

HFF, Inc.
Form 10-Q
November 10, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2014

OR

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

For the transition period from _____ to _____

Commission file number: 001-33280

HFF, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State of Incorporation)

51-0610340
(I.R.S. Employer

Identification No.)

One Oxford Centre
301 Grant Street, Suite 600
Pittsburgh, Pennsylvania
(Address of Principal Executive Offices)

15219
(Zip code)

(412) 281-8714

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer

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

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

Number of shares of Class A common stock, par value \$0.01 per share, of the registrant outstanding as of October 31, 2014 was 37,676,946 shares.

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HFF, INC. AND SUBSIDIARIES

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements, which reflect our current views with respect to, among other things, our operations and financial performance. You can identify these forward-looking statements by the use of words such as outlook, believes, expects, potential, continues, may, will, should, approximately, predicts, intends, plans, estimates, anticipates or the negative version of these words or other comparable words. Such forward-looking statements are subject to various risks and uncertainties. Accordingly, there are or will be important factors that could cause actual outcomes or results to differ materially from those indicated in these statements. We believe these factors include, but are not limited to, those described under the caption Risk Factors in our Annual Report on Form 10-K and this Quarterly Report on Form 10-Q. These factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included in this Quarterly Report on Form 10-Q. We undertake no obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise.

SPECIAL NOTE REGARDING THE REGISTRANT

In connection with our initial public offering of our Class A common stock in February 2007, we effected a reorganization of our business, which had previously been conducted through HFF Holdings LLC (HFF Holdings) and certain of its wholly-owned subsidiaries, including Holliday Fenoglio Fowler, L.P. and HFF Securities L.P. (together, the Operating Partnerships) and Holliday GP Corp. (Holliday GP). In the reorganization, HFF, Inc., a newly-formed Delaware corporation, purchased from HFF Holdings all of the shares of Holliday GP, which is the sole general partner of each of the Operating Partnerships, and approximately 44.7% of the partnership units in each of the Operating Partnerships (including partnership units in the Operating Partnerships held by Holliday GP) in exchange for the net proceeds from the initial public offering and one share of Class B common stock of HFF, Inc. Following this reorganization, HFF, Inc. became and continues to be a holding company holding partnership units in the Operating Partnerships and all of the outstanding shares of Holliday GP. As of August 31, 2012, HFF Holdings had exchanged all of the remaining partnership units in each of the Operating Partnerships for shares of Class A common stock of the Company pursuant to the Exchange Right (as defined in this Quarterly Report on Form 10-Q). As of August 31, 2012 and continuing through the filing date of this Quarterly Report on Form 10-Q, HFF, Inc. through its wholly-owned subsidiaries, holds 100% of the partnership units in the Operating Partnerships and is the only equity holder of the Operating Partnerships. Since all of the partnership units had been exchanged, the Class B common stock of the Company was transferred to the Company and retired on August 31, 2012, in accordance with the Company's certificate of incorporation. We refer to these transactions collectively in this Quarterly Report on Form 10-Q as the Reorganization Transactions. Unless we state otherwise, the information in this Quarterly Report on Form 10-Q gives effect to these Reorganization Transactions.

Unless the context otherwise requires, references to (1) HFF Holdings refer solely to HFF Holdings LLC, a Delaware limited liability company that was previously the holding company for our consolidated subsidiaries, and not to any of its subsidiaries, (2) HFF LP refer to Holliday Fenoglio Fowler, L.P., a Texas limited partnership, (3) HFF Securities refer to HFF Securities L.P., a Delaware limited partnership and registered broker-dealer, (4) Holliday GP refer to Holliday GP Corp., a Delaware corporation and the general partner of HFF LP and HFF Securities, (5) HoldCo LLC refer to HFF Partnership Holdings LLC, a Delaware limited liability company and a wholly-owned subsidiary of HFF, Inc., and (6) Holdings Sub refer to HFF LP Acquisition LLC, a Delaware limited liability company and wholly-owned subsidiary of HFF Holdings (together, the Holdings Affiliates). Our business operations are conducted by HFF LP and HFF Securities, which are sometimes referred to in this Quarterly Report on Form 10-Q as the Operating Partnerships. Also, except where specifically noted, references in this Quarterly Report on Form 10-Q to the Company, we or us mean HFF, Inc., a Delaware corporation and its consolidated subsidiaries, after giving effect to the Reorganization Transactions.

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements**

HFF, Inc.

Consolidated Balance Sheets

*(Dollars in Thousands)**(Current period unaudited)*

| | September 30, 2014 | December 31, 2013 |
|--|-----------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 160,709 | \$ 201,262 |
| Accounts receivable | 3,693 | 1,093 |
| Receivable from affiliate | 2 | |
| Mortgage notes receivable | 189,847 | 93,587 |
| Prepaid taxes | 1,266 | 1,000 |
| Prepaid expenses and other current assets | 3,265 | 2,495 |
| Deferred tax asset, net | 3,953 | 8,779 |
| | | |
| Total current assets, net | 362,735 | 308,216 |
| Property and equipment, net | 7,987 | 6,586 |
| Deferred tax asset, net | 143,736 | 152,320 |
| Goodwill | 3,712 | 3,712 |
| Intangible assets, net | 17,498 | 16,776 |
| Other noncurrent assets | 1,132 | 566 |
| | | |
| Total Assets | \$ 536,800 | \$ 488,176 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities: | | |
| Current portion of long-term debt | \$ 301 | \$ 258 |
| Warehouse line of credit | 189,847 | 93,587 |
| Accrued compensation and related taxes | 39,085 | 53,253 |
| Accounts payable | 1,275 | 1,378 |
| Payable under tax receivable agreement | 10,789 | 10,831 |
| Other current liabilities | 7,802 | 12,524 |
| | | |
| Total current liabilities | 249,099 | 171,831 |
| Deferred rent credit | 6,014 | 5,801 |
| Payable under the tax receivable agreement, less current portion | 123,367 | 134,785 |
| Long-term debt, less current portion | 406 | 185 |

| | | |
|---|-------------------|------------|
| Total liabilities | 378,886 | 312,602 |
| Stockholders' equity: | | |
| Class A common stock, par value \$0.01 per share, 175,000,000 authorized; 38,124,328 and 37,498,796 shares issued, respectively; 37,676,946 and 37,248,416 shares outstanding, respectively | 381 | 372 |
| Treasury stock, 447,382 and 250,380 shares at cost, respectively | (9,042) | (2,760) |
| Additional paid-in-capital | 99,562 | 76,097 |
| Retained earnings | 67,013 | 101,865 |
| Total equity | 157,914 | 175,574 |
| Total liabilities and stockholders' equity | \$ 536,800 | \$ 488,176 |

See accompanying notes to the consolidated financial statements.

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HFF, Inc.

Consolidated Statements of Income

*(Dollars in Thousands, except per share data)**(Unaudited)*

| | Three Months Ended | | Nine Months Ended | |
|---|-----------------------|-----------|-----------------------|------------|
| | September 30, 2014 | 2013 | September 30, 2014 | 2013 |
| Revenues | | | | |
| Capital markets services revenue | \$ 110,786 | \$ 88,546 | \$ 279,506 | \$ 221,509 |
| Interest on mortgage notes receivable | 1,213 | 299 | 2,346 | 1,619 |
| Other | 612 | 569 | 1,577 | 1,509 |
| | 112,611 | 89,414 | 283,429 | 224,637 |
| Expenses | | | | |
| Cost of services | 63,761 | 49,752 | 163,178 | 131,186 |
| Personnel | 11,268 | 11,029 | 36,343 | 28,223 |
| Occupancy | 2,454 | 2,406 | 7,137 | 6,701 |
| Travel and entertainment | 2,414 | 2,130 | 8,485 | 6,698 |
| Supplies, research, and printing | 1,556 | 1,307 | 4,576 | 3,710 |
| Insurance | 512 | 490 | 1,527 | 1,478 |
| Professional fees | 929 | 970 | 3,267 | 2,902 |
| Depreciation and amortization | 1,966 | 1,550 | 5,902 | 5,146 |
| Interest on warehouse line of credit | 638 | 142 | 1,252 | 977 |
| Other operating | 1,330 | 993 | 4,155 | 3,682 |
| | 86,828 | 70,769 | 235,822 | 190,703 |
| Operating income | 25,783 | 18,645 | 47,607 | 33,934 |
| Interest and other income, net | 4,144 | 3,546 | 10,295 | 14,157 |
| Interest expense | (16) | (8) | (32) | (26) |
| (Increase) decrease in payable under the tax receivable agreement | 299 | (701) | 800 | (1,040) |
| Income before income taxes | 30,210 | 21,482 | 58,670 | 47,025 |
| Income tax expense | 12,184 | 8,137 | 24,329 | 18,264 |
| Net income | \$ 18,026 | \$ 13,345 | \$ 34,341 | \$ 28,761 |
| Earnings per share - Basic and Diluted | | | | |
| Income available to HFF, Inc. common stockholders - Basic | \$ 0.48 | \$ 0.36 | \$ 0.91 | \$ 0.77 |

| | | | | | | | | |
|---|----|-------------|----|------|----|-------------|----|------|
| Income available to HFF, Inc. common stockholders - Diluted | \$ | 0.47 | \$ | 0.35 | \$ | 0.91 | \$ | 0.76 |
|---|----|-------------|----|------|----|-------------|----|------|

See accompanying notes to the consolidated financial statements.

Table of Contents**HFF, Inc.****Consolidated Statements of Stockholders Equity***(Dollars in Thousands, except share data)**(Unaudited)*

| | Common Stock | | Treasury Stock | | Additional Paid in Capital | Retained Earnings | Total Equity |
|--|--------------|--------|----------------|------------|----------------------------------|----------------------|-----------------|
| | Shares | Amount | Shares | Amount | | | |
| Stockholders equity, December 31, 2013 | 37,248,416 | \$ 372 | 250,380 | \$ (2,760) | \$ 76,097 | \$ 101,865 | \$ 175,574 |
| Stock compensation and other, net | | | | | 21,476 | | 21,476 |
| Excess tax benefits from share-based award activities | | | | | 971 | | 971 |
| Issuance of Class A common stock, net | 625,532 | 9 | | | (9) | | |
| Repurchase of Class A common stock | (197,002) | | 197,002 | (6,282) | | | (6,282) |
| Dividends paid | | | | | 1,027 | (69,193) | (68,166) |
| Net income | | | | | | 34,341 | 34,341 |
| Stockholders equity, September 30, 2014 | 37,676,946 | \$ 381 | 447,382 | \$ (9,042) | \$ 99,562 | \$ 67,013 | \$ 157,914 |
| | | | | | | | |
| | Common Stock | | Treasury Stock | | Additional Paid in Capital | Retained Earnings | Total Equity |
| | Shares | Amount | Shares | Amount | | | |
| Stockholders equity, December 31, 2012 | 37,063,844 | \$ 371 | 157,617 | \$ (1,055) | \$ 71,267 | \$ 50,439 | \$ 121,022 |
| Stock compensation and other, net | | | | | 3,986 | | 3,986 |
| Excess tax benefits from share-based award activities | | | | | 494 | | 494 |
| Issuance of Class A common stock, net | 277,335 | 2 | | | | | 2 |
| Repurchase of Class A common stock | (92,763) | (1) | 92,763 | (1,705) | | | (1,706) |
| Net income | | | | | | 28,761 | 28,761 |
| Stockholders equity, September 30, 2013 | 37,248,416 | \$ 372 | 250,380 | \$ (2,760) | \$ 75,747 | \$ 79,200 | \$ 152,559 |

See accompanying notes to the consolidated financial statements.

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HFF, Inc.

Consolidated Statements of Cash Flows

*(Dollars In Thousands)**(Unaudited)*

| | Nine Months Ended September 30, | |
|---|--|-------------|
| | 2014 | 2013 |
| Operating activities | | |
| Net income | \$ 34,341 | \$ 28,761 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Stock based compensation | 8,242 | 6,450 |
| Excess tax benefits from share-based award activities | (971) | (494) |
| Deferred taxes | 13,410 | 7,644 |
| (Decrease) increase in payable under the tax receivable agreement | (800) | 1,040 |
| Depreciation and amortization: | | |
| Property and equipment | 1,556 | 1,262 |
| Intangibles | 4,347 | 3,885 |
| Gain on sale or disposition of assets, net | (3,636) | (6,684) |
| Mortgage service rights assumed | (3,023) | (1,569) |
| Proceeds from sale of mortgage servicing rights | 1,590 | 5,425 |
| Increase (decrease) in cash from changes in: | | |
| Accounts receivable | (2,600) | (1,942) |
| Receivable from affiliates | (2) | 124 |
| Payable under the tax receivable agreement | (10,660) | (10,368) |
| Mortgage notes receivable | (96,260) | 254,612 |
| Net borrowings on warehouse line of credit | 96,260 | (254,612) |
| Prepaid taxes, prepaid expenses and other current assets | (1,036) | (3,579) |
| Other noncurrent assets | (566) | 141 |
| Accrued compensation and related taxes | (934) | 7,400 |
| Accounts payable | (103) | 232 |
| Other accrued liabilities | (3,751) | (1,417) |
| Other long-term liabilities | 213 | 1,366 |
| Net cash provided by operating activities | 35,617 | 37,677 |
| Investing activities | | |
| Purchases of property and equipment | (2,440) | (3,272) |
| Net cash used in investing activities | (2,440) | (3,272) |
| Financing activities | | |
| Payments on long-term debt | (253) | (257) |
| Excess tax benefits from share-based award activities | 971 | 494 |
| Dividends paid | (68,166) | |

| | | |
|--|------------|------------|
| Treasury stock | (6,282) | (1,705) |
| Net cash used in financing activities | (73,730) | (1,468) |
| Net (decrease) increase in cash | (40,553) | 32,937 |
| Cash and cash equivalents, beginning of period | 201,262 | 126,331 |
| Cash and cash equivalents, end of period | \$ 160,709 | \$ 159,268 |

See accompanying notes to the consolidated financial statements.

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HFF, Inc.

Notes to Consolidated Financial Statements

1. Organization and Basis of Presentation**Organization**

HFF, Inc., a Delaware corporation (the Company), through its Operating Partnerships, Holliday Fenoglio Fowler, L.P., a Texas limited partnership (HFF LP), and HFF Securities L.P., a Delaware limited partnership and registered broker-dealer (HFF Securities and together with HFF LP, the Operating Partnerships), is a commercial real estate financial intermediary providing commercial real estate and capital markets services including debt placement, investment sales, equity placements, investment banking and advisory services, loan sales and loan sale advisory services, commercial loan servicing, and capital markets advice and maintains 23 offices in the United States.

Initial Public Offering and Reorganization

The Company was formed in November 2006 in connection with a proposed initial public offering of its Class A common stock. On November 9, 2006, the Company filed a registration statement on Form S-1 with the United States Securities and Exchange Commission (the SEC) relating to a proposed underwritten initial public offering of 14,300,000 shares of Class A common stock of the Company (the Offering). On January 30, 2007, the SEC declared the registration statement on Form S-1 effective and the Company priced 14,300,000 shares for the initial public offering at a price of \$18.00 per share. On January 31, 2007, the Company's common stock began trading on the New York Stock Exchange under the symbol HF.

The proceeds of the Offering were used to purchase from HFF Holdings LLC, a Delaware limited liability company (HFF Holdings), all of the shares of Holliday GP Corp. (Holiday GP) and partnership units representing approximately 38.9% of each of the Operating Partnerships (including partnership units in the Operating Partnerships held by Holliday GP).

On February 21, 2007, the underwriters exercised their option to purchase an additional 2,145,000 shares of Class A common stock (15% of original issuance) at \$18.00 per share. These proceeds were used to purchase HFF Holdings partnership units representing approximately 5.8% of each of the Operating Partnerships. The Company did not retain any of the proceeds from the Offering.

In addition to cash received for its sale of all of the shares of Holliday GP and approximately 44.7% of partnership units of each of the Operating Partnerships (including partnership units in the Operating Partnerships held by Holliday GP), HFF Holdings also received, through the issuance of one share of the Company's Class B common stock to HFF Holdings, an exchange right that permitted HFF Holdings to exchange interests in the Operating Partnerships for shares of (i) the Company's Class A common stock (the Exchange Right) and (ii) rights under a tax receivable agreement between the Company and HFF Holdings. Since all of the partnership units had been exchanged as of August 31, 2012, the Class B common stock was transferred to the Company and retired on August 31, 2012 in accordance with the Company's certificate of incorporation. See Note 12 for further discussion of the tax receivable agreement.

As a result of the reorganization, the Company became a holding company through a series of transactions pursuant to a sale and purchase agreement. Pursuant to the Offering and reorganization, the Company's sole assets are, through its wholly-owned subsidiary HFF Partnership Holdings, LLC, a Delaware limited liability company (HoldCo LLC),

partnership interests of HFF LP and HFF Securities and all of the shares of Holliday GP. The transactions that occurred in connection with the initial public offering and reorganization are referred to as the Reorganization Transactions.

Basis of Presentation

The accompanying consolidated financial statements of the Company as of September 30, 2014 and December 31, 2013 and for the three and nine month periods ended September 30, 2014 and September 30, 2013, include the accounts of HFF LP, HFF Securities, and the Company's wholly-owned subsidiaries, Holliday GP and HoldCo LLC. All significant intercompany accounts and transactions have been eliminated.

The purchase of shares of Holliday GP and partnership units in each of the Operating Partnerships are treated as a reorganization under common control for financial reporting purposes. HFF Holdings owned 100% of Holliday GP, HFF LP Acquisition, LLC, a Delaware limited liability company (Holdings Sub), and the Operating Partnerships prior to the Reorganization Transactions. The

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initial purchase of shares of Holliday GP and the initial purchase of units in the Operating Partnerships were accounted for at historical cost, with no change in basis for financial reporting purposes. Accordingly, the net assets of HFF Holdings purchased by the Company are reported in the consolidated financial statements of the Company at HFF Holdings' historical cost.

As the sole stockholder of Holliday GP (the sole general partner of the Operating Partnerships), the Company now operates and controls all of the business and affairs of the Operating Partnerships. The Company consolidates the financial results of the Operating Partnerships.

Pending Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board issued changes to revenue recognition with customers. This update provides a five-step analysis of transactions to determine when and how revenue is recognized. An entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This update will be effective for the Company beginning in fiscal year 2017. This update may be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying this update recognized at the date of initial application. The Company is currently evaluating the impact of the new guidance on its consolidated financial statements.

2. Summary of Significant Accounting Policies

These interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information, the instructions to Quarterly Report on Form 10-Q and Rule 10-01 of Regulation S-X and should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2013. Accordingly, significant accounting policies and disclosures normally provided have been omitted as such items are disclosed therein. In the opinion of management, all adjustments consisting of normal and recurring entries considered necessary for a fair presentation of the results for the interim periods presented have been included. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect reported amounts in the financial statements and accompanying notes. These estimates are based on information available as of the date of the unaudited consolidated financial statements. Therefore, actual results could differ from those estimates. Furthermore, operating results for the three and nine months ended September 30, 2014 are not necessarily indicative of the results expected for the year ending December 31, 2014.

The Company has a firm profit participation plan and office profit participation plans (the Plans) that allow for incentive payments to be made, based on achieving various performance metrics, either in the form of cash or stock at the election of the Company's board of directors. The expense associated with the Plans is included within personnel expenses in the consolidated statements of income. The expense recorded for these Plans is estimated during the year based on actual results at each interim reporting date and an estimate of future results for the remainder of the year. The Plans allow for payments to be made in both cash and share-based awards, the composition of which is determined in the first calendar quarter of the subsequent year. Cash and share-based awards issued under these Plans are subject to vesting conditions over the subsequent year, such that the total expense measured for these Plans is recorded over the period from the beginning of the performance year through the vesting date. Based on an accounting policy election, the expense associated with the share-based component of the estimated incentive payout is recognized before the grant date of the share-based awards due to the fact that the terms of the Plans have been approved by the Company's board of directors and the employees of the Company understand the requirements to earn the award. Prior to the grant date, the share-based component expense is recorded as incentive compensation expense

within personnel expenses in the Company's consolidated statements of income. Following the award, if any, of the related incentive payout, the share-based component expense is reclassified as stock compensation costs within personnel expenses and the share-based component of the accrued incentive compensation is reclassified as additional paid-in-capital upon the granting of the awards on the Company's consolidated balance sheets.

3. Stock Compensation

The stock compensation cost that has been charged against income for the three and nine months ended September 30, 2014 was \$1.6 million and \$8.2 million, respectively, which is recorded in personnel expenses in the consolidated statements of income. The stock compensation cost that has been charged against income for the three and nine months ended September 30, 2013 was \$3.2 million and \$6.4 million, respectively. At September 30, 2014, there was approximately \$20.2 million of unrecognized compensation cost related to non-vested restricted stock units with a weighted average remaining contractual term of 3.7 years. As of September 30, 2014, there were 895,123 restricted stock units outstanding. Stock compensation expense related to the liability awards, which final vesting was on March 1, 2014, that has been included within income for the three and nine months ended September 30, 2014 was \$0.0 million and \$3.3 million, respectively. Stock compensation expense related to the liability awards that has been included within income for the three and nine months ended September 30, 2013 was \$2.9 million and \$4.9 million, respectively.

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During the three month period ended September 30, 2014, no options were granted, vested, exercised or forfeited.

During the three month period ended September 30, 2014, no new restricted stock units were granted or vested, and no restricted stock units were forfeited.

The fair value of vested restricted stock units was \$4.3 million at September 30, 2014.

4. Property and Equipment

Property and equipment consist of the following (dollars in thousands):

| | September 30, 2014 | December 31, 2013 |
|--|-----------------------|----------------------|
| Furniture and equipment | \$ 6,212 | \$ 5,066 |
| Computer equipment | 1,142 | 970 |
| Capitalized software costs | 703 | 530 |
| Leasehold improvements | 8,807 | 7,786 |
| Subtotal | 16,864 | 14,352 |
| Less accumulated depreciation and amortization | (8,877) | (7,766) |
| | \$ 7,987 | \$ 6,586 |

At September 30, 2014 and December 31, 2013, the Company has recorded, within furniture and equipment, office equipment under capital leases of \$1.4 million and \$1.1 million, respectively, including accumulated amortization of \$0.7 million and \$0.7 million, respectively, which is included within depreciation and amortization expense in the accompanying consolidated statements of income. See Note 7 for discussion of the related capital lease obligations.

5. Intangible Assets

The Company's intangible assets are summarized as follows (dollars in thousands):

| | September 30, 2014 | | | December 31, 2013 | | |
|----------------------------------|-----------------------------|-----------------------------|----------------------|-----------------------------|-----------------------------|----------------------|
| | Gross Carrying Amount | Accumulated Amortization | Net Book Value | Gross Carrying Amount | Accumulated Amortization | Net Book Value |
| Amortizable intangible assets: | | | | | | |
| Mortgage servicing rights | \$ 36,973 | \$ (19,575) | \$ 17,398 | \$ 34,100 | \$ (17,424) | \$ 16,676 |
| Unamortizable intangible assets: | | | | | | |
| FINRA license | 100 | | 100 | 100 | | 100 |
| Total intangible assets | \$ 37,073 | \$ (19,575) | \$ 17,498 | \$ 34,200 | \$ (17,424) | \$ 16,776 |

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As of September 30, 2014 and December 31, 2013, the Company serviced \$37.1 billion and \$33.1 billion, respectively, of commercial loans. The Company earned \$4.3 million and \$12.5 million in servicing fees and interest on float and escrow balances for the three and nine month periods ending September 30, 2014, respectively. The Company earned \$4.0 million and \$11.8 million in servicing fees and interest on float and escrow balances for the three and nine month periods ending September 30, 2013, respectively. These revenues are recorded as capital markets services revenues in the consolidated statements of income.

The total commercial loan servicing portfolio includes loans for which there are no corresponding mortgage servicing rights recorded on the balance sheet, as these servicing rights were assumed prior to the Company's adoption of ASC 860, *Transfers and Servicing* (ASC 860) on January 1, 2007 and involved no initial consideration paid by the Company. The Company recorded mortgage servicing rights of \$17.4 million and \$16.7 million on \$32.1 billion and \$27.0 billion, respectively, of the total loans serviced as of September 30, 2014 and December 31, 2013.

The Company stratifies its servicing portfolio based on the type of loan, including life company loans, commercial mortgage backed securities (CMBS), Freddie Mac and limited-service life company loans.

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Changes in the carrying value of mortgage servicing rights for the nine month periods ended September 30, 2014 and 2013, were as follows (dollars in thousands):

| Category | 12/31/13 | Capitalized | Amortized | Sold / | |
|----------------------|------------------|-----------------|-------------------|-----------------|------------------|
| | | | | Transferred | 9/30/14 |
| Freddie Mac | \$ 3,730 | \$ 2,465 | \$ (1,265) | \$ (1,831) | \$ 3,099 |
| CMBS | 10,978 | 1,637 | (1,962) | 1,412 | 12,065 |
| Life company | 1,537 | 1,231 | (930) | | 1,838 |
| Life company limited | 431 | 155 | (190) | | 396 |
| Total | \$ 16,676 | \$ 5,488 | \$ (4,347) | \$ (419) | \$ 17,398 |

| Category | 12/31/12 | Capitalized | Amortized | Sold / | |
|----------------------|------------------|-----------------|-------------------|-------------------|------------------|
| | | | | Transferred | 9/30/13 |
| Freddie Mac | \$ 7,641 | \$ 2,463 | \$ (1,041) | \$ (5,133) | \$ 3,930 |
| CMBS | 7,838 | 606 | (1,463) | 3,948 | 10,929 |
| Life company | 2,021 | 748 | (1,236) | | 1,533 |
| Life company limited | 299 | 215 | (138) | | 376 |
| Total | \$ 17,799 | \$ 4,032 | \$ (3,878) | \$ (1,185) | \$ 16,768 |

Amounts capitalized represent mortgage servicing rights retained upon the sale of originated loans to Freddie Mac and mortgage servicing rights acquired without the exchange of initial consideration. The Company recorded mortgage servicing rights retained upon the sale of originated loans to Freddie Mac of \$1.0 million and \$2.5 million on \$406.1 million and \$937.6 million of loans, respectively, during the three and nine month periods ending September 30, 2014, respectively and \$0.6 million and \$2.5 million on \$181.0 million and \$829.9 million of loans, respectively, during the three and nine month periods ending September 30, 2013, respectively. The Company recorded mortgage servicing rights acquired without the exchange of initial consideration on the CMBS and Life company tranches of \$0.8 million and \$3.0 million on \$2.4 billion and \$5.9 billion of loans, respectively, during the three and nine month periods ending September 30, 2014, respectively and \$0.7 million and \$1.6 million on \$1.5 billion and \$3.6 billion of loans, respectively, during the three and nine month periods ending September 30, 2013. During the nine months ending September 30, 2014 and 2013, the Company sold the cashiering portion of certain Freddie Mac mortgage servicing rights. While the Company transferred the risks and rewards of ownership of the cashiering portion of the mortgage servicing rights, the Company continues to perform limited servicing activities on these loans for a reduced market-based fee. Therefore, the remaining servicing rights were transferred to the CMBS servicing tranche. The net result of these transactions was the Company recording a gain in the three and nine months ending September 30, 2014 of \$0.5 million and \$1.2 million, respectively, and \$1.1 million and \$4.2 million during the three and nine month periods ending September 30, 2013, respectively, within interest and other income, net in the consolidated statements of income. The Company also received securitization compensation in relation to the sale of the cashiering portion of certain Freddie Mac mortgage servicing rights in the three and nine months ending September 30, 2014 of \$0.8 million and \$1.5 million, respectively, and \$0.8 million and \$4.4 million during the three and nine month periods ending September 30, 2013, respectively. The securitization compensation is recorded within interest and other income, net in the consolidated statements of income.

Amortization expense related to intangible assets was \$1.4 million and \$4.3 million during the three and nine month periods ended September 30, 2014 and \$1.1 million and \$3.9 million during the three and nine month periods ending September 30, 2013, respectively, and is recorded in depreciation and amortization in the consolidated statements of income.

Estimated amortization expense for the next five years is as follows (dollars in thousands):

| | |
|-------------------|----------|
| Remainder of 2014 | \$ 1,222 |
| 2015 | 4,374 |
| 2016 | 3,537 |
| 2017 | 2,529 |
| 2018 | 1,879 |
| 2019 | 1,399 |

The weighted-average life of the mortgage servicing rights intangible asset was 5.9 years at September 30, 2014.

Table of Contents**6. Fair Value Measurement**

ASC Topic 820, *Fair Value Measurement* (ASC 820) establishes a valuation hierarchy for disclosure of the inputs to valuation used to measure fair value. This hierarchy prioritizes the inputs into the following three levels: Level 1 inputs which are quoted market prices in active markets for identical assets or liabilities; Level 2 inputs which are observable market-based inputs or unobservable inputs corroborated by market data for the asset or liability; and Level 3 inputs which are unobservable inputs based on our own assumptions that are not corroborated by market data. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

As of September 30, 2014, the Company did not have any financial assets or liabilities recognized at fair value on a recurring basis.

In accordance with generally accepted accounting principles, from time to time, the Company measures certain assets at fair value on a nonrecurring basis. These assets may include mortgage servicing rights and mortgage notes receivable. The mortgage servicing rights are recorded at fair value upon initial recording and were not re-measured at fair value during the third quarter of 2014 because the Company continues to utilize the amortization method under ASC 860 and the fair value of the mortgage servicing rights exceeds the carrying value at September 30, 2014. The fair value of the mortgage notes receivable was based on prices observable in the market for similar loans and equaled carrying value at September 30, 2014. Therefore, no lower of cost or fair value adjustment was required.

The following table sets forth the Company's financial assets that were accounted for at fair value on a nonrecurring basis by level within the fair value hierarchy as of September 30, 2014 (in thousands):

| | September 30, 2014 | | | |
|---|---|--|-------------------------|--|
| | Fair Value Measurements Using: | | | |
| | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Observable Inputs (Level 2) | Other Inputs | Significant Unobservable Inputs (Level 3) |
| | Carrying Value | | | |
| Nonrecurring fair value measurements | | | | |
| Mortgage notes receivable | \$ 189,847 | \$ | \$ | 189,847 |
| Mortgage servicing rights | 17,398 | | | 22,443 |
| Total nonrecurring fair value measurements | \$ 207,245 | \$ | \$ | 189,847 |
| | | | | 22,443 |

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The following table sets forth the Company's financial assets that were accounted for at fair value on a nonrecurring basis by level within the fair value hierarchy as of December 31, 2013 (in thousands):

| | December 31, 2013 | | | |
|---|---------------------------------------|--------------------------|---------------------|-----------|
| | Fair Value Measurements Using: | | | |
| | Quoted Prices in | | | |
| | Active Markets for | | | |
| | Identical | Significant Other | Significant | |
| | Assets | Inputs | Unobservable | |
| | (Level | (Level 2) | Inputs | |
| | 1) | | (Level 3) | |
| | Carrying | | Value | |
| | Value | | (Level 3) | |
| Nonrecurring fair value measurements | | | | |
| Mortgage notes receivable | \$ 93,587 | \$ | \$ 93,587 | \$ |
| Mortgage servicing rights | 16,676 | | | 20,258 |
| Total nonrecurring fair value measurements | \$ 110,263 | \$ | 93,587 | \$ 20,258 |

Mortgage servicing rights do not trade in an active, open market with readily-available observable prices. Since there is no ready market value for the mortgage servicing rights, such as quoted market prices or prices based on sales or purchases of similar assets, the Company determines the fair value of the mortgage servicing rights by estimating the present value of future cash flows associated with the servicing of the loans. Management makes certain assumptions and judgments in estimating the fair value of servicing rights, including the benefits of servicing (contractual servicing fees and interest on escrow and float balances), the cost of servicing, prepayment rates (including risk of default), an inflation rate, the expected life of the cash flows and the discount rate. The significant assumptions utilized to value servicing rights as of September 30, 2014 and December 31, 2013 are as follows:

| | September 30, 2014 | December 31, 2013 |
|-----------------------------|---------------------------|--------------------------|
| Expected life of cash flows | 3 years to 10.6 years | 3 years to 10 years |
| Discount rate (1) | 15% to 20% | 15% to 20% |
| Prepayment rate | 0% to 8% | 0% to 8% |
| Inflation rate | 2% | 2% |
| Cost of service per loan | \$ 1,600 to \$3,992 | \$ 1,600 to \$4,421 |

- (1) Reflects the time value of money and the risk of future cash flows related to the possible cancellation of servicing contracts, transferability restrictions on certain servicing contracts, concentration in the life company portfolio and large loan risk.

The above assumptions are subject to change based on management's judgments and estimates of future changes in the risks related to future cash flows and interest rates. Changes in these factors would cause a corresponding increase or decrease in the prepayment rates and discount rates used in the Company's valuation model.

FASB ASC Topic 825, *Financial Instruments* also requires disclosure of fair value information about financial instruments, whether or not recognized in the accompanying consolidated balance sheets. Our financial instruments, excluding those included in the preceding fair value tables above, are as follows:

Cash and Cash Equivalents: These balances include cash and cash equivalents with maturities of less than three months. The carrying amount approximates fair value due to the short-term maturities of these instruments; these are considered Level 1 fair values.

Warehouse line of credit: Due to the short-term nature and variable interest rates of this instrument, fair value approximates carrying value; these are considered Level 2 fair values.

Table of Contents**7. Capital Lease Obligations**

Capital lease obligations consist of the following at September 30, 2014 and December 31, 2013 (dollars in thousands):

| | September 30, 2014 | December 31, 2013 |
|---------------------------|-----------------------|----------------------|
| Capital lease obligations | \$ 707 | \$ 443 |
| Less current maturities | 301 | 258 |
| | \$ 406 | \$ 185 |

Capital lease obligations consist primarily of office equipment leases that expire at various dates through April 2017. A summary of future minimum lease payments under capital leases at September 30, 2014 is as follows (dollars in thousands):

| | |
|-------------------|---------------|
| Remainder of 2014 | \$ 95 |
| 2015 | 289 |
| 2016 | 234 |
| 2017 | 89 |
| 2018 | |
| | \$ 707 |

8. Warehouse Line of Credit

HFF LP maintains two uncommitted warehouse revolving lines of credit for the purpose of funding the Freddie Mac mortgage loans that it originates in connection with its services as a Freddie Mac Multifamily Program Plus[®] Seller/Servicer. The Company is party to an uncommitted \$350 million financing arrangement with PNC Bank, N.A. (PNC) and an uncommitted \$125 million financing arrangement with The Huntington Bank (Huntington). In May 2013, availability under the Huntington line increased to \$125 million from \$75 million.

Each funding is separately approved on a transaction-by-transaction basis and is collateralized by a loan and mortgage on a multifamily property that is ultimately purchased by Freddie Mac. The PNC and Huntington financing arrangements are only for the purpose of supporting the Company's participation in Freddie Mac's Program Plus Seller/Servicer program and cannot be used for any other purpose. As of September 30, 2014 and December 31, 2013, HFF LP had \$189.8 million and \$93.6 million, respectively, outstanding on the warehouse lines of credit and a corresponding amount of mortgage notes receivable. Interest on the warehouse lines of credit is at the 30-day LIBOR rate (0.15% and 0.17% at September 30, 2014 and December 31, 2013, respectively) plus a spread. HFF LP is also paid interest on its loan secured by a multifamily loan at the rate in the Freddie Mac note.

9. Lease Commitments

The Company leases various corporate offices and office equipment under noncancelable operating leases. These leases have initial terms of one to ten years. Several of the leases have termination clauses whereby the term may be reduced by two to seven years upon prior notice and payment of a termination fee by the Company. Total rental expense charged to operations was \$1.9 million and \$5.6 million, respectively, during the three and nine month periods ended September 30, 2014 and \$1.9 million and \$5.4 million, respectively, during the three and nine month periods ending September 30, 2013 and is recorded within occupancy expense in the consolidated statements of income.

Future minimum rental payments for the next five years under operating leases with noncancelable terms in excess of one year and without regard to early termination provisions are as follows (dollars in thousands):

| | |
|-------------------|-----------|
| Remainder of 2014 | \$ 1,591 |
| 2015 | 6,192 |
| 2016 | 5,620 |
| 2017 | 5,157 |
| 2018 | 4,543 |
| 2019 | 3,839 |
| Thereafter | 5,650 |
| | \$ 32,592 |

The Company subleases certain office space to subtenants, which subleases may be canceled at any time. The rental income received from these subleases is included as a reduction of occupancy expenses in the accompanying consolidated statements of income.

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The Company also leases certain office equipment under capital leases that expire at various dates through 2017. See Note 4 and Note 7 above for further description of the assets and related obligations recorded under these capital leases at September 30, 2014 and December 31, 2013, respectively.

10. Servicing

The Company services commercial real estate loans for lenders. The unpaid principal balance of the servicing portfolio totaled \$37.1 billion and \$33.1 billion at September 30, 2014 and December 31, 2013, respectively.

In connection with its servicing activities, the Company holds funds in escrow for the benefit of mortgagors for hazard insurance, real estate taxes and other financing arrangements. At September 30, 2014 and December 31, 2013, the funds held in escrow totaled \$161.2 million and \$211.1 million, respectively. These funds, and the offsetting liabilities of the borrowers to external parties, are not presented in the Company's consolidated financial statements as they do not represent the assets and liabilities of the Company. Pursuant to the requirements of the various investors for which the Company services loans, the Company maintains bank accounts, holding escrow funds, which have balances in excess of the FDIC insurance limit. The fees earned on these escrow funds are reported in capital markets services revenue in the consolidated statements of income.

11. Legal Proceedings

The Company is party to various litigation matters, in most cases involving ordinary course and routine claims incidental to its business. The Company cannot estimate with certainty its ultimate legal and financial liability with respect to any pending matters. In accordance with ASC 450, *Contingencies*, a reserve for estimated losses is recorded when the amount is probable and can be reasonably estimated. However, the Company does not believe, based on examination of such pending matters, that a material loss related to these matters is reasonably possible.

12. Income Taxes

Income tax expense includes current and deferred taxes as follows (dollars in thousands):

| | Current | Deferred | Total |
|--|----------------|-----------------|--------------|
| Nine Months Ended September 30, 2014: | | | |
| Federal | \$ 8,903 | \$ 11,613 | \$ 20,516 |
| State | 2,016 | 1,797 | 3,813 |
| | \$ 10,919 | \$ 13,410 | \$ 24,329 |
| Nine Months Ended September 30, 2013: | | | |
| Federal | \$ 9,678 | \$ 7,069 | \$ 16,747 |
| State | 942 | 575 | 1,517 |
| | \$ 10,620 | \$ 7,644 | \$ 18,264 |

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The reconciliation between the income tax computed by applying the U.S. federal statutory rate and the effective tax rate on net income is as follows for the nine months ended September 30, 2014 and 2013 (dollars in thousands):

| Income tax expense / (benefit) | September 30, | | | |
|---|----------------------|--------------|------------------|--------------|
| | 2014 | Rate | 2013 | Rate |
| Taxes computed at federal rate | \$ 20,535 | 35.0% | \$ 16,459 | 35.0% |
| State and local taxes, net of federal tax benefit | 2,647 | 4.5% | 2,247 | 4.8% |
| Effect of deferred tax rate change | 776 | 1.3% | (822) | (1.7)% |
| Change in income tax benefit payable to stockholder | (162) | (0.3)% | (178) | (0.4)% |
| Provision to return adjustment | (49) | (0.1)% | | 0.0% |
| Change in state net operating loss | | 0.0% | (155) | (0.3)% |
| Compensation limitation | 51 | 0.1% | 319 | 0.7% |
| Meals and entertainment | 520 | 0.9% | 397 | 0.8% |
| Other | 11 | 0.0% | (3) | (0.0)% |
| Income tax expense | \$ 24,329 | 41.5% | \$ 18,264 | 38.8% |

Deferred income tax assets and liabilities consist of the following at September 30, 2014 and December 31, 2013 (dollars in thousands):

| | September 30, | December 31, |
|---|----------------------|---------------------|
| | 2014 | 2013 |
| Deferred income tax assets: | | |
| Section 754 election tax basis step-up | \$ 148,014 | \$ 158,229 |
| Tenant improvements | 2,736 | 2,522 |
| Net operating loss carryforward | 36 | 379 |
| Restricted stock units | 3,154 | 5,271 |
| Compensation | 3,287 | 3,805 |
| Intangible asset | 479 | 510 |
| Tax credits | | 123 |
| Other | 408 | 348 |
| Deferred income tax asset | 158,114 | 171,187 |
| Deferred income tax liabilities: | | |
| Goodwill | (1,275) | (1,277) |
| Servicing rights | (6,593) | (6,332) |
| Deferred rent | (1,971) | (1,892) |
| Investment in partnership | (586) | (587) |
| Deferred income tax liability | (10,425) | (10,088) |
| Net deferred income tax asset | \$ 147,689 | \$ 161,099 |

The primary deferred tax asset represents a tax basis step-up election under Section 754 of the Internal Revenue Code (Section 754) made by the Company relating to the initial purchase of units of the Operating Partnerships in connection with the Reorganization Transactions and a tax basis step-up on subsequent exchanges of Operating Partnership units for shares of the Company's Class A common stock since the date of the Reorganization Transactions. As a result of the step-up in basis from these transactions, the Company is entitled to annual future tax benefits in the form of amortization for income tax purposes. The annual pre-tax benefit on the Section 754 step-up and past payments under the tax receivable agreement was approximately \$32.8 million at September 30, 2014. To the extent that the Company does not have sufficient taxable income in a year to fully utilize this annual deduction, the unused benefit is recharacterized as a net operating loss and can then be carried back two years or carried forward for twenty years. The Company measured the deferred tax asset based on the estimated income tax effects of the increase in the tax basis of the assets owned by the Operating Partnerships utilizing the enacted tax rates at the date of the transaction. All subsequent changes in the measurement of the deferred tax assets due to changes in the enacted tax rates or changes in the valuation allowance, if any, are recorded as a component of income tax expense.

In evaluating the realizability of the deferred tax assets, management makes estimates and judgments regarding the level and timing of future taxable income, including projecting future revenue growth and changes to the cost structure. In order to realize the anticipated 2014 pre-tax benefit of approximately \$32.8 million, the Company needs to generate approximately \$268 million in revenue during 2014, assuming a constant cost structure. In the event that the Company cannot realize the anticipated 2014 pre-tax benefit of \$32.8 million, the shortfall becomes a net operating loss that can be carried back two years to offset prior years' taxable income or

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carried forward twenty years to offset future taxable income. Based on this analysis and other quantitative and qualitative factors, management believes that it is currently more likely than not that the Company will be able to generate sufficient taxable income to realize the net deferred tax assets resulting from the basis step up transactions (initial sale of units in the Operating Partnerships and subsequent exchanges of Operating Partnership units since the date of the Reorganization Transactions). The Company has state tax effected net operating loss carryforwards of \$36,000 at September 30, 2014. The state net operating loss carryforwards expire from 2020 through 2028.

The Company will recognize interest and penalties related to unrecognized tax benefits in interest and other income, net in the consolidated statements of income. There were no interest or penalties recorded in the three and nine month periods ending September 30, 2014 and 2013.

Tax Receivable Agreement

In connection with the Reorganization Transactions, HFF LP and HFF Securities made an election under Section 754 for 2007 and kept that election in effect for each taxable year in which an exchange of Operating Partnership partnership units for shares of the Company's Class A common stock occurred. The initial sale as a result of the Offering and subsequent exchanges of Operating Partnership units for shares of Class A common stock produced increases in the tax basis of the assets owned by HFF LP and HFF Securities to their fair market value. This increase in tax basis allows the Company to reduce the amount of tax payments to the extent that the Company has taxable income. As a result of the increase in tax basis, the Company is entitled to future tax benefits of \$148.0 million and has recorded this amount as a deferred tax asset on its consolidated balance sheet. The Company has updated its estimate of these future tax benefits based on the changes to the estimated annual effective tax rate for 2014. The Company is obligated, however, pursuant to its tax receivable agreement with HFF Holdings, to pay to HFF Holdings 85% of the amount of cash savings in U.S. federal, state and local income tax that the Company actually realizes as a result of these increases in tax basis and as a result of certain other tax benefits arising from the Company entering into the tax receivable agreement and making payments under that agreement. For purposes of the tax receivable agreement, actual cash savings in income tax is computed by comparing the Company's actual income tax liability to the amount of such taxes that it would have been required to pay had there been no increase to the tax basis of the assets of HFF LP and HFF Securities as a result of the initial sale and later exchanges had the Company not entered into the tax receivable agreement.

The Company accounts for the income tax effects and corresponding tax receivable agreement effects as a result of the initial purchase and the sale of units of the Operating Partnerships in connection with the Reorganization Transactions and subsequent exchanges of Operating Partnership units for the Company's Class A shares, by recognizing a deferred tax asset for the estimated income tax effects of the increase in the tax basis of the assets owned by the Operating Partnerships, based on enacted tax rates at the date of the transaction, less any tax valuation allowance the Company believes is required. In accordance with ASC 740, the tax effects of transactions with stockholders that result in changes in the tax basis of a company's assets and liabilities will be recognized in equity. If transactions with stockholders result in the recognition of deferred tax assets from changes in the Company's tax basis of assets and liabilities, the valuation allowance initially required upon recognition of these deferred assets will be recorded in equity. Subsequent changes in enacted tax rates or any valuation allowance are recorded as a component of income tax expense.

The Company believes it is more likely than not that it will realize the benefit represented by the deferred tax asset, and, therefore, the Company recorded 85% of this estimated amount of the increase in deferred tax assets as a liability to HFF Holdings under the tax receivable agreement and the remaining 15% of the increase in deferred tax assets directly in additional paid-in capital in stockholders' equity at the time of each exchange of Operating Partnership partnership units for shares of the Company's Class A common stock. As of August 31, 2012, all of the Operating

Partnership partnership units have been exchanged.

While the actual amount and timing of payments under the tax receivable agreement depend upon a number of factors, including the amount and timing of taxable income generated in the future, changes in future tax rates, the value of individual assets, the portion of the Company's payments under the tax receivable agreement constituting imputed interest and increases in the tax basis of the Company's assets resulting in payments to HFF Holdings, the Company has estimated that the future payments that will be made to HFF Holdings will be \$134.2 million, and has recorded this obligation to HFF Holdings as a liability on the consolidated balance sheet. To the extent the Company does not realize all of the tax benefits in future years, this liability to HFF Holdings may be reduced.

In conjunction with the filing of the Company's 2013 federal and state tax returns, the benefit for 2013 relating to the Section 754 basis step-up was finalized resulting in \$12.5 million of tax benefits being realized by the Company. As discussed above, the Company is obligated to remit to HFF Holdings 85% of any such cash savings in federal and state tax. As such, during the third quarter of 2014, the Company paid \$10.7 million to HFF Holdings under the tax receivable agreement. In conjunction with the filing

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of the Company's 2012 federal and state tax returns, the benefit for 2012 relating to the Section 754 basis step-up was finalized resulting in \$12.2 million of tax benefits being realized by the Company and as such, during the third quarter of 2013, the Company paid \$10.4 million to HFF Holdings under the tax receivable agreement. As of September 30, 2014, the Company has made payments to HFF Holdings pursuant to the terms of the tax receivable agreement in an aggregate amount of approximately \$52.6 million and the Company anticipates to make a payment of \$10.8 million to HFF Holdings in 2015.

13. Stockholders Equity

The Company is authorized to issue 175,000,000 shares of Class A common stock, par value \$0.01 per share. Each share of Class A common stock entitles its holder to one vote on all matters to be voted on by stockholders generally. Holders of Class A common stock vote together as a single class on all matters presented to our stockholders for their vote or approval. The Company had issued 38,124,328 and 37,498,796 shares of Class A common stock as of September 30, 2014 and December 31, 2013, respectively.

On January 15, 2014, the Company's board of directors declared a special cash dividend of \$1.83 per share of Class A common stock to stockholders of record on January 27, 2014. The aggregate dividend payment was paid on February 6, 2014 and totaled approximately \$68.2 million based on the number of shares of Class A common stock then outstanding. Additionally, 42,108 restricted stock units (dividend units) were granted for those unvested and vested but not issued restricted stock units as of the record date of January 27, 2014. These dividend units follow the same vesting terms as the underlying restricted stock units.

14. Earnings Per Share

The Company's net income and weighted average shares outstanding for the three and nine month periods ended September 30, 2014 and 2013 consist of the following (dollars in thousands):

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|-------------------------------------|------------|------------------------------------|------------|
| | 2014 | 2013 | 2014 | 2013 |
| Net income | \$ 18,026 | \$ 13,345 | \$ 34,341 | \$ 28,761 |
| Weighted Average Shares Outstanding: | | | | |
| Basic | 37,826,081 | 37,378,037 | 37,735,463 | 37,334,913 |
| Diluted | 38,096,432 | 37,816,501 | 37,906,251 | 37,680,894 |

The calculations of basic and diluted net income per share amounts for the three and nine month periods ended September 30, 2014 and 2013 are described and presented below.

Basic Net Income per Share

Numerator net income for the three and nine month periods ended September 30, 2014 and 2013, respectively.

Denominator the weighted average shares of Class A common stock for the three and nine month periods ended September 30, 2014 and 2013, including 149,417 and 129,621 restricted stock units that have vested and whose issuance is no longer contingent as of September 30, 2014 and September 30, 2013, respectively.

Diluted Net Income per Share

Numerator net income for the three and nine month periods ended September 30, 2014 and 2013 as in the basic net income per share calculation described above.

Denominator the weighted average shares of Class A common stock for the three and nine month periods ended September 30, 2014 and 2013, including 149,417 and 129,621 restricted stock units that have vested and whose issuance is no longer contingent as of September 30, 2014 and September 30, 2013, respectively, plus the dilutive effect of the unvested restricted stock units and stock options.

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| | Three months ended September 30, | | Nine months ended September 30, | |
|--|-------------------------------------|------------|------------------------------------|------------|
| | 2014 | 2013 | 2014 | 2013 |
| Basic Earnings Per Share of Class A Common Stock | | | | |
| Numerator: | | | | |
| Net income | \$ 18,026 | \$ 13,345 | \$ 34,341 | \$ 28,761 |
| Denominator: | | | | |
| Weighted average number of shares of Class A common stock outstanding | 37,826,081 | 37,378,037 | 37,735,463 | 37,334,913 |
| Basic net income per share of Class A common stock | \$ 0.48 | \$ 0.36 | \$ 0.91 | \$ 0.77 |
| Diluted Earnings Per Share of Class A Common Stock | | | | |
| Numerator: | | | | |
| Net income | \$ 18,026 | \$ 13,345 | \$ 34,341 | \$ 28,761 |
| Denominator: | | | | |
| Basic weighted average number of shares of Class A common stock | 37,826,081 | 37,378,037 | 37,735,463 | 37,334,913 |
| Add dilutive effect of: | | | | |
| Unvested restricted stock units | 245,075 | 415,513 | 145,588 | 325,721 |
| Stock options | 25,276 | 22,951 | 25,200 | 20,260 |
| Weighted average common shares outstanding diluted | 38,096,432 | 37,816,501 | 37,906,251 | 37,680,894 |
| Diluted earnings per share of Class A common stock | \$ 0.47 | \$ 0.35 | \$ 0.91 | \$ 0.76 |

15. Related Party Transactions

The Company made payments on behalf of two affiliates of \$0 and \$1,617, respectively, during the three and nine month periods ended September 30, 2014 and \$488 and \$48,481, respectively, during the three and nine month periods ended September 30, 2013. These payments by the Company are primarily for professional services fees and other miscellaneous operating expenses on behalf of the affiliates. The Company had a net receivable from affiliates of \$2,000 and zero at September 30, 2014 and December 31, 2013, respectively.

As a result of the Company's initial public offering, the Company entered into a tax receivable agreement with HFF Holdings that provides for the payment by the Company to HFF Holdings of 85% of the amount of the cash savings in U.S. federal, state and local income tax that the Company actually realizes as a result of the increase in tax basis of the assets owned by HFF LP and HFF Securities and as a result of certain other tax benefits arising from entering into the tax receivable agreement and making payments under that agreement. As members of HFF Holdings, each of Mark Gibson, the Company's chief executive officer, Jody Thornton, the Company's president and member of the Company's board of directors and a transaction professional of the Operating Partnerships, John Fowler, a current director emeritus of the Company's board of directors and a transaction professional of the Operating Partnerships, and H. Scott Galloway, Matthew D. Lawton, Gerard T. Sansosti and Manuel A. de Zarraga, each an Executive Managing Director and a transaction professional of the Operating Partnerships, is entitled to participate in such payments, in each case on a pro rata basis based upon such person's ownership of interests in each series of tax receivable payments created by the initial public offering or subsequent exchange of Operating Partnership units. During the third quarter of 2014, Messrs. Gibson, Thornton, Fowler, Galloway, Lawton, Sansosti and de Zarraga received payments of \$0.9 million, \$0.9 million, \$0.7 million, \$0.4 million, \$0.3 million, \$0.4 million and \$0.3 million in connection with the Company's

payment of \$10.7 million to HFF Holdings under the tax receivable agreement. During the third quarter of 2013, Messrs. Gibson, Thornton, Fowler, Galloway, Lawton, Sansosti and de Zarraga received payments of \$0.9 million, \$0.9 million, \$0.7 million, \$0.4 million, \$0.2 million, \$0.4 million and \$0.2 million in connection with the Company's payment of \$10.4 million to HFF Holdings under the tax receivable agreement. The Company retains the remaining 15% of cash savings in income tax that it realizes. For purposes of the tax receivable agreement, cash savings in income tax is computed by comparing the Company's actual income tax liability to the amount of such taxes that it would have been required to pay had there been no increase to the tax basis of the assets of HFF LP and HFF Securities allocable to the Company as a result of the initial sale and later exchanges and had the Company not entered into the tax receivable agreement. The term of the tax receivable agreement commenced upon consummation of the offering and will continue until all such tax benefits have been utilized or have expired. See Note 12 for further information regarding the tax receivable agreement and Note 16 for the amount recorded in relation to this agreement.

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16. Commitments and Contingencies

The Company is obligated, pursuant to its tax receivable agreement with HFF Holdings, to pay to HFF Holdings 85% of the amount of cash savings in U.S. federal, state and local income tax that the Company actually realizes as a result of the increases in tax basis under Section 754 and as a result of certain other tax benefits arising from the Company entering into the tax receivable agreement and making payments under that agreement. The Company has recorded \$134.2 million for this obligation to HFF Holdings as a liability on the consolidated balance sheet as of September 30, 2014.

In recent years, the Company has entered into arrangements with newly-hired producers whereby these producers would be paid additional compensation if certain performance targets are met over a defined period. These payments will be made to the producers only if they enter into an employment agreement at the end of the performance period. Payments under these arrangements, if earned, would be paid in fiscal years 2014 through 2018. Currently, the Company cannot reasonably estimate the amounts that would be payable under all of these arrangements. The Company begins to accrue for these payments when it is deemed probable that payments will be made; therefore, on a quarterly basis, the Company evaluates the probability of each of the producers achieving the performance targets and the probability of each of the producers signing an employment agreement. As of September 30, 2014, \$1.1 million has been accrued for these arrangements on the consolidated balance sheet.

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

The following discussion summarizes the financial position of the Company and its subsidiaries as of September 30, 2014, and the results of our operations for the three and nine month periods ended September 30, 2014, and should be read in conjunction with (i) the unaudited consolidated financial statements and notes thereto included elsewhere in this Quarterly Report on Form 10-Q and (ii) the consolidated financial statements and accompanying notes to our Annual Report on Form 10-K for the year ended December 31, 2013.

Overview

Our Business

We are, based on transaction volume, one of the largest full-service commercial real estate financial intermediaries in the U.S. providing commercial real estate and capital markets services to both the consumers and providers of capital to the U.S. commercial real estate industry. We operate out of 23 offices nationwide with approximately 703 associates including approximately 275 transaction professionals as of September 30, 2014.

Substantially all of our revenues are in the form of capital markets services fees collected from our clients, usually negotiated on a transaction-by-transaction basis. We also earn fees from commercial loan servicing activities. We believe that our multiple product offerings and platform services, diverse client mix, expertise in a wide range of property types and national platform create a diversified revenue stream within the U.S. commercial real estate sector.

We operate in one reportable segment, the commercial real estate financial intermediary segment, and offer debt placement, investment sales, equity placements, investment banking and advisory services, loan sales and loan sale advisory services, commercial loan servicing and capital markets advice.

Our business may be significantly affected by factors outside of our control, particularly including:

Economic and commercial real estate market downturns. Our business is dependent on international and domestic economic conditions and the demand for commercial real estate and related services in the markets in which we operate. A slow-down, a significant downturn and/or recession in either the global economy and/or the domestic economy, including but not limited to even a regional economic downturn, could adversely affect our business. A general decline in acquisition and disposition activity, as well as a general decline in commercial real estate investment activity, can lead to a reduction in fees and commissions for arranging such transactions, as well as in fees and commissions for arranging financing for acquirers and property owners that are seeking to recapitalize their existing properties. Such a general decline can also lead to a significant reduction in our loan servicing activities, due to increased delinquencies and defaults and lack of additional loans that we would have otherwise added to our loan servicing portfolio.

Global and domestic credit and liquidity issues. Global and domestic credit and liquidity issues have in the recent past led to an economic downturn, including a commercial real estate market downturn. This downturn in turn led to a decrease in transaction activity and lower values. Restrictions on the availability of capital, both debt and/or equity, created significant reductions, and could in the future cause, further reductions of the liquidity in and the flow of capital to the commercial real estate markets. These restrictions also caused, and could in the future cause, commercial real estate prices to decrease due to the reduced amount of equity capital and debt financing

available which can lead to a reduction in our revenues.

Decreased investment allocation to commercial real estate class. Allocations to commercial real estate as an asset class for investment portfolio diversification may decrease for a number of reasons beyond our control, including but not limited to poor performance of the asset class relative to other asset classes or the superior performance of other asset classes when compared with the performance of the commercial real estate asset class. In addition, while commercial real estate is now viewed as an accepted and valid class for portfolio diversification, if this perception changes, there could be a significant reduction in the amount of debt and equity capital available in the commercial real estate sector which could therefore, result in decreased transactional volume.

Fluctuations in interest rates. Significant fluctuations in interest rates as well as steady and protracted movements of interest rates in one direction (increases or decreases) could adversely affect the operation and income of commercial real estate properties as well as the demand from investors for commercial real estate investments. Both of these events could adversely affect investor

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demand and the supply of capital for debt and equity investments in commercial real estate. In particular, increased interest rates may cause prices to decrease due to the increased costs of obtaining financing and could lead to decreases in purchase and sale activities, thereby reducing the amounts of investment sales and loan originations and related servicing fees. If our debt placement and investment sales origination and servicing businesses are negatively impacted, it is likely that our other lines of business would also suffer due to the relationship among our various capital markets services.

The factors discussed above have adversely affected and continue to be a risk to our business, as evidenced by the effects of the significant recent disruptions in the global capital and credit markets, and in particular the domestic capital markets. While conditions in 2011 through year to date 2014 have generally improved, the global and domestic credit and liquidity issues, coupled with the global and domestic economic recession/slow down as well as other global and domestic macro events beyond our control, could reduce in the future the number of acquisitions, dispositions and loan originations, as well as the respective number of transactions and transaction volumes. This has had, and may have in the future, a significant adverse effect on our capital markets services revenues (including but not limited to our servicing revenues). The significant balance sheet issues of many of the CMBS lenders, banks, life insurance companies, mortgage REITS and debt funds, captive finance companies and other financial institutions have adversely affected, and could again in the future adversely affect the global and domestic economies and the flow of commercial mortgage debt to the U.S. capital markets, and, in turn, could potentially adversely affect all of our capital markets services platforms and resulting revenues.

Other factors that may adversely affect our business are discussed under the heading "Forward-Looking Statements" and under the caption "Risk Factors" in this Quarterly Report on Form 10-Q.

Table of Contents**Results of Operations**

Following is a discussion of our results of operations for the three months ended September 30, 2014 and September 30, 2013. The table included in the period comparisons below provides summaries of our results of operations. The period-to-period comparisons of financial results are not necessarily indicative of future results. For a description of the key financial measures and indicators included in our consolidated financial statements, refer to the discussion under Management's Discussion and Analysis of Financial Condition and Results of Operations Key Financial Measures and Indicators in our Annual Report on Form 10-K for the year ended December 31, 2013.

| | For the Three Months Ended September 30, | | 2013 | | Total Dollar Change | Total Percentage Change |
|--|---|-----------------|------------------|-----------------|---------------------------|-------------------------------|
| | 2014 | | Dollars | % of Revenue | | |
| | Dollars | % of Revenue | Dollars | % of Revenue | | |
| (dollars in thousands, unless percentages) | | | | | | |
| Revenues | | | | | | |
| Capital markets services revenue | \$ 110,786 | 98.4% | \$ 88,546 | 99.0% | \$ 22,240 | 25.1% |
| Interest on mortgage notes receivable | 1,213 | 1.1% | 299 | 0.3% | 914 | 305.7% |
| Other | 612 | 0.5% | 569 | 0.6% | 43 | 7.6% |
| Total revenues | 112,611 | 100.0% | 89,414 | 100.0% | 23,197 | 25.9% |
| Operating expenses | | | | | | |
| Cost of services | 63,761 | 56.6% | 49,752 | 55.6% | 14,009 | 28.2% |
| Personnel | 11,268 | 10.0% | 11,029 | 12.3% | 239 | 2.2% |
| Occupancy | 2,454 | 2.2% | 2,406 | 2.7% | 48 | 2.0% |
| Travel and entertainment | 2,414 | 2.1% | 2,130 | 2.4% | 284 | 13.3% |
| Supplies, research and printing | 1,556 | 1.4% | 1,307 | 1.5% | 249 | 19.1% |
| Other | 5,375 | 4.8% | 4,145 | 4.6% | 1,230 | 29.7% |
| Total operating expenses | 86,828 | 77.1% | 70,769 | 79.1% | 16,059 | 22.7% |
| Operating income | 25,783 | 22.9% | 18,645 | 20.9% | 7,138 | 38.3% |
| Interest and other income, net | 4,144 | 3.7% | 3,546 | 4.0% | 598 | 16.9% |
| Interest expense | (16) | (0.0)% | (8) | (0.0)% | (8) | 100.0% |
| (Increase) decrease in payable under tax receivable agreement | 299 | 0.3% | (701) | (0.8)% | 1,000 | (142.7)% |
| Income before income taxes | 30,210 | 26.8% | 21,482 | 24.0% | 8,728 | 40.6% |
| Income tax expense | 12,184 | 10.8% | 8,137 | 9.1% | 4,047 | 49.7% |
| Net income | \$ 18,026 | 16.0% | \$ 13,345 | 14.9% | \$ 4,681 | 35.1% |
| Adjusted EBITDA (1) | \$ 31,604 | 28.1% | \$ 25,698 | 28.7% | \$ 5,906 | 23.0% |

- (1) The Company defines Adjusted EBITDA as net income before (i) interest expense, (ii) income tax expense, (iii) depreciation and amortization, (iv) stock-based compensation expense, which is a non-cash charge, (v) income recognized on the initial recording of mortgage servicing rights that are acquired with no initial consideration, which is also a non-cash income amount that can fluctuate significantly based on the level of mortgage servicing right volumes, and (vi) the increase (decrease) in payable under the tax receivable agreement, which represents changes in a liability recorded on the Company's consolidated balance sheet determined by the ongoing remeasurement of related deferred tax assets and, therefore, can be income or expense in the Company's consolidated statement of income in any individual period. The Company uses Adjusted EBITDA in its business operations to, among other things, evaluate the performance of its business, develop budgets and measure its performance against those budgets. The Company also believes that analysts and investors use Adjusted EBITDA as a supplemental measure to evaluate its overall operating performance. However, Adjusted EBITDA has material limitations as an analytical tool and should not be considered in isolation, or as a substitute for analysis of the Company's results as reported under U.S. generally acceptable accounting principles (GAAP). The Company finds Adjusted EBITDA as a useful tool to assist in evaluating performance because it eliminates items related to capital structure and taxes, including the Company's tax receivable agreement. Note that the Company classifies the interest expense on its warehouse lines of credit as an operating expense and, accordingly, it is not eliminated from net income in determining Adjusted EBITDA. Some of the items that the Company has eliminated from net income in determining Adjusted EBITDA are significant to the Company's business. For example, (i) interest expense is a necessary element of the Company's costs and ability to generate revenue because it incurs interest expense related to any outstanding indebtedness, (ii) payment of income taxes is a necessary element of the Company's costs, and (iii) depreciation and amortization are necessary elements of the Company's costs.

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Any measure that eliminates components of the Company's capital structure and costs associated with the Company's operations has material limitations as a performance measure. In light of the foregoing limitations, the Company does not rely solely on Adjusted EBITDA as a performance measure and also considers its GAAP results. Adjusted EBITDA is not a measurement of the Company's financial performance under GAAP and should not be considered as an alternative to net income, operating income or any other measures derived in accordance with GAAP. Because Adjusted EBITDA is not calculated in the same manner by all companies, it may not be comparable to other similarly titled measures used by other companies.

Set forth below is a reconciliation of consolidated net income to Adjusted EBITDA for the Company for the three months ended September 30, 2014 and 2013:

Adjusted EBITDA for the Company is calculated as follows:

(dollars in thousands)

| | For the Three Months Ended September 30, | |
|---|---|------------------|
| | 2014 | 2013 |
| Net income | \$ 18,026 | \$ 13,345 |
| Add: | | |
| Interest expense | 16 | 8 |
| Income tax expense | 12,184 | 8,137 |
| Depreciation and amortization | 1,966 | 1,550 |
| Stock-based compensation (a) | 1,578 | 3,250 |
| Initial recording of mortgage servicing rights | (1,867) | (1,293) |
| Increase (decrease) in payable under the tax receivable agreement | (299) | 701 |
| Adjusted EBITDA | \$ 31,604 | \$ 25,698 |

- (a) Amounts do not reflect expense associated with the stock component of estimated incentive payouts under the Company's firm profit participation bonus plan or office profit participation bonus plans that are anticipated to be paid in respect of the applicable year. Such expense is recorded as incentive compensation expense within personnel expenses in the Company's consolidated statements of income during the year to which the expense relates. Following the award, if any, of the related incentive payout, the stock component expense is reclassified as stock compensation costs within personnel expenses. See Note 2 to the Company's consolidated financial statements for further information regarding the Company's accounting policies relating to its firm profit participation bonus plan and office profit participation bonus plans. Stock-based compensation expense for the three months ended September 30, 2014 reflects \$0.5 million expense recognized during such period that was associated with restricted stock granted in March 2014 under the Company's firm profit participation bonus plan or office profit participation bonus plans in respect of 2013. Stock-based compensation expense for the three months ended September 30, 2013 reflects \$0.3 million expense recognized during such period that was associated with restricted stock granted in March 2013 under the Company's firm profit participation bonus plan or office profit participation bonus plans in respect of 2012. Stock-based payments under such plans were first

made in 2012 in respect of 2011. See Note 3 to the Company's consolidated financial statements for further information regarding the Company's accounting policies relating to its stock compensation.

Revenues. Our total revenues were \$112.6 million for the three months ended September 30, 2014 compared to \$89.4 million for the same period in 2013, an increase of \$23.2 million, or 25.9%. Revenues increased primarily due to a 19.3% increase in total production volumes as compared to the third quarter of 2013.

The revenues we generated from capital markets services for the three months ended September 30, 2014 increased approximately \$22.2 million, or 25.1%, to \$110.8 million from \$88.5 million for the same period in 2013. The increase is primarily attributable to a 19.3% increase in the total production volume during the third quarter of 2014 compared to the third quarter of 2013. During the third quarter of 2013, there was one unusually large transaction. If the Company's production volumes were adjusted to exclude this transaction in 2013, the third quarter of 2014 adjusted production volumes would have increased 28.9% as compared to the third quarter of 2013.

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The revenues derived from interest on mortgage notes receivable were \$1.2 million for the three months ended September 30, 2014 compared to \$0.3 million for the same period in 2013, an increase of approximately \$0.9 million. Revenues increased primarily as a result of an increase in the number of loan originations in the third quarter of 2014 compared to the third quarter of 2013 in connection with our services as a Freddie Mac Multifamily Program Plus® Seller/Service.

The other revenues we earned, which include expense reimbursements from clients related to out-of-pocket costs incurred and vary on a transaction-by-transaction basis, were approximately \$0.6 million for both the three month period ended September 30, 2014 and the three month period ended September 30, 2013.

Total Operating Expenses. Our total operating expenses were \$86.8 million for the three months ended September 30, 2014 compared to \$70.8 million for the same period in 2013, an increase of \$16.1 million, or approximately 22.7%. Expenses increased primarily due to increased cost of services and increased personnel costs resulting primarily from an increase in capital markets services revenue and increased headcount.

The cost of services for the three months ended September 30, 2014 increased \$14.0 million, or 28.2%, to \$63.8 million from \$49.8 million for the same period in 2013. The increase is primarily the result of the increase in commissions and other incentive compensation directly related to the increase in capital markets services revenues, and increase in compensation expense directly tied to performance-based incentives earned in connection with employment agreements for recruited transaction professionals. Also contributing to the increase in cost of services are higher salary and fringe benefit costs from increased headcount. Cost of services as a percentage of capital markets services revenues was approximately 57.6% and 56.2% for the three month periods ended September 30, 2014 and September 30, 2013, respectively.

Personnel expenses that are not directly attributable to providing services to our clients increased approximately \$0.2 million, or 2.2%, to \$11.3 million for the three months ended September 30, 2014 from \$11.0 million for the same period in 2013. The increase is primarily related to an increase in salaries and incentive compensation costs of \$0.5 million, an increase in profit participation costs of \$1.3 million, and a decrease in equity compensation costs (excluding profit participation equity costs) of \$1.9 million during the third quarter 2014 as compared to the third quarter 2013. Personnel expenses are also impacted quarterly by the adjustments made to accrue for the estimated expense associated with the performance-based firm and office profit participation plans. Both the firm and office profit participation plans allow for payments in the form of both cash and share-based awards based on the decision of the Company's board of directors. The stock compensation cost included in personnel expenses was \$1.6 million and \$3.2 million for the three months ended September 30, 2014 and 2013, respectively. The decrease in stock compensation costs is primarily due to the mark-to-market adjustment in the third quarter of 2013 on restricted stock awards accounted for as liability awards which resulted in \$2.9 million of expense, of which there was no such expense in the third quarter of 2014 as the liability awards fully vested in the first quarter of 2014, partially offset by the restricted stock awards granted in January 2014 of \$1.1 million, of which there was no such cost in the third quarter of 2013. At September 30, 2014, there was approximately \$20.2 million of unrecognized compensation cost related to share based awards. The weighted average remaining contractual term of the unvested restricted stock units is 3.7 years as of September 30, 2014. The weighted average remaining contractual term of the vested options is 4.0 years as of September 30, 2014.

Occupancy, travel and entertainment and supplies, research and printing expenses for the three months ended September 30, 2014 increased \$0.6 million, or 9.9%, to \$6.4 million compared to the same period in 2013. These increases are primarily due to increased travel and entertainment costs stemming from the increase in headcount and production volumes, increased occupancy costs from office expansions and increased supplies, research and printing costs from the increase in production volumes and the number of transactions.

Other expenses, including costs for insurance, professional fees, depreciation and amortization, interest on our warehouse line of credit and other operating expenses, were \$5.4 million in the three months ended September 30, 2014, an increase of \$1.2 million, or 29.7%, versus \$4.1 million in the three months ended September 30, 2013. This increase is primarily related to higher depreciation and amortization, interest on the warehouse line of credit and other operating costs.

Net Income. Our net income for the three months ended September 30, 2014 was \$18.0 million, an increase of \$4.7 million versus \$13.3 million for the same fiscal period in 2013. This increase is primarily due to the increase in revenues.

Interest and other income, net for the three months ended September 30, 2014 was \$4.1 million, an increase of \$0.6 million as compared to \$3.5 million for the same fiscal period in 2013 primarily due to higher income from the initial recording of mortgage

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servicing rights of \$0.6 million and higher other income earned in connection with the our agency business, slightly offset by lower gains on sale of servicing rights on certain loans of \$0.6 million and lower securitization compensation from the securitization of certain loans of \$0.1 million.

The interest expense we incurred in the three months ended September 30, 2014 was \$16,000 as compared to \$8,000 in the three months ended September 30, 2013.

(Increase) decrease in payable under the tax receivable agreement reflects the change in the estimated tax benefits owed to HFF Holdings under the tax receivable agreement. The \$299,000 decrease in payable under the tax receivable agreement for the three month period ended September 30, 2014 represents 85% of the decrease in the related deferred tax asset.

Income tax expense was approximately \$12.2 million for the three months ended September 30, 2014, as compared to \$8.1 million in the three months ended September 30, 2013. This increase is primarily due to the higher income before income taxes during the three months ended September 30, 2014 as compared to the same period in the prior year. During the three months ended September 30, 2014, the Company recorded a current income tax expense of \$9.6 million and deferred income tax expense of \$2.6 million.

Following is a discussion of our results of operations for the nine months ended September 30, 2014 and September 30, 2013. The table included in the period comparisons below provides summaries of our results of operations. The period-to-period comparisons of financial results are not necessarily indicative of future results. For a description of the key financial measures and indicators included in our consolidated financial statements, refer to the discussion under Management's Discussion and Analysis of Financial Condition and Results of Operations Key Financial Measures and Indicators in our Annual Report on Form 10-K for the year ended December 31, 2013.

| | For the Nine Months Ended September 30, | | | | Total Dollar Change | Total Percentage Change |
|--|--|-----------------|----------------|-----------------|---------------------------|-------------------------------|
| | 2014 | 2013 | | | | |
| | Dollars | % of Revenue | Dollars | % of Revenue | | |
| (dollars in thousands, unless percentages) | | | | | | |
| Revenues | | | | | | |
| Capital markets services revenue | \$ 279,506 | 98.6% | \$ 221,509 | 98.6% | \$ 57,997 | 26.2% |
| Interest on mortgage notes receivable | 2,346 | 0.8% | 1,619 | 0.7% | 727 | 44.9% |
| Other | 1,577 | 0.6% | 1,509 | 0.7% | 68 | 4.5% |
| Total revenues | 283,429 | 100.0% | 224,637 | 100.0% | 58,792 | 26.2% |
| Operating expenses | | | | | | |
| Cost of services | 163,178 | 57.6% | 131,186 | 58.4% | 31,992 | 24.4% |
| Personnel | 36,343 | 12.8% | 28,223 | 12.6% | 8,120 | 28.8% |
| Occupancy | 7,137 | 2.5% | 6,701 | 3.0% | 436 | 6.5% |
| Travel and entertainment | 8,485 | 3.0% | 6,698 | 3.0% | 1,787 | 26.7% |
| Supplies, research and printing | 4,576 | 1.6% | 3,710 | 1.7% | 866 | 23.3% |

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| | | | | | | |
|---|-----------|--------|-----------|--------|-----------|---------|
| Other | 16,103 | 5.7% | 14,185 | 6.3% | 1,918 | 13.5% |
| Total operating expenses | 235,822 | 83.2% | 190,703 | 84.9% | 45,119 | 23.7% |
| Operating income | 47,607 | 16.8% | 33,934 | 15.1% | 13,673 | 40.3% |
| Interest and other income, net | 10,295 | 3.6% | 14,157 | 6.3% | (3,862) | (27.3)% |
| Interest expense | (32) | (0.0)% | (26) | (0.0)% | (6) | 23.1% |
| (Increase) decrease in payable under tax receivable agreement | 800 | 0.3% | (1,040) | (0.5)% | 1,840 | NM |
| Income before income taxes | 58,670 | 20.7% | 47,025 | 20.9% | 11,645 | 24.8% |
| Income tax expense | 24,329 | 8.6% | 18,264 | 8.1% | 6,065 | 33.2% |
| Net income | \$ 34,341 | 12.1% | \$ 28,761 | 12.8% | \$ 5,580 | 19.4% |
| Adjusted EBITDA (1) | \$ 66,559 | 23.5% | \$ 55,655 | 24.8% | \$ 10,904 | 19.6% |

NM not meaningful

(1) Set forth below is a reconciliation of consolidated net income to Adjusted EBITDA for the Company for the nine months ended September 30, 2014 and 2013:

Table of Contents**Adjusted EBITDA for the Company is calculated as follows:***(dollars in thousands)*

| | For the Nine Months Ended September 30, | |
|---|--|-------------|
| | 2014 | 2013 |
| Net income | \$ 34,341 | \$ 28,761 |
| Add: | | |
| Interest expense | 32 | 26 |
| Income tax expense | 24,329 | 18,264 |
| Depreciation and amortization | 5,902 | 5,146 |
| Stock-based compensation (a) | 8,243 | 6,450 |
| Initial recording of mortgage servicing rights | (5,488) | (4,032) |
| Increase (decrease) in payable under the tax receivable agreement | (800) | 1,040 |
| Adjusted EBITDA | \$ 66,559 | \$ 55,655 |

- (a) Amounts do not reflect expense associated with the stock component of estimated incentive payouts under the Company's firm profit participation bonus plan or office profit participation bonus plans that are anticipated to be paid in respect of the applicable year. Such expense is recorded as incentive compensation expense within personnel expenses in the Company's consolidated statements of income during the year to which the expense relates. Following the award, if any, of the related incentive payout, the stock component expense is reclassified as stock compensation costs within personnel expenses. See Note 2 to the Company's consolidated financial statements for further information regarding the Company's accounting policies relating to its firm profit participation bonus plan and office profit participation bonus plans. Stock-based compensation expense for the nine months ended September 30, 2014 reflects \$1.4 million expense recognized during such period that was associated with restricted stock granted in March 2014 under the Company's firm profit participation bonus plan or office profit participation bonus plans in respect of 2013. Stock-based compensation expense for the nine months ended September 30, 2013 reflects \$0.9 million expense recognized during such period that was associated with restricted stock granted in March 2013 under the Company's firm profit participation bonus plan or office profit participation bonus plans in respect of 2012. Stock-based payments under such plans were first made in 2012 in respect of 2011. See Note 3 to the Company's consolidated financial statements for further information regarding the Company's accounting policies relating to its stock compensation.

Revenues. Our total revenues were \$283.4 million for the nine months ended September 30, 2014 compared to \$224.6 million for the same period in 2013, an increase of \$58.8 million, or 26.2%. Revenues increased primarily due to a 21.8% increase in total production volumes as compared to the first nine months of 2013.

The revenues we generated from capital markets services for the nine months ended September 30, 2014 increased \$58.0 million, or 26.2%, to \$279.5 million from \$221.5 million for the same period in 2013. The increase is primarily attributable to a 21.8% increase in the total production volume during the first nine months

of 2014 compared to the first nine months of 2013. There was one unusually large transaction in each of the first nine months of 2014 and 2013. If the Company's production volumes were adjusted to exclude these transactions, the first nine months of 2014 adjusted production volumes would have increased approximately 22.4% as compared to the first nine months of 2013.

The revenues derived from interest on mortgage notes receivable were \$2.3 million for the nine months ended September 30, 2014 compared to \$1.6 million for the same period in 2013, an increase of approximately \$0.7 million. Revenues increased primarily as a result of an increase in the number of loan originations in the first nine months of 2014 compared to the first nine months of 2013 in connection with our services as a Freddie Mac Multifamily Program Plus® Seller/Servicer.

The other revenues we earned, which include expense reimbursements from clients related to out-of-pocket costs incurred and vary on a transaction-by-transaction basis, were approximately \$1.6 million for the nine month period ended September 30, 2014 and \$1.5 million for the nine month period ended September 30, 2013, an increase of approximately 4.5%.

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Total Operating Expenses. Our total operating expenses were \$235.8 million for the nine months ended September 30, 2014 compared to \$190.7 million for the same period in 2013, an increase of \$45.1 million, or 23.7%. Expenses increased primarily due to increased cost of services and increased personnel costs resulting primarily from an increase in capital markets services revenue and increased headcount.

The cost of services for the nine months ended September 30, 2014 increased \$32.0 million, or 24.4%, to \$163.2 million from \$131.2 million for the same period in 2013. The increase is primarily the result of the increase in commissions and other incentive compensation directly related to the increase in capital markets services revenues. Also contributing to the increase in cost of services are higher salary and fringe benefit costs from increased headcount. Cost of services as a percentage of capital markets services revenues was approximately 58.4% and 59.2% for the nine month periods ended September 30, 2014 and September 30, 2013, respectively.

Personnel expenses that are not directly attributable to providing services to our clients increased \$8.1 million, or 28.8%, to \$36.3 million for the nine months ended September 30, 2014 from \$28.2 million for the same period in 2013. The increase is primarily related to an increase in salaries and incentive compensation costs of \$1.4 million, an increase in profit participation costs of \$4.1 million and an increase in equity compensation costs of \$1.2 million. Personnel expenses are also impacted quarterly by the adjustments made to accrue for the estimated expense associated with the performance-based firm and office profit participation plans. Both the firm and office profit participation plans allow for payments in the form of both cash and share-based awards based on the decision of the Company's board of directors. The stock compensation cost included in personnel expenses was \$8.2 million and \$6.4 million for the nine months ended September 30, 2014 and 2013, respectively. The increase in stock compensation costs is primarily due to restricted stock awards granted in January 2014 of \$2.8 million, of which there was no such cost in the first nine months of 2013, slightly offset by the mark-to-market adjustment on restricted stock awards accounted for as liability awards which resulted in \$3.3 million of expense (or a \$1.7 million decrease as compared to the first nine months of 2013). At September 30, 2014, there was approximately \$20.2 million of unrecognized compensation cost related to share based awards. The weighted average remaining contractual term of the unvested restricted stock units is 3.7 years as of September 30, 2014. The weighted average remaining contractual term of the vested options is 4.0 years as of September 30, 2014.

Occupancy, travel and entertainment and supplies, research and printing expenses for the nine months ended September 30, 2014 increased \$3.1 million, or 18.1%, to \$20.2 million compared to the same period in 2013. These increases are primarily due to increased travel and entertainment costs stemming from the increase in headcount and production volumes, increased occupancy costs from office expansions and increased supplies, research and printing costs from the increase in production volumes and the number of transactions.

Other expenses, including costs for insurance, professional fees, depreciation and amortization, interest on our warehouse line of credit and other operating expenses, were \$16.1 million in the nine months ended September 30, 2014, an increase of \$1.9 million, or approximately 13.5%, versus \$14.2 million in the nine months ended September 30, 2013. This increase is primarily related to increased amortization of \$0.5 million due to a higher balance of mortgage servicing rights and increased depreciation of leasehold improvements of \$0.2 million, increased interest on warehouse line of credit of \$0.3 million, increased professional fees of \$0.4 million and increased other operating costs of \$0.5 million.

Net Income. Our net income for the nine months ended September 30, 2014 was \$34.3 million, an increase of approximately \$5.6 million versus \$28.8 million for the same fiscal period in 2013. This increase is primarily due to the increase in revenue as described above which was slightly offset by lower interest and other income, net as discussed below.

Interest and other income, net for the nine months ended September 30, 2014 was \$10.3 million, a decrease of approximately \$3.9 million as compared to \$14.2 million for the same fiscal period in 2013 primarily due to lower gains on sale of servicing rights on certain loans of \$3.1 million and lower securitization compensation from the securitization of certain loans of \$2.9 million. These decreases were slightly offset by higher income on the initial recording of mortgage servicing rights of \$1.5 million.

The interest expense we incurred in the nine months ended September 30, 2014 and 2013 was \$32,000 and \$26,000, respectively.

(Increase) decrease in payable under the tax receivable agreement reflects the change in the estimated tax benefits owed to HFF Holdings under the tax receivable agreement. The \$0.8 million decrease in payable under the tax receivable agreement for the nine month period ended September 30, 2014 represents 85% of the decrease in the related deferred tax asset. The \$1.0 million increase in payable under the tax receivable agreement for the nine month period ended September 30, 2013 represents 85% of the increase in the related deferred tax asset.

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Income tax expense was approximately \$24.3 million for the nine months ended September 30, 2014, as compared to \$18.3 million in the nine months ended September 30, 2013. This increase is primarily due to the higher income before income taxes and a higher effective tax rate during the nine months ended September 30, 2014 compared to the same period of the prior year. During the nine months ended September 30, 2014, the Company recorded a current income tax expense of \$10.9 million and deferred income tax expense of \$13.4 million.

Financial Condition

Total assets increased to \$536.8 million at September 30, 2014 from \$488.2 million at December 31, 2013, primarily due to an increase in mortgage notes receivable of \$96.3 million due to a higher number of loans pending sale to Freddie Mac at September 30, 2014, compared to December 31, 2013, an increase in property and equipment, net of \$1.4 million and an increase in accounts receivable, net of \$2.6 million. These increases in assets were partially offset by decreases in cash and cash equivalents of \$40.6 million primarily due to a dividend payment of \$68.2 million and a decrease in the deferred tax assets of \$13.4 million.

Total liabilities increased to \$378.9 million at September 30, 2014 from \$312.6 million at December 31, 2013, primarily due to an increase in amounts outstanding under the warehouse lines of credit of \$96.3 million due to a higher number of loans pending sale to Freddie Mac at September 30, 2014, compared to December 31, 2013. This increase was partially offset by a decrease in accrued compensation and related taxes of \$14.2 million primarily due to the payment of incentive compensation that was accrued as of December 31, 2013 and a decrease in other current liabilities of \$4.7 million primarily from the payment of federal, state and local income taxes.

Cash Flows

Our historical cash flows are primarily related to the timing of receipt of transaction fees, the timing of distributions to members of HFF Holdings and payment of commissions and bonuses to employees.

First Nine Months of 2014

Cash and cash equivalents decreased \$40.6 million in the nine months ended September 30, 2014. Net cash of \$35.6 million was provided by operating activities, primarily resulting from \$34.3 million of net income which was partially offset by uses of cash from a \$10.7 million payment under the tax receivable agreement, a \$0.9 million decrease in accrued compensation and related taxes, a \$3.8 million decrease in other accrued liabilities, a \$1.0 million increase in prepaid taxes, prepaid expenses and other current assets and a \$2.6 million increase in accounts receivable. Cash of \$2.4 million was used for investing in property and equipment. Financing activities used \$73.7 million primarily due to a \$68.2 million dividend payment that we made to holders of our Class A common stock on February 6, 2014. Additionally, payments on certain capital leases used \$0.3 million, \$6.3 million was used to purchase shares of Class A common stock in connection with the minimum employee statutory tax withholdings and we recognized a \$1.0 million excess tax benefit related to share-based award activities.

First Nine Months of 2013

Cash and cash equivalents increased \$32.9 million in the nine months ended September 30, 2013. Net cash of \$37.7 million was provided by operating activities, primarily resulting from net income of \$28.8 million and an increase in accrued compensation and related taxes of \$7.4 million. These sources of cash were partially offset by a \$10.4 million payment under the tax receivable agreement, a \$1.9 million increase in accounts receivable, a \$1.4 million decrease in other accrued liabilities, and a decrease of \$3.6 million in prepaid taxes, prepaid expenses and other current assets. Cash of \$3.3 million was used for investing in property and equipment. Financing activities used \$0.3 million for the

payments on certain capital leases and \$1.7 million to purchase shares of Class A common stock in connection with employee tax withholdings, and we recognized a \$0.5 million excess tax benefit related to share-based award activities.

Table of Contents**Liquidity and Capital Resources**

Our current assets typically have consisted primarily of cash and cash equivalents and accounts receivable in relation to earned transaction fees. At September 30, 2014, our cash and cash equivalents of approximately \$160.7 million were invested or held in a mix of money market funds and bank demand deposit accounts at two financial institutions. Our liabilities have typically consisted of accounts payable and accrued compensation. We regularly monitor our liquidity position, including cash level, credit lines, interest and payments on debt, capital expenditures and other matters relating to liquidity and to compliance with regulatory net capital requirements.

Over the nine month period ended September 30, 2014, we generated approximately \$35.6 million of cash from operations. Our short-term liquidity needs are typically related to compensation expenses and other operating expenses such as occupancy, supplies, marketing, professional fees and travel and entertainment. For the nine months ended September 30, 2014, we incurred approximately \$235.8 million in total operating expenses. A large portion of our operating expenses are variable, highly correlated to our revenue streams and dependent on the collection of transaction fees. During the nine months ended September 30, 2014, approximately 64.2% of our operating expenses were considered variable expenses. Our cash flow generated from operations historically has been sufficient to enable us to meet our objectives. However, if the economy deteriorates at the rate it did during 2008 and 2009, we may be unable to generate enough cash flow from operations to meet our operating needs and therefore we could use all or substantially all of our existing cash reserves on hand to support our operations. We currently believe that cash flows from operating activities and our existing cash balance will provide adequate liquidity and are sufficient to meet our working capital needs for the foreseeable future.

Our tax receivable agreement with HFF Holdings entered into in connection with our initial public offering provides for the payment by us to HFF Holdings of 85% of the amount of cash savings in U.S. federal, state and local income tax that we actually realize as a result of the increases in tax basis and as a result of certain other tax benefits arising from our entering into the tax receivable agreement and making payments under that agreement. We have estimated that future payments that will be made to HFF Holdings will be \$134.2 million, of which approximately \$10.8 million is anticipated to be paid in 2015. Our liquidity needs related to our long term obligations are primarily related to our facility leases. Additionally, for the nine months ended September 30, 2014, we incurred approximately \$7.1 million in occupancy expenses and approximately \$32,000 in interest expense.

We are a party to an uncommitted \$350 million financing arrangement with PNC Bank, N.A. (PNC) and an uncommitted \$125 million financing arrangement with The Huntington National Bank (Huntington), to fund our Freddie Mac loan closings. Pursuant to these arrangements, PNC or Huntington funds the multifamily Freddie Mac loan closings on a transaction-by-transaction basis, with each loan being separately collateralized by a loan and mortgage on a multifamily property that is ultimately purchased by Freddie Mac. The PNC and Huntington National Bank financing arrangements are only for the purpose of supporting our participation in Freddie Mac's Program Plus Seller Servicer program and cannot be used for any other purpose. As of September 30, 2014, we had outstanding borrowings of \$189.8 million under the PNC/Huntington arrangements and a corresponding amount of mortgage notes receivable. Although we believe that our current financing arrangements with PNC and Huntington are sufficient to meet our current needs in connection with our participation in Freddie Mac's Program Plus Seller Servicer program, in the event we are not able to secure financing for our Freddie Mac loan closings, we will cease originating such Freddie Mac loans until we have available financing.

Critical Accounting Policies; Use of Estimates

We prepare our financial statements in accordance with U.S. generally accepted accounting principles. In applying many of these accounting principles, we need to make assumptions, estimates and/or judgments that affect the

reported amounts of assets, liabilities, revenues and expenses in our consolidated financial statements. We base our estimates and judgments on historical experience and other assumptions that we believe are reasonable under the circumstances. These assumptions, estimates and/or judgments, however, are often subjective and our actual results may change negatively based on changing circumstances or changes in our analyses. If actual amounts are ultimately different from our estimates, the revisions are included in our results of operations for the period in which the actual amounts become known. We believe the following critical accounting policies could potentially produce materially different results if we were to change underlying assumptions, estimates and/or judgments. See the notes to our consolidated financial statements for a summary of our significant accounting policies.

Goodwill. We evaluate goodwill for potential impairment annually or more frequently if circumstances indicate impairment may have occurred. Changes in accounting standards, which were adopted by the Company in 2013, provide the option to qualitatively assess goodwill for impairment before completing a quantitative assessment. Under the qualitative approach, if, after assessing the totality of events or circumstances, including macroeconomic, industry and market factors, and entity-specific factors, the Company

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determines it is likely (more likely than not) that the fair value of a reporting unit is greater than its carrying amount, then the quantitative impairment analysis is not required. The Company performs the required annual goodwill impairment evaluation in the fourth quarter of each year. No impairment of goodwill was determined to exist for the years ended December 31, 2013 or 2012.

Intangible Assets. Our intangible assets primarily include mortgage servicing rights under agreements with third party lenders. Servicing rights are recorded at the lower of cost or market. Mortgage servicing rights do not trade in an active, open market with readily available observable prices. Since there is no ready market value for the mortgage servicing rights, such as quoted market prices or prices based on sales or purchases of similar assets, the Company determines the fair value of the mortgage servicing rights by estimating the present value of future cash flows associated with servicing the loans. Management makes certain assumptions and judgments in estimating the fair value of servicing rights. The estimate is based on a number of assumptions, including the benefits of servicing (contractual servicing fees and interest on escrow and float balances), the cost of servicing, prepayment rates (including risk of default), an inflation rate, the expected life of the cash flows and the discount rate. The cost of servicing, prepayment rates and discount rates are the most sensitive factors affecting the estimated fair value of the servicing rights. Management estimates a market participant's cost of servicing by analyzing the limited market activity and considering the Company's own internal servicing costs. Management estimates the discount rate by considering the various risks involved in the future cash flows of the underlying loans which include the cancellation of servicing contracts, concentration in the life company portfolio and the incremental risk related to large loans. Management estimates the prepayment levels of the underlying mortgages by analyzing recent historical experience. Many of the commercial loans being serviced have financial penalties for prepayment or early payoff before the stated maturity date. As a result, the Company has consistently experienced a low level of loan runoff. The estimated value of the servicing rights is impacted by changes in these assumptions. As of September 30, 2014, the fair value and net book value of the servicing rights were \$22.4 million and \$17.4 million, respectively. The most sensitive assumptions in estimating the fair value of the mortgage servicing rights are the level of prepayments, discount rate and cost of servicing. If the assumed level of prepayments increased 163.0%, the discount rate increased 102.0% or if there is a 12.0% increase in the cost of servicing at the stratum level, the estimated fair value of the servicing rights may result in the recorded mortgage servicing rights being potentially impaired and would require management to measure the amount of the impairment charge. The effect of a variation in each of these assumptions on the estimated fair value of the servicing rights is calculated independently without changing any other assumption. Servicing rights are amortized in proportion to and over the period of estimated servicing income which results in an accelerated level of amortization. We evaluate amortizable intangible assets on an annual basis, or more frequently if circumstances so indicate, for potential impairment.

Income Taxes. The Company accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and for tax losses and for tax credit carryforwards, if any. Deferred tax assets and liabilities are measured using tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period of the tax rate change. In assessing the realizability of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Our effective tax rate is sensitive to several factors including changes in the mix of our geographic profitability. We evaluate our estimated tax rate on a quarterly basis to reflect changes in: (i) our geographic mix of income, (ii) legislative actions on statutory tax rates, and (iii) tax planning for jurisdictions affected by double taxation. We continually seek to develop and implement potential strategies and/or actions that would reduce our overall effective tax rate.

The net deferred tax asset of \$147.7 million at September 30, 2014 is comprised mainly of a \$148.0 million deferred tax asset related to the Section 754 of the Internal Revenue Code (Section 754) election tax basis step up. The net deferred tax asset related to the Section 754 election tax basis step up of \$148.0 million represents annual pre-tax deductions on the Section 754 basis step up and payments under the tax receivable agreement of approximately \$32.8 million in 2014, then increasing to \$53.0 million in 2021 and then decreasing over the next nine years to approximately \$0.1 million in 2030. In order to realize the anticipated pre-tax benefit of approximately \$32.8 million in 2014, the Company needs to generate approximately \$268 million in revenue, assuming a constant cost structure. In the event that the Company cannot realize the annual pre-tax benefit each year, the shortfall becomes a net operating loss that can be carried back two years to offset prior years' taxable income, if any, or carried forward twenty years to offset future taxable income. During 2008 and 2009, based on the decline in production volume and corresponding impact on operating results, we did not realize the entire benefit of the annual deduction. Currently, \$36,000 of this cumulative benefit is characterized as a net operating loss and can be carried forward for periods that begin to expire in 2028. The net operating loss limitation does not impact the Company's ability to fully utilize the net operating loss before its expiration. In evaluating the realizability of these deferred tax assets, management makes estimates and judgments regarding the level and timing of future taxable income, including projecting future revenue growth and changes to the cost structure. Based on this analysis and other quantitative and qualitative factors,

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management believes that it is currently more likely than not that the Company will be able to generate sufficient taxable income to realize the net deferred tax assets. Based on revenue and taxable income generated through September 30, 2014, management currently expects to realize the entire \$32.8 million anticipated pre-tax benefit. If it is more likely than not that the Company would not be able to generate a sufficient level of taxable income through the carryforward period, a valuation allowance would be recorded as a charge to income tax expense and a proportional reduction would be made in the payable under the tax receivable agreement which would be recorded as income in the consolidated statements of income. The trend in revenue growth over the next few years and through the amortization and carryforward periods is a key factor in assessing the realizability of the deferred tax assets.

Leases. The Company leases all of its facilities under operating lease agreements. These lease agreements typically contain tenant improvement allowances. The Company records tenant improvement allowances as leasehold improvement assets, included in property and equipment, net in the consolidated balance sheet, and related deferred rent liabilities and amortizes them on a straight-line basis over the shorter of the term of the lease or useful life of the asset as additional depreciation expense and a reduction to rent expense, respectively. Lease agreements sometimes contain rent escalation clauses or rent holidays, which are recognized on a straight-line basis over the life of the lease in accordance with ASC 840, *Leases* (ASC 840). Lease terms generally range from one to ten years. An analysis is performed on each equipment lease to determine whether it should be classified as a capital or operating lease according to ASC 840.

Share Based Compensation. The Company estimates the grant-date fair value of stock options using the Black-Scholes option-pricing model. For restricted stock awards, the fair value of the awards is calculated as the difference between the market value of the Company's Class A common stock on the date of grant and the purchase price paid by the employee. Until March 2014, the Company also had restricted stock awards that were accounted for as liability awards and required remeasurement to fair value at the end of each reporting period. The Company's awards are generally subject to graded or cliff vesting schedules. Compensation expense is adjusted for estimated forfeitures and is recognized on a straight-line basis over the requisite service period of the award. Forfeiture assumptions are evaluated on a quarterly basis and updated as necessary.

Employment / Non-compete Agreements. The Company has entered into arrangements with newly-hired producers whereby these producers would be paid additional compensation if certain performance targets are met over a defined period. Some of these agreements contain provisions that the payments will be made to the producers only if they enter into an employment agreement at the end of the performance period. Payments under these arrangements, if earned, would be paid in fiscal years 2016 through 2018. The Company begins to accrue for these payments when it is deemed probable that payments will be made; therefore, on a quarterly basis, the Company evaluates the probability of each of the producers achieving the performance targets and the probability of each of the producers signing an employment agreement, if applicable. As of September 30, 2014, \$1.1 million has been made for these arrangements.

Firm and Office Profit Participation Plans. The Company's firm and office profit participation plans provide for payments in cash and share-based awards if certain performance targets are achieved during the year. The expense associated with the plans is included in personnel expenses in the consolidated statements of income. The expense recorded for these plans is estimated during the year based on actual results at each interim reporting date and an estimate of future results for the remainder of the year. The plans allow for payments to be made in both cash and share-based awards, the composition of which is determined in the first calendar quarter of the subsequent year. Cash and share-based awards issued under these plans are subject to vesting conditions over the subsequent year, such that the total expense measured for these plans is recorded over the period from the beginning of the performance year through the vesting date. Based on an accounting policy election, the expense associated with the share-based component of the estimated incentive payout is recognized before the grant date of the stock due to the fact that the terms of the profit participation plans have been approved by the Company's board of directors and the employees of

the Company understand the requirements to earn the award. Prior to the grant date, the share-based component-related expense is recorded as incentive compensation expense within personnel expenses in the Company's consolidated statements of income. Following the award, if any, the related incentive payout, the share-based component expense is reclassified as stock compensation costs with personnel expenses.

Certain Information Concerning Off-Balance Sheet Arrangements

We do not currently invest in any off-balance sheet vehicles that provide liquidity, capital resources, market or credit risk support, or engage in any leasing activities that expose us to any liability that is not reflected in our consolidated financial statements.

Table of Contents**Seasonality**

Our capital markets services revenue has historically been seasonal, which can affect an investor's ability to compare our financial condition and results of operation on a quarter-by-quarter basis. This seasonality has caused our revenue, operating income, net income and cash flows from operating activities to be lower in the first half of the year and higher in the second half of the year. The typical concentration of earnings and cash flows in the last nine months of the year has historically been due to an industry-wide focus of clients to complete transactions towards the end of the calendar year. However, given the recent disruptions, write-offs and credit losses in the global and domestic capital markets, the liquidity issues facing all global capital markets, and in particular the U.S. commercial real estate markets, this historical pattern of seasonality may or may not continue. For example, the seasonality described above did not occur in 2007 or 2008, causing historical comparisons to be even more difficult to gauge.

Effect of Inflation and/or Deflation

Inflation and/or deflation, or both, could significantly affect our compensation costs, particularly those not directly tied to our transaction professionals' compensation, due to factors such as availability of capital and/or increased costs of capital. The rise of inflation could also significantly and adversely affect certain expenses, such as debt service costs, information technology and occupancy costs. To the extent that inflation and/or deflation results in rising interest rates and has other effects upon the commercial real estate markets in which we operate and, to a lesser extent, the securities markets, it may affect our financial position and results of operations by reducing the demand for commercial real estate and related services which could have a material adverse effect on our financial condition. See Part II, Item 1A, "Risk Factors" in this Quarterly Report on Form 10-Q.

Pending Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board issued changes to revenue recognition with customers. This update provides a five-step analysis of transactions to determine when and how revenue is recognized. An entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This update will be effective for the Company beginning in fiscal year 2017. This update may be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying this update recognized at the date of initial application. The Company is currently evaluating the impact of the new guidance on its consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Due to the nature of our business and the manner in which we conduct our operations, in particular the fact that our financial instruments that are exposed to concentrations of credit risk consist primarily of short-term cash deposits and investments, we believe we do not face any material interest rate risk, foreign currency exchange rate risk, equity price risk or other market risk.

Item 4. Controls and Procedures***Management's Quarterly Evaluation of Disclosure Controls and Procedures***

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934, as amended is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that

such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required financial disclosure.

Our Chief Executive Officer and Chief Financial Officer (our principal executive officer and principal financial officer, respectively) have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our principal executive officer and principal financial officer have concluded that, as of September 30, 2014, the Company's disclosure controls and procedures are effective to provide reasonable assurance that material information required to be included in our periodic SEC reports is recorded, processed, summarized and reported within the time periods specified in rules and forms.

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The design of any system of control is based upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated objectives under all future events, no matter how remote, or that the degree of compliance with the policies or procedures may not deteriorate. Because of its inherent limitations, disclosure controls and procedures may not prevent or detect all misstatements. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives.

Changes in Internal Controls

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

Table of Contents**PART II. OTHER INFORMATION****Item 1. Legal Proceedings.**

We are party to various litigation matters, in most cases involving normal ordinary course and routine claims incidental to our business. We cannot estimate with certainty our ultimate legal and financial liability with respect to such pending matters. However, we believe, based on our examination of such pending matters, that our ultimate liability for such matters will not have a material adverse effect on our business or financial condition.

Item 1A. Risk Factors.

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, Item 1A. Risk Factors, in our Annual Report on Form 10-K for the year ended December 31, 2013, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

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

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

None.

Item 5. Other Information.

None.

Item 6. Exhibits.

A. Exhibits

| | |
|---------|--|
| 31.1 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith). |
| 31.2 | Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith). |
| 32.1 | Certification pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith). |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema |

| | |
|---------|---|
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase |
| 101.DEF | XBRL Taxonomy Definition Linkbase |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase |

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SIGNATURES

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

HFF, INC.

Dated: November 10, 2014

By: /s/ Mark D. Gibson
Mark D. Gibson
*Chief Executive Officer,
Director and Executive Managing Director
(Principal Executive Officer)*

Dated: November 10, 2014

By: /s/ Gregory R. Conley
Gregory R. Conley
*Chief Financial Officer
(Principal Financial and Accounting Officer)*

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EXHIBIT INDEX

| | |
|---------|--|
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