weighted average shares outstanding	36,516	37,006	33,159
Basic earnings per share	$ 1.65	$ 1.29	$ 0.86
Diluted EPS			
Net income	$ 60,069	$ 47,704	$ 31,428
Basic weighted average shares outstanding	36,516	37,006	33,159
Effect of dilutive shares:			
Series B Preferred Stock			3,500
Stock options, restricted stock and warrants	1,300	2,602	2,392
Diluted weighted average shares outstanding	37,816	39,608	39,051
Diluted earnings per share	$ 1.59	$ 1.20	$ 0.80

Stock options, restricted stock and warrants totaling 0.1 million shares, 0.3 million shares and 0.4 million shares for the years ended December 31, 2012, 2011 and 2010, respectively, were excluded from the computation of diluted earnings per share because their effect would have been antidilutive. The computation of diluted shares can vary among periods due, in part, to the change in the average price of the Company s common stock.

12. Commitments and Contingencies

The Company leases office space and equipment under non-cancelable lease agreements expiring at various dates through 2022. Office space leases are subject to escalation based on certain costs incurred by the landlord. Minimum rental commitments as of December 31, 2012 under such operating and capital leases were as follows:

	Operating Leases	Capital Leases

Year Ending December 31,	(In thousands)	
2013	$ 1,796	$ 322
2014	1,763	42
2015	2,026	
2016	2,039	
2017	2,952	
2018 and thereafter	7,255	
Minimum lease payments	17,831	364
Less amount representing interest		15
	$ 17,831	$ 349

MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Rental expense for the years ended December 31, 2012, 2011 and 2010 was $2.6 million, $2.5 million and $2.7 million, respectively, and is included in occupancy expense in the Consolidated Statements of Operations. Rental expense has been recorded based on the total minimum lease payments after giving effect to rent abatement and concessions, which are being amortized on a straight-line basis over the life of the lease. The Company is contingently obligated for standby letters of credit amounting to $1.5 million that were issued to landlords for office space.

In 2008, the Company assigned the lease agreement on a leased property to a third party. The Company is contingently liable should the assignee default on future lease obligations through the November 2015 lease termination date. The aggregate amount of future lease obligations under this arrangement is $1.1 million as of December 31, 2012.

The Company, through two regulated subsidiaries, executes certain bond transactions between and among institutional investor and broker-dealer clients on a riskless principal basis by serving as counterparty to both the buyer and the seller in matching back-to-back trades, which are then settled through a third-party clearing organization. The Company acts as intermediary on a riskless principal basis in these bond transactions by serving as counterparty to the two clients involved. Settlement typically occurs within one to three trading days after the trade date. Cash settlement of the transaction occurs upon receipt or delivery of the underlying instrument that was traded. Under securities clearing agreements with the independent third party, the Company maintains a collateral deposit with the clearing broker in the form of cash. As of December 31, 2012, the amount of the collateral deposit included in securities and cash provided as collateral in the Consolidated Statements of Financial Condition was $0.9 million. The Company is exposed to credit risk in the event a counterparty does not fulfill its obligation to complete a transaction. Pursuant to the terms of the securities clearing agreements between the Company and the independent clearing broker, the clearing broker has the right to charge the Company for losses resulting from a counterparty s failure to fulfill its contractual obligations. The losses are not capped at a maximum amount and apply to all trades executed through the clearing broker. At December 31, 2012, the Company had not recorded any liabilities with regard to this right.

In the normal course of business, the Company enters into contracts that contain a variety of representations, warranties and general indemnifications. The Company s maximum exposure under these arrangements is unknown, as this would involve future claims that may be made against the Company that have not yet occurred. However, based on experience, the Company expects the risk of loss to be remote.

13. Segment Information

As an electronic multi-dealer platform for the trading of fixed-income securities, the Company s operations constitute a single business segment. Because of the highly integrated nature of the financial markets in which the Company competes and the integration of the Company s worldwide business activities, the Company believes that results by geographic region or client sector are not necessarily meaningful in understanding its business.

14. Retirement Savings Plans

The Company, through its U.S. and U.K. subsidiaries, offers its employees the opportunity to invest in defined contribution plans. For the years ended December 31, 2012, 2011 and 2010, the Company contributed $1.1 million, $1.2 million and $0.9 million, respectively, to the plans.

15. Customer Concentration

During the years ended December 31, 2012, 2011 and 2010, no single client accounted for more than 10% of total revenue. One institutional investor client accounted for approximately 13.5%, 14.6% and 15.8% of trading volumes during the years ended December 31, 2012, 2011 and 2010, respectively. This institutional investor client also beneficially owns approximately 7% of the outstanding shares of the Company s common stock.

16. Acquisition

On October 26, 2012, the Company entered into an agreement to acquire all of the outstanding shares of Xtrakter from Euroclear S.A./N.V. Xtrakter is a U.K.-based provider of regulatory transaction reporting, financial market data and trade matching services to the European securities markets. The acquisition of Xtrakter will provide the Company with an expanded set of technology solutions ahead of incoming regulatory mandates from Europe.

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MARKETAXESS HOLDINGS INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The aggregate purchase price is £26.0 million (approximately $40.5 million) in cash, plus transaction costs, and is subject to a post-closing adjustment based on the net working capital of Xtrakter on the closing date. The purchase price will be funded from available cash on hand. The Company received FSA approval of the change in control on February 18, 2013 and expects to complete the acquisition of Xtrakter on or about February 28, 2013.

17. Subsequent Events

Credit Facility

On January 14, 2013, the Company entered into a three-year credit agreement (Credit Agreement) which provides for revolving loans and letters of credit up to an aggregate of $50.0 million (Credit Facility). Subject to satisfaction of certain specified conditions, the Company is permitted to upsize the Credit Facility by an additional $50.0 million in total.

Borrowings under the Credit Facility will bear interest at a rate per annum equal to either of the following, as designated by the Company for each borrowing: (A) the sum of (i) the greatest of (a) the prime rate, as defined, (b) the federal funds effective rate plus 0.50% and (c) one month adjusted LIBOR plus 1.00% plus (ii) 0.50% or (B) the sum of (i) adjusted LIBOR plus (ii) 1.50%. Default interest is 2.00% per annum in excess of the rate otherwise applicable in the case of any overdue principal or any other overdue amount. The Company is also required to pay a commitment fee to the lenders under the Credit Facility in respect of unutilized revolving loan commitments at a rate of 0.30% per annum.

The Company s existing and future domestic subsidiaries (other than any broker-dealer subsidiary) have guaranteed the Company s obligations under the Credit Agreement. Subject to customary exceptions and exclusions, the Credit Facility is collateralized by first priority pledges (subject to permitted liens) of substantially all of the Company s personal property assets and the personal property assets of the Company s domestic subsidiaries that have guaranteed the Credit Facility, including the equity interests of the Company s domestic subsidiaries and the equity interests of certain of the Company s foreign subsidiaries (limited, in the case of the voting equity interests of the foreign subsidiaries, to a pledge of 65% of those equity interests). Each of the Company and the guarantors will also be required to provide mortgages on any real property owned by it.

The Credit Agreement requires that the Company s consolidated total leverage ratio tested on the last day of each fiscal quarter not exceed 2.5 to 1.0. The Credit Agreement also requires that the Company s consolidated interest coverage ratio tested on the last day of each fiscal quarter not exceed 3.5 to 1.0.

If an event of default occurs, including failure to pay principal or interest due on the loan balance, a voluntary or involuntary proceeding seeking liquidation, change in control of the Company, or one or more judgments against the Company in excess of $10 million, the lenders would be entitled to accelerate the facility and take various other actions, including all actions permitted to be taken by a secured creditor. If certain bankruptcy events of default occur, the facility will automatically accelerate.

Employee Matter

The Company assesses its liabilities and contingencies in connection with outstanding legal proceedings, if any, utilizing the latest information available. For matters where it is probable that the Company will incur a material loss and the amount can be reasonably estimated, the Company would establish an accrual for the loss. Once established, the accrual would be adjusted to reflect any relevant developments. When a loss contingency is not both probable and estimable, the Company does not establish an accrual.

On January 2, 2013, a former employee of the Company filed a complaint against the Company with the U.S. Department of Labor alleging retaliatory employment practices in violation of the whistleblower provisions of the Sarbanes-Oxley Act. The relief sought includes, among other things, reinstatement, back pay and compensatory and punitive damages.

The Company believes the complaint is without merit and intends to vigorously defend itself against the allegations. Given the preliminary stage and the inherent uncertainty of the potential outcome of such proceedings, the Company cannot estimate the reasonably possible range of loss at this time. Based on the available information, the Company believes that the low end of the reasonably possible range of loss is zero and, accordingly, no loss accrual has been provided in the Company s accompanying financial statements.

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Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.***

None.

Item 9A. ***Controls and Procedures.***

Our management, including the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures, as that term is defined in Rule 13a-15(e) and Rule 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act), as of December 31, 2012. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective to ensure that information required to be disclosed by MarketAxess in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms, and to ensure that information is accumulated and communicated to our management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) and Rule 15d-15(f) under the Exchange Act) during the quarter ended December 31, 2012 identified in connection with the evaluation thereof by our management, including the Chief Executive Officer and Chief Financial Officer, that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Management s annual report on internal control over financial reporting and the report of our independent registered public accounting firm appears in Part II, Item 8. Financial Statements and Supplementary Data of this Annual Report on Form 10-K.

Item 9B. ***Other Information.***

None.

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PART III

Item 10. ***Directors, Executive Officers and Corporate Governance.***

The information required by this item is incorporated herein by reference to the sections entitled Proposal 1 Election of Directors, Corporate Governance and Board Matters, Executive Officers and Other Matters Section 16(a) beneficial ownership reporting compliance in the Company s definitive Proxy Statement (the Proxy Statement) for the Annual Meeting of Stockholders to be held in the second quarter of 2013. The Company intends to file the Proxy Statement within 120 days after the end of its fiscal year (i.e., on or before April 30, 2013). The Company s Code of Conduct applicable to directors and all employees, including senior financial officers, is available on the Company s website at www.marketaxess.com. If the Company makes any amendments to its Code of Conduct that is required to be disclosed pursuant to the Exchange Act, the Company will make such disclosures on its website.

Item 11. ***Executive Compensation.***

The information required by this item is incorporated herein by reference to the sections entitled Compensation Discussion and Analysis, Report of the Compensation Committee of the Board of Directors, Executive Compensation and Corporate Governance and Board Matters Directors compensation in the Company s Proxy Statement.

Item 12. ***Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.***

The information required by this item with respect to the security ownership of certain beneficial owners and management is incorporated herein by reference to the section entitled Security Ownership of Certain Beneficial Owners and Management in the Company s Proxy Statement.

Equity Compensation Plan Information

The following table provides certain information regarding common stock authorized for issuance under the Company s equity compensation plans as of December 31, 2012:

Plan Category	Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants and Rights (a)	Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights (b)	Number of Securities Remaining Available for Future Issuance under Equity Compensation Plans (Excluding Securities Reflected in Column (a)) (c)
Equity compensation plans approved by stockholders (1)	1,429,822	$ 13.62	5,116,163

(1) These plans consist of the Company s 2012 Incentive Plan and 2001 Stock Incentive Plan.

Item 13. ***Certain Relationships and Related Transactions, and Director Independence.***

The information required by this item is incorporated herein by reference to the section entitled Certain Relationships and Related Party Transactions in the Company s Proxy Statement.

Item 14. ***Principal Accounting Fees and Services.***

The information required by this item is incorporated herein by reference to the section entitled Proposal 2 Ratification of Selection of Independent Registered Public Accounting Firm Audit and other fees in the Company s Proxy Statement.

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PART IV

Item 15. ***Exhibits and Financial Statement Schedules.***

(a) Financial Statements and Schedules

The financial statements are set forth under Item 8 of this Annual Report on Form 10-K. Financial statement schedules have been omitted since they are either not required, not applicable, or the information is otherwise included.

(b) Exhibit Listing

Number	Description
2.1	Share Purchase Agreement, dated October 26, 2012 by and among MarketAxess Holdings Inc. and Euroclear S.A./N.V. (incorporated by reference to Exhibit 10.1 to the registrant s Current Report on Form 8-K/A dated November 2, 2012)
3.1	Amended and Restated Certificate of Incorporation (incorporated by reference to Exhibit 3.2 to the registrant s Registration Statement on Form S-1, as amended (Registration No. 333-112718))
3.2(a)	Amended and Restated Bylaws (incorporated by reference to Exhibit 3.4 to the registrant s Registration Statement on Form S-1, as amended (Registration No. 333-112718))
3.2(b)	Amendment No. 1 to the Amended and Restated Bylaws (incorporated by reference to Exhibit 3.1 to the registrant s Current Report on Form 8-K dated January 25, 2013)
3.3	Form of Certificate of Designation of Series A Preferred Stock of MarketAxess Holdings Inc. (incorporated by reference to Exhibit 3.1 to the registrant s Registration Statement on Form 8-A dated June 3, 2008)
4.1	Specimen Common Stock certificate (incorporated by reference to Exhibit 4.1 to the registrant s Registration Statement on Form S-1, as amended (Registration No. 333-112718))
4.2	See Exhibits 3.1 and 3.2 for provisions defining the rights of holders of common stock and non-voting common stock of the registrant
10.1(a)	MarketAxess Holdings Inc. Amended and Restated 2001 Stock Incentive Plan (incorporated by reference to Exhibit 10.7 to the registrant s Annual Report on Form 10-K dated February 17, 2012)#
10.1(b)	Amendment to the MarketAxess Holdings Inc. 2001 and 2000 Stock Incentive Plans (incorporated by reference to Exhibit 10.9 to the registrant s Registration Statement on Form S-1, as amended (Registration No. 333-112718)) #
10.2	MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Appendix A to the registrant s Proxy Statement for its Annual Meeting for Stockholders held on June 7, 2012, filed on April 25, 2012)#
10.3	MarketAxess Holdings Inc. 2004 Annual Performance Incentive Plan (incorporated by reference to Exhibit 10.11 to the registrant s Registration Statement on Form S-1, as amended (Registration No. 333-112718)) #
10.4	MarketAxess Holdings Inc. 2009 Code Section 162(m) Executive Performance Incentive Plan (incorporated by reference to Appendix B to the registrant s Proxy Statement for its Annual Meeting for Stockholders held on June 7, 2012, filed on April 25, 2012)#
10.5(a)	Form of Restricted Stock Agreement for Richard M. McVey pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.1 to the registrant s Current Report on Form 8-K dated January 23, 2009)#
10.5(b)	Form of Restricted Stock Agreement for Employees other than Richard M. McVey pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.3 to the registrant s Current Report on Form 8-K dated January 15, 2008)#

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Number	Description
10.6(a)	Form of Restricted Stock Unit Agreement for Richard M. McVey pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.3 to the registrant s Current Report on Form 8-K dated January 19, 2011)#
10.6(b)	Form of Restricted Stock Unit Agreement for employees other than Richard M. McVey pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.4 to the registrant s Current Report on Form 8-K dated January 19, 2011)#
10.6(c)	Guidelines for Restricted Stock Units granted under the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.1 to the registrant s Current Report on Form 8-K dated January 19, 2011)#
10.7(a)	Form of Performance Share Award Agreement for Richard M. McVey pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.1 to the registrant s Current Report on Form 8-K dated January 15, 2008)#
10.7(b)	Form of Performance Share Award Agreement for Employees other than Richard M. McVey pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.2 to the registrant s Current Report on Form 8-K dated January 15, 2008)#
10.8(a)	Form of Incentive Stock Option Agreement for Mr. McVey pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.5 to the registrant s Current Report on Form 8-K dated January 15, 2008)#
10.8(b)	Form of Incentive Stock Option Agreement for Employees other than Richard M. McVey pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Exhibit 10.4 to the registrant s Current Report on Form 8-K dated January 15, 2008)#
10.8(c)	Form of Non Qualified Stock Option Agreement pursuant to the MarketAxess Holdings Inc. 2012 Incentive Plan (incorporated by reference to Appendix C to the registrant s Proxy Statement for its Annual Meeting of Stockholders held on June 7, 2006, filed on May 1, 2006)#
10.9(a)	MarketAxess Severance Pay Plan, effective August 1, 2006 (incorporated by reference to Exhibit 10.28(a) to the registrant s Form 10-K for the year ended December 31, 2009 filed on March 3, 2009)#
10.9(b)	Amendment No. 1 to MarketAxess Severance Pay Plan, dated as of December 17, 2008 (incorporated by reference to Exhibit 10.28(b) to the registrant s Form 10-K for the year ended December 31, 2009 filed on March 3, 2009)#
10.10(a)	Letter Agreement, dated January 19, 2011, by and between MarketAxess Holdings Inc. and Richard M. McVey (incorporated by reference to Exhibit 10.4 to the registrant s Current Report on Form 8-K dated January 14, 2011)#
10.10(b)	Incentive Stock Option Agreement, dated January 19, 2011, by and between MarketAxess Holdings Inc. and Richard M. McVey Incentive Stock Option Agreement, dated January 19, 2011, by and between MarketAxess Holdings Inc. and Richard M. McVey (incorporated by reference to Exhibit 10.6 to the registrant s Current Report on Form 8-K dated January 19, 2011)#
10.10(c)	Restricted Stock Unit Agreement, dated January 19, 2011, by and between MarketAxess Holdings Inc. and Richard M. McVey (incorporated by reference to Exhibit 10.8 to the registrant s Current Report on Form 8-K dated January 19, 2011)#
21.1*	Subsidiaries of the Registrant
23.1*	Consent of PricewaterhouseCoopers LLP
31.1*	Certification by Chief Executive Officer pursuant to Exchange Act Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

Number	Description
31.2*	Certification by Chief Financial Officer pursuant to Exchange Act Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification by Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema Document
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document

* Filed herewith.

** Attached as Exhibit 101 to this Annual Report on Form 10-K are the following materials, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Statements of Financial Condition as of December 31, 2012 and December 31, 2011; (ii) Consolidated Statements of Operations for the Years Ended
December 31, 2012, 2011 and 2010; (iii) Consolidated Statements of Comprehensive Income for the Years Ended

December 31, 2012, 2011 and 2010; (iv) Consolidated Statement of Stockholders Equity for the Years Ended

December 31, 2012, 2011 and 2010; (v) Consolidated Statements of Cash Flows for the Years Ended

December 31, 2012, 2011 and 2010; and (vi) Notes to the Consolidated Financial Statements.

Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

Management contract or compensatory plan or arrangement.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

MARKETAXESS HOLDINGS INC.

By: /s/ RICHARD M. MCVEY
Richard M. McVey
Chief Executive Officer

Date: February 21, 2013

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated:

Signature	Title(s)	Date
/s/ RICHARD M. MCVEY Richard M. McVey	Chief Executive Officer and Chairman of the Board of Directors (principal executive officer)	February 21, 2013
/s/ ANTONIO L. DELISE Antonio L. DeLise	Chief Financial Officer (principal financial and accounting officer)	February 21, 2013
/s/ STEVEN L. BEGLEITER Steven L. Begleiter	Director	February 21, 2013
/s/ SHARON BROWN-HRUSKA Sharon Brown-Hruska	Director	February 21, 2013
/s/ STEPHEN P. CASPER Stephen P. Casper	Director	February 21, 2013
/s/ DAVID G. GOMACH David G. Gomach	Director	February 21, 2013
/s/ CARLOS HERNANDEZ Carlos Hernandez	Director	February 21, 2013
/s/ RONALD M. HERSCH Ronald M. Hersch	Director	February 21, 2013
/s/ JOHN STEINHARDT John Steinhardt	Director	February 21, 2013
/s/ JAMES J. SULLIVAN James J. Sullivan	Director	February 21, 2013

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11,674

Federal Home Loan Bank advances, net
Level 2

98,758

98,942

98,385

98,812

Long-term debt, net
Level 2

7,592

7,506

8,405

8,314

Accrued interest payable
Level 1

357

357

343

343

Interest rate swaps
Level 2

1,481

1,481

774

774

Off-balance-sheet financial instruments:

Commitments to extend credit
Level 3

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Standby letters of credit
Level 3

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(1) All loans are Level 2 except impaired loans of $0 and $98 as of March 31, 2016 and December 31, 2015, respectively, which are Level 3.

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

"SAFE HARBOR" CONCERNING FORWARD-LOOKING STATEMENTS

Certain statements in this report, other than purely historical information, including estimates, projections, statements relating to our business plans, objectives and expected operating results, and the assumptions upon which those statements are based, are “forward-looking statements” within the meanings of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). Forward-looking statements may appear throughout this report. These forward-looking statements are generally identified by the words “believes,” “expects,” “intends,” “anticipates,” “projects,” “future,” “may,” “should,” “will,” “strategy,” “plan,” “opportunity,” “will be,” “will likely result,” “will continue” or similar re references to estimates, predictions or future events. Such forward-looking statements are based upon certain underlying assumptions, risks and uncertainties. Because of the possibility that the underlying assumptions are incorrect or do not materialize as expected in the future, actual results could differ materially from these forward-looking statements. Risks and uncertainties that may affect future results include: interest rate risk; competitive pressures; pricing pressures on loans and deposits; changes in credit and other risks posed by the Company's loan and investment portfolios, including declines in commercial or residential real estate values or changes in the allowance for loan losses dictated by new market conditions or regulatory requirements; actions of bank and nonbank competitors; changes in local and national economic conditions; changes in regulatory requirements, limitations and costs; changes in customers' acceptance of the Company's products and services; cyber-attacks; and any other risks described in the “Risk Factors” sections of this and other reports filed by the Company with the Securities and Exchange Commission. The Company undertakes no obligation to revise or update such forward-looking statements to reflect current or future events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

CRITICAL ACCOUNTING POLICIES

The discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements that have been prepared in accordance with GAAP. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, income and expenses. These estimates are based upon historical experience and on various other assumptions that management believes are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. The estimates and judgments that management believes have the most effect on the Company's reported financial position and results of operations are described as critical accounting policies in the Company's Annual Report on Form 10-K for the year ended December 31, 2015, as filed with the Securities and Exchange Commission on March 3, 2016. There have been no significant changes in the critical accounting policies or the assumptions and judgments utilized in applying these policies since the year ended December 31, 2015.

THREE MONTHS ENDED MARCH 31, 2016

OVERVIEW

The following discussion describes the consolidated operations and financial condition of the Company, which includes West Bank and West Bank's wholly owned subsidiary WB Funding Corporation (which owned an interest in a limited liability company that was sold in the fourth quarter of 2015). Results of operations for the three months ended March 31, 2016 are compared to the results for the same period in 2015, and the consolidated financial condition of the Company as of March 31, 2016 is compared to balances as of December 31, 2015. The Company operates in three markets: central Iowa, which is generally the greater Des Moines metropolitan area; eastern Iowa, which is the area including and surrounding Iowa City and Coralville, Iowa; and the Rochester, Minnesota area.

Net income for the three months ended March 31, 2016 was $5,696, or $0.35 per diluted common share, compared to $5,103, or $0.32 per diluted common share, for the three months ended March 31, 2015. The Company's annualized return on average assets and return on average equity for the three months ended March 31, 2016 were 1.31 and 14.77 percent, respectively, compared to 1.27 and 14.57 percent, respectively, for the three months ended March 31, 2015.

The increase in net income for the three months ended March 31, 2016 compared to the same period in 2015 was primarily due to growth in net interest income as the result of continued loan growth and the recognition of tax-exempt gain from bank-owned life insurance. Partially offsetting these improvements to net income for the three months ended March 31, 2016 compared to the three months ended March 31, 2015, were increases in the provision for loan losses and in noninterest expense.

Net interest income for the three months ended March 31, 2016 grew $736 compared to the three months ended March 31, 2015. The increase was primarily due to the $28,241 increase in loans outstanding from December 31, 2015 to March 31, 2016. Average loans outstanding for the first three months of 2016 were $67,513 higher than for the first three months of 2015. Management believes loan growth will continue to be strong in 2016 as the demand for commercial, construction and development, and commercial real estate loans remains strong in all three of the Company's markets. In association with the loan growth, the Company recorded a provision for loan losses of $200 for the three months ended March 31, 2016, compared to no provision in the three months ended March 31, 2015. The allowance for loan losses was 1.20 percent of outstanding loans as of March 31, 2016 and December 31, 2015.

The Company recognized tax-exempt gain from bank-owned life insurance of $443 in the three months ended March 31, 2016 due to the losses of one of our colleagues and a former employee. Partially offsetting this tax-exempt income was an increase of approximately $171 in noninterest expense due to the recognition of costs associated with the death of the employee. The remaining $182 increase in noninterest expense for the three months ended March 31, 2016, compared to the same period in 2015 was mainly due to increased salary and benefit costs, and normal increases in operating costs.

Another significant change in the first quarter of 2016 was the purchase of a previously leased branch facility in Waukee, Iowa. The purchase is expected to reduce ongoing occupancy costs. Previously announced construction is underway for a permanent office in Rochester, Minnesota. The new facility will replace a leased office and is expected to open in the third quarter of 2016. We believe the more prominent location of the new office will enhance our ability to expand our customer base in that market.

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(in thousands, except share and per share data)

Each quarter throughout the year, the Company's four key performance metrics are compared to our identified peer group of 16 companies. The group of 16 publicly traded peer financial institutions against which we compare our performance each quarter consists of BankFinancial Corporation, Baylake Corp., Farmers Capital Bank Corporation, First Defiance Financial Corp., First Mid-Illinois Bancshares, Inc., Hills Bancorporation, Horizon Bancorp, Isabella Bank Corporation, Mercantile Bank Corporation, MidWestOne Financial Group, Inc., MutualFirst Financial, Inc., Peoples Bancorp, Pulaski Financial Corp., QCR Holdings, Inc., Southwest Bancorp and Waterstone Financial, Inc. The members of the peer group are selected based on their business focus, scope and location of operations, size and other considerations. The Company is in the middle of the group in terms of size. The group is periodically reviewed, with changes made primarily to reflect merger and acquisition activity. Our goal is to perform at or near the top of these peers relative to what we consider to be four key metrics: return on average assets, return on average equity, efficiency ratio and Texas ratio. We believe these measures encompass the factors that define the performance of a community bank. When contrasted with the peer group's metrics for the year ended December 31, 2015 (latest data available), the Company's metrics for the three months ended March 31, 2016 were better than those of each company in the peer group as shown in the table below.

	West Bancorporation, Inc.	Peer Group Range
	Three months ended March 31, 2016	Year ended December 31, 2015
Return on average assets	1.31%	0.35% - 1.19%
Return on average equity	14.77%	2.70% - 11.65%
Efficiency ratio*	46.91%	54.97% - 79.93%
Texas ratio*	0.76%	3.77% - 29.06%

* A lower ratio is more desirable.

Raymond James & Associates, Inc. recently included the Company on its Community Bankers Cup awards listing of the top ten percent of community banks in the United States. The awards were based on profitability, operational efficiency and balance sheet metrics. The pool of 301 community banks considered for recognition were all publicly traded domestic banks with assets between $500 million and $10 billion as of December 31, 2015. The Company was ranked number five out of the 301 banks across America and was the only Iowa bank and one of very few from the Midwest to be listed in the top ten percent. This was the fourth consecutive year West Bancorporation, Inc. has been included on the awards list.

At its meeting on April 27, 2016, the Board of Directors declared a quarterly dividend of $0.17 per common share. The dividend is payable on May 25, 2016, to stockholders of record as of May 11, 2016. This represents the highest quarterly dividend ever paid by the Company and an increase from the $0.16 dividend paid in the four prior quarters.

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(in thousands, except share and per share data)

RESULTS OF OPERATIONS

The following table shows selected financial results and measures for the three months ended March 31, 2016 compared with the same period in 2015.

	Three Months Ended March 31,			
	2016	2015	Change	Change %
Net income	$5,696	$5,103	$593	11.62%
Average assets	1,744,098	1,623,638	120,460	7.42 %
Average stockholders' equity	155,119	142,059	13,060	9.19 %
Return on average assets	1.31 %	1.27 %	0.04 %	
Return on average equity	14.77 %	14.57 %	0.20 %	
Net interest margin	3.51 %	3.59 %	(0.08)%	
Efficiency ratio*	46.91 %	48.25 %	(1.34)%	
Dividend payout ratio	45.13 %	43.93 %	1.20 %	
Average equity to average assets ratio	8.89 %	8.75 %	0.14 %	

	As of March 31,		
	2016	2015	Change
Texas ratio*	0.76 %	2.73 %	(1.97)%
Equity to assets ratio	8.94 %	8.72 %	0.22 %
Tangible common equity ratio	8.94 %	8.72 %	0.22 %

* A lower ratio is more desirable.

Definitions of ratios:
- Return on average assets - annualized net income divided by average assets.
- Return on average equity - annualized net income divided by average stockholders' equity.
- Net interest margin - annualized tax-equivalent net interest income divided by average interest-earning assets.
- Efficiency ratio - noninterest expense (excluding other real estate owned expense) divided by noninterest income (excluding net securities gains and gains/losses on disposition of premises and equipment) plus tax-equivalent net interest income.
- Dividend payout ratio - dividends paid to common stockholders divided by net income.
- Texas ratio - total nonperforming assets divided by tangible common equity plus the allowance for loan losses.
- Equity to assets ratio - equity divided by assets.
- Tangible common equity ratio - common equity less intangible assets divided by tangible assets.

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Net Interest Income

The following table presents average balances and related interest income or interest expense, with the resulting average yield or rate by category of interest-earning assets or interest-bearing liabilities. Interest income and the resulting net interest income are shown on a fully taxable basis.

Data for the three months ended March 31:

	Average Balance				Interest Income/Expense				Yield/Rate		
	2016	2015	Change	Change-%	2016	2015	Change	Change-%	2016	2015	Change
Interest-earning assets:											
Loans:											
Commercial	$349,635	$313,962	$35,673	11.36 %	$3,615	$3,199	$416	13.00 %	4.16%	4.13%	0.03 %
Real estate	896,510	862,819	33,691	3.90 %	10,026	9,563	463	4.84 %	4.50%	4.49%	0.01 %
Consumer and other	7,414	9,265	(1,851)	(19.98)%	73	88	(15)	(17.05)%	3.94%	3.86%	0.08 %
Total loans	1,253,559	1,186,046	67,513	5.69 %	13,714	12,850	864	6.72 %	4.40%	4.39%	0.01 %
Investment securities:											
Taxable	256,681	230,754	25,927	11.24 %	1,155	1,125	30	2.67 %	1.80%	1.95%	(0.15)%
Tax-exempt	124,153	103,266	20,887	20.23 %	1,332	1,155	177	15.32 %	4.29%	4.47%	(0.18)%
Total investment securities	380,834	334,020	46,814	14.02 %	2,487	2,280	207	9.08 %	2.61%	2.73%	(0.12)%
Federal funds sold	14,630	15,231	(601)	(3.95)%	20	10	10	100.00 %	0.55%	0.27%	0.28 %
Total interest-earning assets	$1,649,023	$1,535,297	$113,726	7.41 %	16,221	15,140	1,081	7.14 %	3.96%	4.00%	(0.04)%
Interest-bearing liabilities:											
Deposits:											
Interest-bearing demand, savings and money											

market	$861,065	$800,722	$60,343	7.54 %	537	324	213	65.74 %	0.25 %	0.16 %	0.09 %
Time deposits	112,036	134,258	(22,222)	(16.55)%	168	247	(79)	(31.98)%	0.60 %	0.75 %	(0.15)%
Total deposits	973,101	934,980	38,121	4.08 %	705	571	134	23.47 %	0.29 %	0.25 %	0.04 %
Other borrowed funds	141,600	170,335	(28,735)	(16.87)%	1,120	986	134	13.59 %	3.18 %	2.35 %	0.83 %
Total interest-bearing liabilities	$1,114,701	$1,105,315	$9,386	0.85 %	1,825	1,557	268	17.21 %	0.66 %	0.57 %	0.09 %
Tax-equivalent net interest income					$14,396	$13,583	$813	5.99 %			
Net interest spread									3.30 %	3.43 %	(0.13)%
Net interest margin									3.51 %	3.59 %	(0.08)%

The Company's largest component of net income is net interest income. Fluctuations in net interest income can result from the combination of changes in the average balances of asset and liability categories and changes in interest rates. Interest rates earned and paid are affected by general economic conditions, particularly changes in market interest rates, and by competitive factors, government policies and the actions of regulatory authorities. Net interest margin is a measure of the net return on interest-earning assets and is computed by dividing annualized tax-equivalent net interest income by total average interest-earning assets for the period. Management continually develops and applies strategies to maintain the net interest margin.

The net interest margin for the three months ended March 31, 2016 declined 8 basis points to 3.51 percent compared to the same period in 2015. The Board of Governors of the Federal Reserve System (the Federal Reserve) increased the target federal funds interest rate by 25 basis points in December 2015, the first interest rate change in seven years. This action was the impetus for the Company increasing interest rates on certain deposit categories in the same month. The other primary drivers of the decline in the net interest margin for the three months ended March 31, 2016 compared to the three months ended March 31, 2015 were the 12 basis point reduction in yield on investment securities and the 83 basis point increase in the rate on other borrowed funds. Despite the decline in the net interest margin, tax-equivalent net interest income for the three months ended March 31, 2016 increased $813 compared to the same time period in 2015, primarily as the result of the increase in average outstanding loans and the offset of the prime rate increase in mid-December 2015. Management expects the persisting low interest rate environment to continue to put pressure on the net interest margin throughout the remainder of 2016 if the Federal Reserve maintains its current monetary policy.

Tax-equivalent interest income on loans increased $864 for the three months ended March 31, 2016 compared to the three months ended March 31, 2015. The improvement was due to the $67,513 increase in average loan balances quarter-over-quarter in conjunction with the effect of the one basis point increase in the yield for the three months ended March 31, 2016 compared to the three months ended March 31, 2015. The Company continues to focus on expanding existing and entering into new customer relationships while maintaining strong credit quality. The yield on the Company's loan portfolio is affected by the mix of the loans in the portfolio, the interest rate environment, the effects of competition, the level of nonaccrual loans and reversals of previously accrued interest on charged-off loans. The political and economic environments can also influence the volume of new loan originations and the mix of variable rate versus fixed rate loans

The average balance of investment securities was $46,814 higher during the three months ended March 31, 2016 than during the same period in 2015, while a lower yield on the most recent portfolio purchases caused the portfolio yield to decline for the three months ended March 31, 2016, compared to the same period last year. The increase in average balances was primarily attributable to purchases of $99,901 made in the last four months of 2015. No investment securities were purchased during the three months ended March 31, 2016.

Average interest-bearing demand, savings and money market deposits increased $60,343 for the three months ended March 31, 2016 compared to the three months ended March 31, 2015, mainly due to an increase in average public fund money market accounts. The average rate paid on deposits for the three months ended March 31, 2016 increased four basis points compared to the three months ended March 31, 2015. The increase in rates was primarily due to increasing interest rates on certain money market deposit products in late December 2015. Meanwhile, interest rates continued to decline on time deposits as maturing time deposits had higher rates than are currently offered. The average balance of time deposits continues to decline as fewer customers are willing to lock in low rates in this extended period of historically low interest rates.

The average rate paid on other borrowed funds increased 83 basis points for the three months ended March 31, 2016 compared to the three months ended March 31, 2015, while the average balance declined $28,735 quarter-over-quarter. The increase in the average rate paid was due to the combination of amortization of interest rate swap termination fees paid in 2015, an interest rate swap that became effective in December 2015, and an increase in rates for variable rate FHLB advances. The decline in the average balance for the three months ended March 31, 2016 compared to the same three months of 2015 was due to the the combination of a reduction in average overnight borrowings and principal payments on long-term borrowings.

Provision for Loan Losses and the Related Allowance for Loan Losses

The provision for loan losses represents a charge made to earnings to maintain an adequate allowance for loan losses. The adequacy of the allowance for loan losses is evaluated quarterly by management and reviewed by the Board of Directors. The allowance for loan losses is management's best estimate of probable losses inherent in the loan portfolio as of the balance sheet date. Based upon the evaluations, the provision for loan losses for the three months ended March 31, 2016 and 2015 was $200 and $0, respectively.

(in thousands, except share and per share data)

Factors considered in establishing an appropriate allowance include: an assessment of the financial condition of the borrower; the value and adequacy of loan collateral; the condition of the local economy and the condition of the specific industry of the borrower; the levels and trends of loans by segment; and a review of delinquent and classified loans. The quarterly evaluation focuses on factors such as specific loan reviews, changes in the components of the loan portfolio given the current and forecasted economic conditions, and historical loss experience. Any one of the following conditions may result in the review of a specific loan: concern about whether the customer's cash flow or net worth is sufficient to repay the loan; delinquency status; criticism of the loan in a regulatory examination; the suspension of interest accrual; or other factors, including whether the loan has other special or unusual characteristics that suggest special monitoring is warranted. The Company's concentration risks include geographic concentration in central and eastern Iowa and southeastern Minnesota. The local economies are composed primarily of service industries and state and county governments.

West Bank has a significant portion of its loan portfolio in commercial real estate loans, commercial lines of credit, commercial term loans, and construction and land development loans. West Bank's typical commercial borrower is a small or medium-sized, privately owned business entity. West Bank's commercial loans typically have greater credit risks than residential mortgage or consumer loans because they often have larger balances and repayment usually depends on the borrowers' successful business operations. Commercial loans also involve additional risks because they generally are not fully repaid over the loan period and, thus, may require refinancing or a large payoff at maturity. When the economy turns downward, commercial borrowers may not be able to repay their loans, and the value of their assets, which are usually pledged as collateral, may decrease rapidly and significantly.

While management uses available information to recognize losses on loans, further reduction in the carrying amounts of loans may be necessary based on changes in circumstances, changes in the overall economy in the markets we currently serve, or later acquired information. Identifiable sectors within the general economy are subject to additional volatility, which at any time may have a substantial impact on the loan portfolio. In addition, regulatory agencies, as integral parts of their examination processes, periodically review the credit quality of the loan portfolio and the level of the allowance for loan losses. Such agencies may require West Bank to recognize additional losses based on such agencies' review of information available to them at the time of their examinations.

West Bank's policy is to charge off loans when, in management's opinion, a loan or a portion of a loan is deemed uncollectible. Concerted efforts are made to maximize subsequent recoveries. The following table summarizes the activity in the Company's allowance for loan losses for the three months ended March 31, 2016 and 2015 and related ratios.

	Three Months Ended March 31,		
	2016	2015	Change
Balance at beginning of period	$14,967	$13,607	$1,360
Charge-offs	—	(38)	38
Recoveries	113	309	(196)
Net recoveries	113	271	(158)
Provision for loan losses charged to operations	200	—	200
Balance at end of period	$15,280	$13,878	$1,402
Average loans outstanding	$1,253,559	$1,185,946	
Ratio of annualized net (recoveries) during the period to average loans outstanding	(0.04)%	(0.09)%	

Ratio of allowance for loan losses to average loans outstanding	1.22	%	1.17	%

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(in thousands, except share and per share data)

In general, the U.S. economy is growing, but at a lower rate than was considered normal before the financial crisis. Job growth continues at approximately 200,000 new jobs per month, and the national unemployment rate remains at 5.0 percent. Activity in the housing market continues at a moderate pace. Interest rates are expected to gradually increase, although any increase may be delayed due to the slowing world economy. The economic environments in Iowa and Minnesota continue to slowly improve. Based on the current economic indicators, the Company decided to maintain the economic factors within the allowance for loan losses evaluation at the same levels used in 2015. In the first three months of 2016, the Company continued to use experience factors based on the highest losses calculated over a rolling 12-, 16-, or 20-quarter period. As the experience factors continued to decline, management decided to increase the factors for other considerations in the first three months of 2016 for construction and development, commercial real estate, home equity and consumer loans to maintain an adequate allowance for loan losses. This held the portion of the allowance for loan losses related to loans collectively evaluated for impairment at 1.16 percent as of March 31, 2016 and December 31, 2015. Management believes the resulting allowance for loan losses as of March 31, 2016 was adequate to absorb the losses inherent in the loan portfolio at the end of the quarter.

Noninterest Income

The following table shows the variance from the prior year in the noninterest income categories shown in the Consolidated Statements of Income. In addition, accounts within the “Other income” category that represent a significant portion of the total or a significant variance are shown below.

	Three Months Ended March 31,			
Noninterest income:	2016	2015	Change	Change %
Service charges on deposit accounts	$596	$620	$(24)	(3.87)%
Debit card usage fees	447	435	12	2.76%
Trust services	297	325	(28)	(8.62)%
Increase in cash value of bank-owned life insurance	168	189	(21)	(11.11)%
Gain from bank-owned life insurance	443	—	443	NA
Realized investment securities gains, net	—	11	(11)	(100.00)%
Other income:				
Revenue from residential mortgage banking	22	35	(13)	(37.14)%
All other income	257	245	12	4.90%
Total other income	279	280	(1)	(0.36)%
Total noninterest income	$2,230	$1,860	$370	19.89%

Revenue from trust services was lower during the three months ended March 31, 2016 compared to the same time period in 2015 mainly due to fewer one-time estate fees. Partially offsetting the lower amount of one-time fees were ongoing business development efforts, which resulted in growth in the number of accounts and amount of assets held within trust accounts.

The increase in cash value of bank-owned life insurance was lower in the three months ended March 31, 2016 than in the three months ended March 31, 2015, as crediting rates within the policies have declined slightly due to the historically low interest rate environment. As previously mentioned, gain from bank-owned life insurance was $443 for the three months ended March 31, 2016 due to the deaths of a colleague and one of our former employees.

The Company did not sell any investment securities during the first three months of 2016, while net gains on sales of securities of $11 were recognized during the first three months of 2015. The sales in 2015 were undertaken in order to capitalize on available net gains while being able to reinvest the proceeds in investment securities with higher yields.

Revenue from residential mortgage banking declined in the three months ended March 31, 2016 compared to the same period in 2015 as the final gains on sales of residential mortgage loans occurred in January 2015, as residential mortgage underwriting and processing were outsourced to a third party beginning in January 2015. The Company currently receives a fee from that third party for each residential mortgage loan initiated and closed by our retail staff.

(in thousands, except share and per share data)

Noninterest Expense

The following table shows the variance from the prior year in the noninterest expense categories shown in the Consolidated Statements of Income. In addition, accounts within the "Other expenses" category that represent a significant portion of the total or a significant variance are shown below.

	Three Months Ended March 31,			
Noninterest expense:	2016	2015	Change	Change %
Salaries and employee benefits	$4,256	$3,990	$ 266	6.67 %
Occupancy	951	1,049	(98)	(9.34)%
Data processing	579	574	5	0.87 %
FDIC insurance expense	218	202	16	7.92 %
Professional fees	234	204	30	14.71 %
Director fees	240	188	52	27.66 %
Other expenses:				
Marketing	56	63	(7)	(11.11)%
Business development	176	174	2	1.15 %
Insurance expense	88	82	6	7.32 %
Bank service charges and investment advisory fees	189	173	16	9.25 %
Postage and courier	86	88	(2)	(2.27)%
Trust	96	94	2	2.13 %
Consulting fees	66	64	2	3.13 %
Supplies	63	77	(14)	(18.18)%
Low income housing projects amortization	109	46	63	136.96 %
All other	392	378	14	3.70 %
Total other	1,321	1,239	82	6.62 %
Total noninterest expense	$7,799	$7,446	$ 353	4.74 %

Salaries and employee benefits increased for the three months ended March 31, 2016 compared to the three months ended March 31, 2015, as the result of higher stock-based compensation costs and increased health insurance costs.

When contrasted with the three months ended March 31, 2015, occupancy costs declined for the three months ended March 31, 2016, mostly as the result of the previously mentioned purchase of the Waukee, Iowa, branch facility. The reduction included a one-time reversal of previously accrued rent related to the terms of the previous lease.

Professional fees increased for the three months ended March 31, 2016 compared to the same time period in 2015 chiefly due to increased legal fees associated with defense costs for previously disclosed litigation.

Director fees increased for the three months ended March 31, 2016 compared to the same period in 2015 as a result of increased stock-based compensation costs.

The year-to-date 2016 increase in the cost of low income housing project amortization compared to the three months ended March 31, 2015 was related to the Company making commitments to invest in additional projects. The projected expense for the year ended December 31, 2016 is approximately $400 compared to $228 for the year ended December 31, 2015.

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Income Tax Expense

The Company recorded income tax expense of $2,234 (28.2 percent of pre-tax income) for the three months ended March 31, 2016 compared with $2,274 (30.8 percent of pre-tax income) for the three months ended March 31, 2015. The Company's consolidated income tax rate differs from the federal statutory income tax rate primarily due to tax-exempt interest income, the tax-exempt increase in cash value of bank-owned life insurance, disallowed interest expense, state income taxes and changes in the valuation allowance. For the three months ended March 31, 2016, the tax rate was also lower than the statutory income tax rate due to $443 of tax-exempt gain from bank-owned life insurance. The tax rate for the first quarters of 2016 and 2015 was also impacted by year-to-date federal low income housing tax credits of approximately $88 and $75, respectively.

FINANCIAL CONDITION

The Company had total assets of $1,755,119 as of March 31, 2016, an increase of 0.38 percent compared to total assets as of December 31, 2015. The most significant changes in the balance sheet were increases in loans, premises and equipment, and deposits, and decreases in cash and cash equivalents and securities available for sale. A summary of changes in the components of the balance sheet is described below.

Investment Securities

The balance of investment securities available for sale declined by $9,379 during the three months ended March 31, 2016, which was attributed primarily to normal principal paydowns on mortgage-backed securities and collateralized mortgage obligations. This cash flow was used to fund loan growth.

As of March 31, 2016, approximately 72 percent of the available for sale investment securities portfolio consisted of government agency guaranteed collateralized mortgage obligations and mortgage-backed securities. In the current low interest rate environment, management believes both provide relatively good yields, have little to no credit risk and provide fairly consistent cash flows.

Loans and Nonperforming Assets

Loans outstanding increased $28,241 from $1,246,688 as of December 31, 2015, to $1,274,929 as of March 31, 2016. Growth in the loan portfolio during the first three months of 2016 was primarily in the construction, commercial and commercial real estate segments. The Company continues to focus on business development efforts in all of its markets. Management believes loan growth will continue to be strong in all three of our markets during 2016.

Credit quality of the Company's loan portfolio remains strong as nonperforming loans remained at less than a quarter percent of total loans outstanding as of March 31, 2016, as shown in the table below. The Company's Texas ratio, which is computed by dividing total nonperforming assets by tangible common equity plus the allowance for loan losses, was 0.76 percent as of March 31, 2016, compared to 0.87 percent as of December 31, 2015. The ratio for both dates was significantly better than the December 31, 2015 peer group average, which was approximately 10.75 percent, according to data in the December 2015 Bank Holding Company Performance Report, which is prepared by the Division of Supervision and Regulation of the Federal Reserve.

(in thousands, except share and per share data)

The following table sets forth the amount of nonperforming loans and assets held by the Company and common ratio measurements of those items as of the dates shown.

	March 31, 2016	December 31, 2015	Change
Nonaccrual loans	$ 1,286	$ 1,381	$ (95)
Loans past due 90 days and still accruing interest	—	—	—
Troubled debt restructured loans [(1)]	20	80	(60)
Total nonperforming loans	1,306	1,461	(155)
Other real estate owned	—	—	—
Total nonperforming assets	$ 1,306	$ 1,461	$ (155)
Nonperforming loans to total loans	0.10 %	0.12 %	(0.02)%
Nonperforming assets to total assets	0.07 %	0.08 %	(0.01)%

(1) While TDR loans are commonly reported by the industry as nonperforming, those not classified in the nonaccrual category are accruing interest due to payment performance. TDR loans on nonaccrual status are categorized as nonaccrual. There were three TDR loans as of March 31, 2016 and December 31, 2015, with aggregate balances of $577 and $613, respectively, categorized as nonaccrual.

For additional information, refer to the “Provision for Loan Losses and the Related Allowance for Loan Losses” in this section, and Notes 4 and 9 to the financial statements.

Premises and Equipment

Premises and equipment increased $5,736 from $11,562 as of December 31, 2015, to $17,298 as of March 31, 2016. In February 2016, the Company purchased a branch facility for $4,512 that had previously been leased. The Company also continues with the construction of a new office in Rochester, Minnesota.

Deposits

Deposits increased $5,018 during the first three months of 2016, or 0.35 percent, compared to December 31, 2015. Savings deposits, which include money market and insured cash sweep money market accounts, increased $62,543 from December 31, 2015 to March 31, 2016. Interest-bearing demand accounts declined $20,524, and noninterest-bearing demand accounts declined $29,298, from December 31, 2015 to March 31, 2016. These changes were due to the combination of business development efforts and normal fluctuations, as corporate customers' liquidity needs vary at any given time. Total time deposits declined $7,703 during the first three months of 2016 due to the continued low interest rate environment. As of March 31, 2016, a significant related party relationship maintained total deposit balances with West Bank of approximately $162,000.

Borrowings

Short-term borrowings declined to $17,000 as of March 31, 2016 from $19,000 as of December 31, 2015. The need for overnight funding is primarily dependent on corporate customer deposit fluctuations, loan fundings and loan repayments. Long-term debt declined $813 during the first three months of 2016, primarily due to scheduled repayments.

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Liquidity and Capital Resources

The objectives of liquidity management are to ensure the availability of sufficient cash flows to meet all financial commitments and to capitalize on opportunities for profitable business expansion. The Company's principal source of funds is deposits. Other sources include loan principal repayments, proceeds from the maturity and sale of investment securities, principal payments on collateralized mortgage obligations and mortgage-backed securities, federal funds purchased, advances from the FHLB, and funds provided by operations. Liquidity management is conducted on both a daily and a long-term basis. Investments in liquid assets are adjusted based on expected loan demand, projected loan and investment securities maturities and payments, expected deposit flows and the objectives set by the Company's asset-liability management policy. The Company had liquid assets (cash and cash equivalents) of $56,723 as of March 31, 2016 compared with $72,651 as of December 31, 2015.

As of March 31, 2016, West Bank had additional borrowing capacity available from the FHLB of approximately $206,000, as well as $67,000 through unsecured federal funds lines of credit with correspondent banks. Net cash from operating activities contributed $7,099 and $7,328 to liquidity for the three months ended March 31, 2016 and 2015, respectively. The combination of high levels of potentially liquid assets, cash flows from operations, and additional borrowing capacity provided the Company with strong liquidity as of March 31, 2016.

The Company's total stockholders' equity increased to $156,926 at March 31, 2016 from $152,377 at December 31, 2015. The increase was primarily the result of net income less dividends paid and an increase in accumulated other comprehensive income.

At March 31, 2016, the Company's tangible common equity as a percent of tangible assets was 8.94 percent compared to 8.72 percent as of December 31, 2015.

The Company and West Bank are subject to various regulatory capital requirements administered by federal and state banking agencies. Failure to meet minimum capital requirements (as shown in the following table) can result in certain mandatory and possibly additional discretionary actions by regulators, which, if undertaken, could have a direct material effect on the Company's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and West Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance sheet items as calculated under regulatory accounting practices. The Company's and West Bank's capital amounts and classifications are also subject to qualitative judgments by the regulators about components, risk weightings and other factors. Management believes the Company and West Bank met all capital adequacy requirements to which they were subject as of March 31, 2016.

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West Bancorporation, Inc.
Management's Discussion and Analysis
(in thousands, except share and per share data)

The Company's and West Bank's capital amounts and ratios are presented in the following table.

	Actual		For Capital Adequacy Purposes With Capital Conservation Buffer		To Be Well-Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of March 31, 2016:						
Total Capital (to Risk-Weighted Assets)						
Consolidated	$191,426	11.94%	$138,311	8.625%	N/A	N/A
West Bank	177,850	11.19%	137,107	8.625%	$158,965	10.00%
Tier 1 Capital (to Risk-Weighted Assets)						
Consolidated	176,127	10.98%	106,239	6.625%	N/A	N/A
West Bank	162,551	10.23%	105,314	6.625%	127,172	8.00 %
Common Equity Tier 1 Capital (to Risk-Weighted Assets)						
Consolidated	156,127	9.74 %	82,185	5.125%	N/A	N/A
West Bank	162,551	10.23%	81,470	5.125%	103,327	6.50 %
Tier 1 Leverage						
Consolidated	176,127	10.11%	69,664	4.00 %	N/A	N/A
West Bank	162,551	9.39 %	69,244	4.00 %	86,555	5.00 %
As of December 31, 2015:						
Total Capital (to Risk-Weighted Assets)						
Consolidated	$187,790	12.12%	$123,979	8.00 %	N/A	N/A
West Bank	174,450	11.32%	123,279	8.00 %	$154,099	10.00%
Tier 1 Capital (to Risk-Weighted Assets)						
Consolidated	172,807	11.15%	92,984	6.00 %	N/A	N/A
West Bank	159,467	10.35%	92,460	6.00 %	123,279	8.00 %
Common Equity Tier 1 Capital (to Risk-Weighted Assets)						
Consolidated	152,807	9.86 %	69,738	4.50 %	N/A	N/A
West Bank	159,467	10.35%	69,345	4.50 %	100,164	6.50 %
Tier 1 Leverage						
Consolidated	172,807	9.91 %	69,764	4.00 %	N/A	N/A
West Bank	159,467	9.20 %	69,352	4.00 %	86,690	5.00 %

On January 1, 2015, the Company and West Bank became subject to the rules of the Basel III regulatory capital framework and related Dodd-Frank Wall Street Reform and Consumer Protection Act changes. The new rules included the implementation of a new capital conservation buffer that is added to the minimum requirements for capital adequacy purposes. The capital conservation buffer is subject to a three year phase-in period that began on January 1, 2016 and will be fully phased-in on January 1, 2019 at 2.5 percent. The required phase-in capital conservation buffer during 2016 is 0.625 percent. A banking organization with a conservation buffer of less than the required amount will be subject to limitations on capital distributions, including dividend payments and certain discretionary bonus payments to executive officers. At March 31, 2016, the ratios for the Company and West Bank were sufficient to meet the fully phased-in conservation buffer.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of earnings volatility that results from adverse changes in interest rates and market prices. The Company's market risk is primarily interest rate risk arising from its core banking activities of lending and deposit taking. Interest rate risk is the risk that the change in market interest rates may adversely affect the Company's net interest income. Management continually develops and implements strategies to mitigate this risk. The analysis of the Company's interest rate risk as of December 31, 2015 was presented in the Company's Form 10-K filed with the Securities and Exchange Commission on March 3, 2016. The Company has not experienced any material changes to its interest rate risk position since December 31, 2015. Management does not believe that the Company's primary market risk exposure and management of that exposure in the first three months of 2016 materially changed compared to those in the year ended December 31, 2015.

Item 4. Controls and Procedures

a. Evaluation of disclosure controls and procedures. As of the end of the period covered by this report, an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) was performed under the supervision, and with the participation, of the Company's Chief Executive Officer and Chief Financial Officer. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act was recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

b. Changes in internal controls over financial reporting. There were no changes in the Company's internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II - OTHER INFORMATION

Item 1. Legal Proceedings

Information required by this item is set forth in Note 8 of the Notes to Consolidated Financial Statements included in Part I Item 1 of this report and is incorporated herein by reference.

Item 1A. Risk Factors

Management does not believe there have been any material changes in the risk factors that were disclosed in the Company's Form 10-K filed with the Securities and Exchange Commission on March 3, 2016.

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

During the first quarter of 2016, there were no purchases of the Company's common shares under the existing stock repurchase plan. The current authorization of the stock repurchase plan expired in April 2016 and was not renewed by the the Board of Directors.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

The following exhibits are filed as part of this report:

Exhibits	Description
31.1	Certification of Chief Executive Officer under Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer under Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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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.

West Bancorporation, Inc.
(Registrant)

April 28, 2016	By: /s/ David D. Nelson
Date	David D. Nelson
	Chief Executive Officer and President
	(Principal Executive Officer)
April 28, 2016	By: /s/ Douglas R. Gulling
Date	Douglas R. Gulling
	Executive Vice President, Treasurer and Chief Financial Officer
	(Principal Financial Officer)
April 28, 2016	By: /s/ Marie I. Roberts
Date	Marie I. Roberts
	Senior Vice President, Controller and Chief Accounting Officer
	(Principal Accounting Officer)

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