
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended September 30, 2022

OR

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

Commission File No. 001-38604

Focus Financial Partners Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or Other Jurisdiction
of Incorporation or Organization)

875 Third Avenue, 28th Floor
New York, NY
(Address of Principal Executive Offices)

47-4780811
(I.R.S. Employer
Identification No.)

10022
(Zip Code)

(646) 519-2456

(Registrant's telephone number, including area code)

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

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Class A common stock, par value \$0.01 per share	FOCS	Nasdaq Global Select Market

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

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
Emerging growth company

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

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

As of November 1, 2022, the registrant had 65,865,932 shares of Class A common stock and 11,653,693 shares of Class B common stock outstanding.

[Table of Contents](#)

**FOCUS FINANCIAL PARTNERS INC.
INDEX TO FORM 10-Q
FOR THE QUARTER ENDED SEPTEMBER 30, 2022**

	<u>Page No.</u>
<u>PART I: FINANCIAL INFORMATION</u>	
<u>Item 1.</u>	
<u>Financial Statements</u>	2
<u>Unaudited condensed consolidated balance sheets</u>	2
<u>Unaudited condensed consolidated statements of operations</u>	3
<u>Unaudited condensed consolidated statements of comprehensive income (loss)</u>	4
<u>Unaudited condensed consolidated statements of cash flows</u>	5
<u>Unaudited condensed consolidated statements of changes in equity</u>	7
<u>Notes to unaudited condensed consolidated financial statements</u>	8
<u>Item 2.</u>	
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	25
<u>Item 3.</u>	
<u>Quantitative and Qualitative Disclosures about Market Risk</u>	47
<u>Item 4.</u>	
<u>Controls and Procedures</u>	47
<u>PART II: OTHER INFORMATION</u>	
<u>Item 1.</u>	
<u>Legal Proceedings</u>	48
<u>Item 1A.</u>	
<u>Risk Factors</u>	48
<u>Item 2.</u>	
<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	49
<u>Item 6.</u>	
<u>Exhibits</u>	49
<u>SIGNATURES</u>	50

PART I: FINANCIAL INFORMATION

Item 1. Financial Statements

FOCUS FINANCIAL PARTNERS INC.

Unaudited condensed consolidated balance sheets

(In thousands, except share and per share amounts)

	December 31, 2021	September 30, 2022
ASSETS		
Cash and cash equivalents	\$ 310,684	\$ 128,528
Accounts receivable less allowances of \$3,255 at 2021 and \$3,949 at 2022	198,827	207,992
Prepaid expenses and other assets	123,826	174,007
Fixed assets—net	47,199	49,818
Operating lease assets	249,850	257,749
Debt financing costs—net	4,254	3,648
Deferred tax assets—net	267,332	232,332
Goodwill	1,925,315	2,092,787
Other intangible assets—net	1,581,719	1,637,816
TOTAL ASSETS	<u>\$ 4,709,006</u>	<u>\$ 4,784,677</u>
LIABILITIES AND EQUITY		
LIABILITIES		
Accounts payable	\$ 11,580	\$ 11,822
Accrued expenses	72,572	108,542
Due to affiliates	105,722	66,868
Deferred revenue	10,932	15,554
Contingent consideration and other liabilities	468,284	320,176
Deferred tax liabilities	31,973	39,477
Operating lease liabilities	277,324	286,930
Borrowings under credit facilities (stated value of \$2,407,302 and \$2,438,779 at December 31, 2021 and September 30, 2022, respectively)	2,393,669	2,427,211
Tax receivable agreements obligations	219,542	221,237
TOTAL LIABILITIES	<u>3,591,598</u>	<u>3,497,817</u>
COMMITMENTS AND CONTINGENCIES (Note 12)		
EQUITY		
Class A common stock, par value \$0.01, 500,000,000 shares authorized; 65,320,124 and 65,865,932 shares issued and outstanding at December 31, 2021 and September 30, 2022, respectively	653	658
Class B common stock, par value \$0.01, 500,000,000 shares authorized; 11,439,019 and 11,653,693 shares issued and outstanding at December 31, 2021 and September 30, 2022, respectively	114	116
Additional paid-in capital	841,753	930,042
Retained earnings	24,995	116,429
Accumulated other comprehensive income	3,029	11,378
Total shareholders' equity	870,544	1,058,623
Non-controlling interest	246,864	228,237
Total equity	<u>1,117,408</u>	<u>1,286,860</u>
TOTAL LIABILITIES AND EQUITY	<u>\$ 4,709,006</u>	<u>\$ 4,784,677</u>

See notes to unaudited condensed consolidated financial statements

FOCUS FINANCIAL PARTNERS INC.
Unaudited condensed consolidated statements of operations
(In thousands, except share and per share amounts)

	For the three months ended September 30,		For the nine months ended September 30,	
	2021	2022	2021	2022
REVENUES:				
Wealth management fees	\$ 433,967	\$ 499,017	\$ 1,213,782	\$ 1,531,617
Other	20,568	20,847	60,283	64,025
Total revenues	454,535	519,864	1,274,065	1,595,642
OPERATING EXPENSES:				
Compensation and related expenses	144,249	186,320	424,337	546,251
Management fees	127,166	122,971	345,443	397,612
Selling, general and administrative	75,637	89,915	208,481	273,336
Intangible amortization	46,055	67,331	133,041	192,256
Non-cash changes in fair value of estimated contingent consideration	36,243	(30,708)	96,241	(82,450)
Depreciation and other amortization	3,622	4,016	10,835	11,454
Total operating expenses	432,972	439,845	1,218,378	1,338,459
INCOME FROM OPERATIONS	21,563	80,019	55,687	257,183
OTHER INCOME (EXPENSE):				
Interest income	206	126	310	146
Interest expense	(16,543)	(26,491)	(37,893)	(63,999)
Amortization of debt financing costs	(1,102)	(949)	(2,856)	(2,999)
Other income (expense)—net	312	(2,347)	(219)	(3,834)
Income from equity method investments	91	51	514	157
Total other expense—net	(17,036)	(29,610)	(40,144)	(70,529)
INCOME BEFORE INCOME TAX	4,527	50,409	15,543	186,654
INCOME TAX EXPENSE	2,678	12,120	6,038	59,965
NET INCOME	1,849	38,289	9,505	126,689
Non-controlling interest	(1,200)	(9,040)	(6,623)	(35,255)
NET INCOME ATTRIBUTABLE TO COMMON SHAREHOLDERS	\$ 649	\$ 29,249	\$ 2,882	\$ 91,434
Income per share of Class A common stock:				
Basic	\$ 0.01	\$ 0.45	\$ 0.05	\$ 1.40
Diluted	\$ 0.01	\$ 0.44	\$ 0.05	\$ 1.39
Weighted average shares of Class A common stock outstanding:				
Basic	59,940,166	65,599,493	55,978,639	65,441,151
Diluted	60,438,510	65,821,228	56,447,070	65,729,339

See notes to unaudited condensed consolidated financial statements

FOCUS FINANCIAL PARTNERS INC.

Unaudited condensed consolidated statements of comprehensive income (loss)

(In thousands)

	For the three months ended		For the nine months ended	
	September 30,		September 30,	
	2021	2022	2021	2022
Net income	\$ 1,849	\$ 38,289	\$ 9,505	\$ 126,689
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	(5,057)	(13,237)	(5,876)	(20,662)
Unrealized gain on interest rate swaps designated as cash flow hedges	432	7,710	5,937	31,811
Comprehensive income (loss)	(2,776)	32,762	9,566	137,838
Less: Comprehensive (income) loss attributable to non-controlling interest	14	(7,994)	(7,194)	(38,055)
Comprehensive income (loss) attributable to common shareholders	\$ (2,762)	\$ 24,768	\$ 2,372	\$ 99,783

See notes to unaudited condensed consolidated financial statements

FOCUS FINANCIAL PARTNERS INC.

Unaudited condensed consolidated statements of cash flows

(In thousands)

	For the nine months ended	
	September 30,	
	2021	2022
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 9,505	\$ 126,689
Adjustments to reconcile net income to net cash provided by operating activities—net of effect of acquisitions:		
Intangible amortization	133,041	192,256
Depreciation and other amortization	10,835	11,454
Amortization of debt financing costs	2,856	2,999
Non-cash equity compensation expense	24,569	22,190
Non-cash changes in fair value of estimated contingent consideration	96,241	(82,450)
Income from equity method investments	(514)	(157)
Distributions received from equity method investments	773	1,059
Deferred taxes and other non-cash items	(570)	38,492
Changes in cash resulting from changes in operating assets and liabilities:		
Accounts receivable	(22,247)	(7,959)
Prepaid expenses and other assets	(17,731)	(7,083)
Accounts payable	1,974	21
Accrued expenses	35,382	37,729
Due to affiliates	22,715	(39,020)
Contingent consideration and other liabilities	(61,181)	(69,038)
Deferred revenue	2,200	3,134
Net cash provided by operating activities	237,848	230,316
CASH FLOWS FROM INVESTING ACTIVITIES:		
Cash paid for acquisitions and contingent consideration—net of cash acquired	(286,803)	(361,675)
Purchase of fixed assets	(6,560)	(13,152)
Investment and other, net	(17,232)	(5,232)
Net cash used in investing activities	(310,595)	(380,059)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings under credit facilities	1,169,500	100,000
Repayments of borrowings under credit facilities	(419,145)	(68,523)
Proceeds from issuance of common stock, net	25,767	—
Payments in connection with unit redemption, net	(25,767)	—
Payments in connection with tax receivable agreements	(4,423)	(3,856)
Contingent consideration paid	(67,735)	(35,929)
Payments of deferred acquisition consideration	—	(1,484)
Payments of debt financing costs	(8,282)	(1,111)
Proceeds from exercise of stock options	6,186	1,158
Distributions for unitholders	(26,391)	(20,519)
Other	(46)	375
Net cash provided by (used in) financing activities	649,664	(29,889)
EFFECT OF EXCHANGE RATES ON CASH AND CASH EQUIVALENTS	(568)	(2,524)
CHANGE IN CASH AND CASH EQUIVALENTS	576,349	(182,156)
CASH AND CASH EQUIVALENTS:		
Beginning of period	65,858	310,684
End of period	\$ 642,207	\$ 128,528

See Note 13 for supplemental cash flow disclosure
See notes to unaudited condensed consolidated financial statements

FOCUS FINANCIAL PARTNERS INC.

Unaudited condensed consolidated statements of changes in equity
Three months ended September 30, 2021 and 2022
(In thousands, except share amounts)

	Class A		Class B		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity	Non-controlling Interest	Total Equity
	Shares	Amount	Shares	Amount						
Balance at July 1, 2021	59,792,889	\$ 598	12,692,740	\$ 127	\$ 650,421	\$ 16,816	\$ 734	\$ 668,696	\$ 230,389	\$ 899,085
Net income	—	—	—	—	—	649	—	649	1,200	1,849
Issuance of units in connection with an acquisition and contingent consideration	—	—	64,706	—	—	—	—	—	—	—
Issuance (cancellation) of common stock in connection with exercise of Focus LLC common unit exchange rights	418,669	4	(418,669)	(4)	21,901	—	—	21,901	—	21,901
Issuance of common stock in connection with exercise of Focus LLC incentive unit exchange rights	34,898	—	—	—	1,825	—	—	1,825	—	1,825
Exercise of stock options	68,885	1	—	—	2,168	—	—	2,169	—	2,169
Change in non-controlling interest allocation	—	—	—	—	(18,833)	—	—	(18,833)	(4,129)	(22,962)
Non-cash equity compensation expenses	—	—	—	—	1,569	—	—	1,569	—	1,569
Currency translation adjustment-net of tax	—	—	—	—	—	—	(3,735)	(3,735)	(1,322)	(5,057)
Unrealized gain on interest rate swaps designated as cash flow hedges-net of tax	—	—	—	—	—	—	324	324	108	432
Adjustments of deferred taxes, net of amounts payable under tax receivable agreements and changes from Focus LLC interest transactions	—	—	—	—	490	—	—	490	—	490
Balance at September 30, 2021	<u>60,315,341</u>	<u>\$ 603</u>	<u>12,338,777</u>	<u>\$ 123</u>	<u>\$ 659,541</u>	<u>\$ 17,465</u>	<u>\$ (2,677)</u>	<u>\$ 675,055</u>	<u>\$ 226,246</u>	<u>\$ 901,301</u>
Balance at July 1, 2022	65,442,389	654	12,034,104	120	910,222	87,180	15,859	\$ 1,014,035	\$ 234,821	\$ 1,248,856
Net income	—	—	—	—	—	29,249	—	29,249	9,040	38,289
Issuance (cancellation) of common stock in connection with exercise of Focus LLC common unit exchange rights	381,573	4	(381,573)	(4)	15,469	—	—	15,469	—	15,469
Issuance of common stock in connection with exercise of Focus LLC incentive unit exchange rights	15,158	—	—	—	615	—	—	615	—	615
Exercise of stock options	26,767	—	—	—	736	—	—	736	—	736
Restricted stock units vesting and related withholding	45	—	—	—	—	—	—	—	—	—
Restricted common units vesting	—	—	1,162	—	—	—	—	—	—	—
Change in non-controlling interest allocation	—	—	—	—	1,009	—	—	1,009	(14,578)	(13,569)
Non-cash equity compensation expenses	—	—	—	—	2,226	—	—	2,226	—	2,226
Currency translation adjustment-net of tax	—	—	—	—	—	—	(10,666)	(10,666)	(2,571)	(13,237)
Unrealized gain on interest rate swaps designated as cash flow hedges-net of tax	—	—	—	—	—	—	6,185	6,185	1,525	7,710
Adjustments of deferred taxes, net of amounts payable under tax receivable agreements and changes from Focus LLC interest transactions	—	—	—	—	(235)	—	—	(235)	—	(235)
Balance at September 30, 2022	<u>65,865,932</u>	<u>\$ 658</u>	<u>11,653,693</u>	<u>\$ 116</u>	<u>\$ 930,042</u>	<u>\$ 116,429</u>	<u>\$ 11,378</u>	<u>\$ 1,058,623</u>	<u>\$ 228,237</u>	<u>\$ 1,286,860</u>

See notes to unaudited condensed consolidated financial statements

FOCUS FINANCIAL PARTNERS INC.

**Unaudited condensed consolidated statements of changes in equity
Nine months ended September 30, 2021 and 2022**

(In thousands, except share amounts)

	Class A Common Stock		Class B Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity	Non-controlling Interest	Total Equity
	Shares	Amount	Shares	Amount						
Balance at January 1, 2021	51,158,712	\$ 512	20,661,595	\$ 207	\$ 526,664	\$ 14,583 2,882	\$ — (2,167)	\$ 539,799 2,882	\$ 319,080 6,623	\$ 858,879 9,505
Net income	—	—	—	—	—	—	—	—	—	—
Issuance of units in connection with an acquisition and contingent consideration	—	—	233,098	1	—	—	—	1	—	1
Issuance (cancellation) of common stock in connection with offering, net	6,568,098	65	(6,306,301)	(63)	317,858	—	—	317,860	—	317,860
Issuance (cancellation) of common stock in connection with exercise of Focus LLC common unit exchange rights	2,249,615	22	(2,249,615)	(22)	109,677	—	—	109,677	—	109,677
Issuance of common stock in connection with exercise of Focus LLC incentive unit exchange rights	169,530	2	—	—	8,348	—	—	8,350	—	8,350
Exercise of stock options	169,386	2	—	—	5,343	—	—	5,345	—	5,345
Change in non-controlling interest allocation	—	—	—	—	(328,318)	—	—	(328,318)	(100,028)	(428,346)
Non-cash equity compensation expenses	—	—	—	—	3,859	—	—	3,859	—	3,859
Currency translation adjustment-net of tax	—	—	—	—	—	—	(4,516)	(4,516)	(1,360)	(5,876)
Unrealized gain on interest rate swaps designated as cash flow hedges-net of tax	—	—	—	—	—	—	4,006	4,006	1,931	5,937
Adjustments of deferred taxes, net of amounts payable under tax receivable agreements and changes from Focus LLC interest transactions	—	—	—	—	16,110	—	—	16,110	—	16,110
Balance at September 30, 2021	<u>60,315,341</u>	<u>\$ 603</u>	<u>12,338,777</u>	<u>\$ 123</u>	<u>\$ 659,541</u>	<u>\$ 17,465</u>	<u>\$ (2,677)</u>	<u>\$ 675,055</u>	<u>\$ 226,246</u>	<u>\$ 901,301</u>
Balance at January 1, 2022	65,320,124	\$ 653	11,439,019	\$ 114	\$ 841,753	\$ 24,995 91,434	\$ 3,029	\$ 870,544 91,434	\$ 246,864 35,255	\$ 1,117,408 126,689
Net income	—	—	—	—	—	—	—	—	—	—
Issuance of units in connection with an acquisition and contingent consideration	—	—	700,085	7	—	—	—	7	—	7
Issuance (cancellation) of common stock in connection with exercise of Focus LLC common unit exchange rights	486,573	5	(486,573)	(5)	19,592	—	—	19,592	—	19,592
Issuance of common stock in connection with exercise of Focus LLC incentive unit exchange rights	17,114	—	—	—	702	—	—	702	—	702
Exercise of stock options	42,076	—	—	—	1,158	—	—	1,158	—	1,158
Restricted stock units vesting and related withholding	45	—	—	—	—	—	—	—	—	—
Restricted common units vesting	—	—	1,162	—	—	—	—	—	—	—
Change in non-controlling interest allocation	—	—	—	—	65,618	—	—	65,618	(56,682)	8,936
Non-cash equity compensation expenses	—	—	—	—	6,323	—	—	6,323	—	6,323
Currency translation adjustment-net of tax	—	—	—	—	—	—	(16,574)	(16,574)	(4,088)	(20,662)
Unrealized gain on interest rate swaps designated as cash flow hedges-net of tax	—	—	—	—	—	—	24,923	24,923	6,888	31,811
Adjustments of deferred taxes, net of amounts payable under tax receivable agreements and changes from Focus LLC interest transactions	—	—	—	—	(5,104)	—	—	(5,104)	—	(5,104)
Balance at September 30, 2022	<u>65,865,932</u>	<u>\$ 658</u>	<u>11,653,693</u>	<u>\$ 116</u>	<u>\$ 930,042</u>	<u>\$116,429</u>	<u>\$ 11,378</u>	<u>\$ 1,058,623</u>	<u>\$ 228,237</u>	<u>\$ 1,286,860</u>

See notes to unaudited condensed consolidated financial statements [Click or tap here to enter text.](#)

FOCUS FINANCIAL PARTNERS INC.

Notes to unaudited condensed consolidated financial statements

(In thousands, except unit data, share and per share amounts)

1. GENERAL

Organization and Business— Focus Financial Partners Inc. (“Focus Inc.”) was formed as a Delaware corporation on July 29, 2015. Focus Inc. is the managing member of Focus Financial Partners, LLC (“Focus LLC”) and operates and controls the businesses and affairs of Focus LLC.

Focus LLC is a Delaware limited liability company that was formed in November 2004. Focus LLC’s subsidiaries commenced revenue-generating and acquisition activities in January 2006. Focus LLC’s activities are governed by its Fourth Amended and Restated Operating Agreement (the “Operating Agreement”). Focus LLC is in the business of acquiring and overseeing independent fiduciary wealth management and related businesses.

The unaudited condensed consolidated financial statements reflect the results of operations and financial position of Focus Inc. and its subsidiaries (the “Company”).

2. SUMMARY OF ACCOUNTING POLICIES

Basis of Presentation—The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial statements and pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments, consisting of only normal recurring adjustments, considered necessary for fair presentation have been included. The unaudited condensed consolidated financial statements include the accounts of Focus Inc. and its majority and wholly owned subsidiaries. Focus Inc. consolidates Focus LLC and its subsidiaries’ financial statements and records the interests in Focus LLC consisting of common units, restricted common units and the common unit equivalent of incentive units of Focus LLC that Focus Inc. does not own as non-controlling interests (see Note 3). Intercompany transactions and balances have been eliminated in consolidation. These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and footnotes thereto included in the Company’s Annual Report on Form 10-K as filed with the SEC on February 17, 2022.

Operating results for the three and nine months ended September 30, 2022 are not necessarily indicative of the results that may be expected for the year ending December 31, 2022.

Use of Estimates—The preparation of the unaudited condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

FOCUS FINANCIAL PARTNERS INC.

Notes to unaudited condensed consolidated financial statements (continued)

(In thousands, except unit data, share and per share amounts)

Revenue

The Company disaggregates revenue by wealth management fees and other. The Company does not allocate revenue by the type of service provided in connection with providing holistic wealth management client services. The Company generally manages its business based on the operating results of the enterprise taken as a whole, not by geographic region. The following table disaggregates the revenues based on the location of the partner firm legal entities that generate the revenues and therefore may not be reflective of the geography in which clients are located.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2022	2021	2022
Domestic revenue	\$ 427,729	\$ 486,536	\$ 1,197,874	\$ 1,504,221
International revenue	26,806	33,328	76,191	91,421
Total revenue	\$ 454,535	\$ 519,864	\$ 1,274,065	\$ 1,595,642

International revenue primarily consists of revenue generated by partner firm legal entities in Australia, Canada, Switzerland and the United Kingdom.

Recent Accounting Pronouncements

In March 2020, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2020-04, “Facilitation of the Effects of Reference Rate Reform on Financial Reporting.” ASU No. 2020-04 provides optional expedients and exceptions for applying generally accepted accounting principles to contract modifications and hedging relationships, subject to meeting certain criteria, that reference the London InterBank Offered Rate (“LIBOR”) or another rate that is expected to be discontinued. The amendments in ASU No. 2020-04 are effective for all entities as of March 12, 2020 through December 31, 2022. The adoption of ASU No. 2020-04 did not have a material impact on the Company’s consolidated financial statements; however, the Company will continue to evaluate the impacts, if any, of the provisions of ASU No. 2020-04 on the Company’s debt and hedging arrangements through December 31, 2022.

3. NON-CONTROLLING INTEREST AND INCOME PER SHARE

The calculation of controlling and non-controlling interest is as follows as of September 30, 2021 and 2022:

	2021	2022
Focus LLC common units	12,338,777	11,653,693
Focus LLC restricted common units	71,374	192,463
Common unit equivalents of outstanding vested and unvested Focus LLC incentive units(1)	8,656,088	3,680,928
Total common units, restricted common units and common unit equivalents attributable to non-controlling interest	21,066,239	15,527,084
Total common units, restricted common units and common unit equivalents of incentive units outstanding	81,381,580	81,393,016
Non-controlling interest allocation	25.9 %	19.1 %
Company’s interest in Focus LLC	74.1 %	80.9 %

(1) Focus LLC common units issuable upon conversion of 16,233,899 and 16,165,917 (see Note 9) vested and unvested Focus LLC incentive units outstanding as of September 30, 2021 and 2022, respectively, was

FOCUS FINANCIAL PARTNERS INC.

Notes to unaudited condensed consolidated financial statements (continued)

(In thousands, except unit data, share and per share amounts)

calculated using the common unit equivalent of vested and unvested Focus LLC incentive units based on the closing price of the Company's Class A common stock on the last trading day of the periods.

Basic income per share is calculated utilizing net income attributable to common shareholders divided by the weighted average number of shares of Class A common stock outstanding during the same periods. The calculation of basic income per share is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2022	2021	2022
Net income attributable to common shareholders	\$ 649	\$ 29,249	\$ 2,882	\$ 91,434
Weighted average shares of Class A common stock outstanding	59,940,166	65,599,493	55,978,639	65,441,151
Basic income per share	\$ 0.01	\$ 0.45	\$ 0.05	\$ 1.40

Diluted income per share is calculated utilizing net income attributable to common shareholders divided by the weighted average number of shares of Class A common stock outstanding during the same periods plus the effect, if any, of the potentially dilutive shares of the Company's Class A common stock from stock options, restricted stock units and Focus LLC common units, including contingently issuable Focus LLC common units, if any, restricted common units and incentive units as calculated using the treasury stock method:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2022	2021	2022
Net income attributable to common shareholders	\$ 649	\$ 29,249	\$ 2,882	\$ 91,434
Weighted average shares of Class A common stock outstanding	59,940,166	65,599,493	55,978,639	65,441,151
Effect of dilutive stock options	441,809	197,520	420,801	264,938
Effect of dilutive restricted stock units	56,535	24,215	47,630	23,250
Total	60,438,510	65,821,228	56,447,070	65,729,339
Diluted income per share	\$ 0.01	\$ 0.44	\$ 0.05	\$ 1.39

Diluted income per share for the three and nine months ended September 30, 2021 and 2022 excludes shares related to 155,000 market-based stock options, as modified, that vest on the sixth anniversary of the pricing of the Company's initial public offering ("IPO") with vesting based on the highest volume weighted average per share price for any ninety-calendar day period ("90-day VWAP") prior to the anniversary, with 0% vesting if the highest 90-day VWAP is \$80.00 or less and 100% vesting if the highest 90-day VWAP is \$110.00 or more, with linear interpolation in between (see Note 9). Such market-based criteria were not met at September 30, 2021 and 2022.

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)**

Focus LLC common, restricted common and incentive units may be exchanged for the Company's Class A common stock, subject to certain limitations (see Note 9). In computing the dilutive effect, if any, that the exchange would have on net income per share, net income attributable to Class A common shareholders would be adjusted due to the elimination of the non-controlling interests (including any associated tax impact). For the three and nine months ended September 30, 2021 and 2022, such exchange is not reflected in diluted net income per share as the assumed exchange is not dilutive.

4. ACQUISITIONS**Business Acquisitions**

Business acquisitions are accounted for in accordance with FASB Accounting Standards Codification ("ASC") Topic 805: *Business Combinations*.

The Company has incorporated contingent consideration, or earn out provisions, into the structure of its acquisitions. The Company recognizes the fair value of estimated contingent consideration at the acquisition date as part of the consideration transferred in the exchange. The contingent consideration is remeasured to fair value at each reporting date until the contingency is resolved. The purchase price associated with business acquisitions and the allocation thereof during the nine months ended September 30, 2022 is as follows:

	2022
Number of business acquisitions closed	11
Consideration:	
Cash due at closing	\$ 356,854
Estimated working capital adjustment and other	889
Cash due subsequent to closing at net present value	9,611
Fair market value of Focus LLC common units issued at closing	23,432
Fair market value of estimated contingent consideration	28,869
Total consideration	<u>\$ 419,655</u>
Allocation of purchase price:	
Total tangible assets	\$ 24,921
Total liabilities assumed	(29,072)
Customer relationships	232,125
Management contracts	8,805
Goodwill	181,302
Other acquired intangibles	1,574
Total allocated consideration	<u>\$ 419,655</u>

Management believes approximately \$368,287 of tax goodwill and intangibles related to business acquisitions completed during the nine months ended September 30, 2022 will be deductible for tax purposes over a 15 year period. Additional tax goodwill may be deductible when estimated contingent consideration is earned and paid.

The accompanying unaudited condensed consolidated statement of operations for the nine months ended September 30, 2022 includes revenue and income from operations for the three business acquisitions that are new subsidiary partner firms from the acquisition date of \$15,284 and \$460, respectively.

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)****Asset Acquisition**

The Company separately purchases customer relationships and other intangible assets. These purchases are accounted for as asset acquisitions as they do not qualify as business acquisitions pursuant to ASC Topic 805: *Business Combinations*. Total purchase consideration for asset acquisitions during the nine months ended September 30, 2022 consisted of cash of \$6,823, cash due subsequent to closing of \$3,000 and contingent consideration, the amount of which will be determined when the outcome is determinable.

The weighted-average useful lives of intangible assets acquired during the nine months ended September 30, 2022 are as follows:

	Number of years
Customer relationships	9
Management contracts	7
Other acquired intangibles	5
Weighted-average useful life of all intangibles acquired	9

From October 1, 2022 to November 3, 2022, in aggregate the Company completed eight acquisitions, consisting of asset acquisitions and business acquisitions for cash of \$44,452 plus contingent consideration.

5. GOODWILL AND OTHER INTANGIBLE ASSETS

The following table summarizes the change in the goodwill balances for the year ended December 31, 2021 and the nine months ended September 30, 2022:

	December 31, 2021	September 30, 2022
Balance beginning of period:		
Goodwill	\$ 1,278,183	\$ 1,947,939
Cumulative impairment losses	(22,624)	(22,624)
	<u>1,255,559</u>	<u>1,925,315</u>
Goodwill acquired	677,195	181,302
Other	(7,439)	(13,830)
	<u>669,756</u>	<u>167,472</u>
Balance end of period:		
Goodwill	1,947,939	2,115,411
Cumulative impairment losses	(22,624)	(22,624)
	<u>\$ 1,925,315</u>	<u>\$ 2,092,787</u>

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)**

The following table summarizes the amortizing acquired intangible assets at December 31, 2021:

	<u>Gross Carry Amount</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
Customer relationships	\$ 2,228,461	\$ (787,016)	\$ 1,441,445
Management contracts	191,578	(57,153)	134,425
Other acquired intangibles	10,911	(5,062)	5,849
Total	<u>\$ 2,430,950</u>	<u>\$ (849,231)</u>	<u>\$ 1,581,719</u>

The following table summarizes the amortizing acquired intangible assets at September 30, 2022:

	<u>Gross Carry Amount</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
Customer relationships	\$ 2,460,851	\$ (962,690)	\$ 1,498,161
Management contracts	199,761	(66,860)	132,901
Other acquired intangibles	13,219	(6,465)	6,754
Total	<u>\$ 2,673,831</u>	<u>\$ (1,036,015)</u>	<u>\$ 1,637,816</u>

6. FAIR VALUE MEASUREMENTS

ASC Topic 820, *Fair Value Measurement* establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability, developed based on market data obtained from sources independent of the Company. Unobservable inputs reflect the Company's own assumptions about the assumptions market participants would use in pricing the asset or liability, developed based on the best information available in the circumstances.

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels, as follows:

Level 1—Unadjusted price quotations in active markets for identical assets or liabilities.

Level 2—Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3—Significant unobservable inputs that are not corroborated by market data.

FOCUS FINANCIAL PARTNERS INC.

Notes to unaudited condensed consolidated financial statements (continued)

(In thousands, except unit data, share and per share amounts)

Marketable securities

At September 30, 2022, the fair value of the Company's investment in a mutual fund was \$16,591 which is included in prepaid expenses and other assets in the accompanying unaudited condensed consolidated balance sheets. The fair value was determined using Level 1 inputs.

First Lien Term Loan

The implied fair value of the Company's First Lien Term Loan (as defined below) based on Level 2 inputs at December 31, 2021 and September 30, 2022 are as follows:

	December 31, 2021		September 30, 2022	
	Stated Value	Fair Value	Stated Value	Fair Value
First Lien Term Loan - Tranche A	\$ 1,610,928	\$ 1,598,846	\$ 1,598,408	\$ 1,556,450
First Lien Term Loan - Tranche B	796,374	792,392	790,371	762,708

Derivatives

At December 31, 2021 and September 30, 2022, the fair value of the Company's \$850,000 notional amount interest rate swap agreements was \$5,810 and \$46,608, respectively, which is included in prepaid expenses and other assets in the accompanying unaudited condensed consolidated balance sheets. The fair value was based on Level 2 inputs which included the relevant interest rate forward curves.

Business acquisitions

For business acquisitions, the Company recognizes the fair value of goodwill and other acquired intangible assets, and estimated contingent consideration at the acquisition date as part of purchase price. This fair value measurement is based on unobservable (Level 3) inputs.

The following table represents changes in the fair value of estimated contingent consideration for business acquisitions for the year ended December 31, 2021 and the nine months ended September 30, 2022:

Balance at January 1, 2021	\$ 169,670
Additions to estimated contingent consideration	212,074
Payments of contingent consideration	(143,107)
Non-cash changes in fair value of estimated contingent consideration	112,416
Other	(1,026)
Balance at December 31, 2021	\$ 350,027
Additions to estimated contingent consideration	28,869
Assumed estimated contingent consideration obligation	12,637
Payments of contingent consideration	(116,449)
Non-cash changes in fair value of estimated contingent consideration	(82,450)
Other	(3,479)
Balance at September 30, 2022	\$ 189,155

Estimated contingent consideration is included in contingent consideration and other liabilities in the accompanying unaudited condensed consolidated balance sheets.

FOCUS FINANCIAL PARTNERS INC.

Notes to unaudited condensed consolidated financial statements (continued)

(In thousands, except unit data, share and per share amounts)

At December 31, 2021 and September 30, 2022, amounts due to sellers in connection with business acquisitions of \$114,156 and \$124,001, respectively, are included in contingent consideration and other liabilities in the unaudited condensed consolidated balance sheets.

During the year ended December 31, 2021, the Company paid \$131,827 in cash and issued \$11,280 in Focus LLC common units as contingent consideration associated with business acquisitions. During the nine months ended September 30, 2022, the Company paid \$106,751 in cash and issued \$9,698 in Focus LLC common units as contingent consideration associated with business acquisitions.

During the nine months ended September 30, 2021 and 2022, the Company paid cash of \$3,911 and \$8,646, respectively, as contingent consideration associated with asset acquisitions. These amounts are included in cash paid for acquisitions and contingent consideration—net of cash acquired in investing activities in the unaudited condensed consolidated statement of cash flows.

In determining fair value of the estimated contingent consideration, the acquired business' future performance is estimated using financial projections for the acquired business. These financial projections, as well as alternative scenarios of financial performance, are measured against the performance targets specified in each respective acquisition agreement. In addition, discount rates are established based on the cost of debt and the cost of equity. The Company uses the Monte Carlo Simulation Model to determine the fair value of the Company's estimated contingent consideration.

The significant unobservable inputs used in the fair value measurement of the Company's estimated contingent consideration are the forecasted growth rates over the measurement period and discount rates. Significant increases or decreases in the Company's forecasted growth rates over the measurement period or discount rates would result in a higher or lower fair value measurement.

Inputs used in the fair value measurement of estimated contingent consideration at December 31, 2021 and September 30, 2022 are summarized below:

Quantitative Information About Level 3 Fair Value Measurements			
Fair Value at December 31, 2021	Valuation Techniques	Unobservable Inputs	Ranges
\$ 350,027	Monte Carlo Simulation Model	Forecasted growth rates	0.7% - 20.1 %
		Discount rates	9.0% - 15.0 %

Quantitative Information About Level 3 Fair Value Measurements			
Fair Value at September 30, 2022	Valuation Techniques	Unobservable Inputs	Ranges
\$ 189,155	Monte Carlo Simulation Model	Forecasted growth rates	(25.8)% - 38.5 %
		Discount rates	12.0% - 19.0 %

7. CREDIT FACILITY

As of September 30, 2022, Focus LLC's credit facility (the "Credit Facility") consisted of a \$2,388,779 first lien term loan (the "First Lien Term Loan"), consisting of a tranche A ("Tranche A") and tranche B ("Tranche B"), and a \$650,000 first lien revolving credit facility (the "First Lien Revolver").

FOCUS FINANCIAL PARTNERS INC.

Notes to unaudited condensed consolidated financial statements (continued)

(In thousands, except unit data, share and per share amounts)

Tranche A bears interest (at Focus LLC's option) at: (i) LIBOR plus a margin of 2.00% or (ii) the lender's Base Rate (as defined in the Credit Facility) plus a margin of 1.00%. Tranche A requires quarterly installment repayments of \$4,173 and has a maturity date of July 2024.

Tranche B bears interest (at Focus LLC's option) at: (i) LIBOR plus a margin of 2.50% with a 0.50% LIBOR floor or (ii) the lender's Base Rate plus a margin of 1.50%. Tranche B requires quarterly installment repayments of \$2,001 and has a maturity date of June 2028.

In April 2022, Focus LLC amended the First Lien Revolver to extend the maturity date to June 2024 and change the benchmark interest rate from LIBOR to the Secured Overnight Financing Rate ("SOFR"). As amended, the First Lien Revolver bears interest (at Focus LLC's option) at SOFR, including a credit adjustment spread, plus a margin of 2.00% with step downs to 1.75%, 1.50% and 1.25% or the lender's Base Rate plus a margin of 1.00% with step downs to 0.75%, 0.50% and 0.25%, based on achievement of a specified First Lien Leverage Ratio. The First Lien Revolver unused commitment fee is 0.50% with step downs to 0.375% and 0.25% based on achievement of a specified First Lien Leverage Ratio. Up to \$30,000 of the First Lien Revolver is available for the issuance of letters of credit, subject to certain limitations. In connection with the amendment, Focus LLC incurred \$1,111 in debt financing costs.

Focus LLC's obligations under the Credit Facility are collateralized by the majority of Focus LLC's assets. The Credit Facility contains various customary covenants, including, but not limited to: (i) incurring additional indebtedness or guarantees, (ii) creating liens or other encumbrances on property or granting negative pledges, (iii) entering into a merger or similar transaction, (iv) selling or transferring certain property and (v) declaring dividends or making other restricted payments.

Focus LLC is required to maintain a First Lien Leverage Ratio (as defined in the Credit Facility) of not more than 6.25:1.00 as of the last day of each fiscal quarter. At September 30, 2022, Focus LLC's First Lien Leverage Ratio was 3.98:1.00, which satisfied the maximum ratio of 6.25:1.00. First Lien Leverage Ratio means the ratio of amounts outstanding under the First Lien Term Loan and First Lien Revolver plus other outstanding debt obligations secured by a lien on the assets of Focus LLC (excluding letters of credit other than unpaid drawings thereunder) minus unrestricted cash and cash equivalents to Consolidated EBITDA (as defined in the Credit Facility). Consolidated EBITDA for purposes of the Credit Facility was \$579,866 at September 30, 2022. Focus LLC is also subject on an annual basis to contingent principal payments based on an excess cash flow calculation (as defined in the Credit Facility) for any fiscal year if the First Lien Leverage Ratio exceeds 3.75:1.00. No contingent principal payments were required to be made in 2021. Based on the excess cash flow calculation for the year ended December 31, 2021, no contingent principal payments are required to be made in 2022.

The Company defers and amortizes its debt financing costs over the respective terms and tranches of the First Lien Term Loan and First Lien Revolver. The debt financing costs related to the First Lien Term Loan are recorded as a reduction of the carrying amount of the First Lien Term Loan in the unaudited condensed consolidated balance sheets. The debt financing costs related to the First Lien Revolver are recorded in debt financing costs-net in the unaudited condensed consolidated balance sheets.

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)**

The following is a reconciliation of principal amounts outstanding under the Credit Facility to borrowings under the Credit Facility recorded in the unaudited condensed consolidated balance sheets at December 31, 2021 and September 30, 2022:

	December 31, 2021	September 30, 2022
First Lien Term Loan - Tranche A	\$ 1,610,928	\$ 1,598,408
First Lien Term Loan - Tranche B	796,374	790,371
First Lien Revolver	—	50,000
Unamortized debt financing costs	(7,523)	(6,241)
Unamortized discount	(6,110)	(5,327)
Total	<u>\$ 2,393,669</u>	<u>\$ 2,427,211</u>

At December 31, 2021 and September 30, 2022, unamortized debt financing costs associated with the First Lien Revolver of \$4,254 and \$3,648, respectively, were recorded in debt financing costs-net in the unaudited condensed consolidated balance sheets.

Weighted-average interest rates for outstanding borrowings were approximately 3% for the year ended December 31, 2021 and the nine months ended September 30, 2022.

As of December 31, 2021 and September 30, 2022, the First Lien Revolver available unused commitment line was \$642,085 and \$590,079, respectively.

As of December 31, 2021 and September 30, 2022, Focus LLC was contingently obligated for letters of credit in the amount of \$7,915 and \$9,921, respectively, each bearing interest at an annual rate of approximately 2%.

8. DERIVATIVES

At September 30, 2022, the Company has (i) a 4 year floating to fixed interest rate swap with a notional amount of \$400,000 that was entered into in March 2020, the terms of which provide that the Company pays interest to the counterparty each month at a rate of 0.713% and receives interest from the counterparty each month at the 1 month USD LIBOR rate, subject to a 0% floor and (ii) two 4 year floating to fixed interest rate swap agreements with notional amounts of \$250,000 and \$200,000, that were entered into in April 2020, the terms of which provide that the Company pays interest to the counterparties each month at a rate of 0.537% and 0.5315%, respectively, and receives interest from the counterparties each month at the 1 month USD LIBOR rate, subject to a 0% floor. The interest rate swaps effectively fix the variable interest rate applicable to \$850,000 of borrowings outstanding on the First Lien Term Loan. The Company designated these swaps as cash flow hedges of the Company's exposure to the variability of the payment of interest on these portions of its First Lien Term Loan borrowings.

At December 31, 2021 and September 30, 2022, the fair value of the interest rate swaps was \$5,810 and \$46,608, respectively, which is included in prepaid expenses and other assets in the accompanying unaudited condensed consolidated balance sheets. The interest rate swaps continue to be effective hedges, and as such, the offsetting adjustment to the fair value is recorded in accumulated other comprehensive income (loss), net of tax of \$1,194 and \$10,181 at December 31, 2021 and September 30, 2022, respectively.

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)****9. EQUITY****Exchange rights**

Each Focus LLC common unit, together with a corresponding share of Focus Inc.'s Class B common stock, and Focus LLC incentive unit (after conversion into a number of Focus LLC common units taking into account the then-current value of the common units and such incentive unit's aggregate hurdle amount) is exchangeable, pursuant to the terms and subject to the conditions set forth in the Operating Agreement, for one share of Focus Inc.'s Class A common stock, or, if either Focus Inc. or Focus LLC so elects, cash.

In March 2022, the Company issued an aggregate of 26,956 shares of Class A common stock and retired 25,000 shares of Class B common stock and 4,250 incentive units in Focus LLC, and acquired 26,956 common units in Focus LLC, in each case as part of the regular quarterly exchanges offered to holders of units in Focus LLC.

In May 2022, the Company issued an aggregate of 80,000 shares of Class A common stock and retired 80,000 shares of Class B common stock and acquired 80,000 common units in Focus LLC, in each case as part of the regular quarterly exchanges offered to holders of units in Focus LLC.

In August 2022, the Company issued an aggregate of 396,731 shares of Class A common stock and retired 381,573 shares of Class B common stock and 36,357 incentive units in Focus LLC, and acquired 396,731 common units in Focus LLC, in each case as part of the regular quarterly exchanges offered to holders of units in Focus LLC.

Other

In February 2022, Focus LLC issued 187,795 common units and Focus Inc. issued a corresponding number of shares of Class B common stock in connection with a contingent consideration payment.

In April 2022, Focus LLC issued 512,290 common units and Focus Inc. issued a corresponding number of shares of Class B common stock in connection with an acquisition.

Stock Options and Restricted Stock Units

The following table provides information relating to the changes in the Company's stock options during the nine months ended September 30, 2022:

	Stock Options	Weighted Average Exercise Price
Outstanding—January 1, 2022	1,931,868	\$ 37.47
Granted	351,476	51.71
Exercised	(42,076)	27.54
Forfeited	(79,247)	51.95
Outstanding—September 30, 2022	<u>2,162,021</u>	39.45
Vested—September 30, 2022	<u>825,538</u>	31.70

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)**

The Company uses the Black-Scholes option-pricing model to determine the fair value of time-based stock options. The determination of the fair value using the Black-Scholes option-pricing model is affected by the price of Focus Inc.'s Class A common stock, as well as by assumptions regarding a number of complex and subjective variables. These variables include the Company's expected unit price volatility over the term of the stock option, expected term, risk-free interest rates and expected dividend yield.

The estimated grant-date fair value of the time-based stock option grants during the nine months ended September 30, 2022 were calculated based on the following weighted-average assumptions:

Expected term	6.3 years
Expected stock price volatility	34 %
Risk-free interest rate	1.85 %
Expected dividend yield	— %
Weighted average grant date fair value	\$ 19.08

The following table provides information relating to the changes in the Company's restricted stock units during the nine months ended September 30, 2022:

	Restricted Stock Units	Weighted Average Grant Date Fair Value
Outstanding—January 1, 2022	187,756	\$ 47.69
Granted	—	—
Forfeited	(15,713)	46.80
Vested	(78)	48.09
Outstanding—September 30, 2022	<u>171,965</u>	<u>47.77</u>

In connection with the IPO, the Company granted market-based stock options to purchase an aggregate of 155,000 shares of Class A common stock that would have vested on the fifth anniversary of the IPO if the 90-day VWAP within such five year period immediately following the IPO reaches at least \$100. In March 2022, these stock options were modified whereby the stock options will vest in July 2024, the sixth anniversary of the pricing of the Company's IPO, with vesting based on the highest 90-day VWAP prior to the anniversary, with 0% vesting if the highest 90-day VWAP is \$80.00 or less and 100% vesting if the highest 90-day VWAP is \$110.00 or more, with linear interpolation in between. The vested stock options can only be exercised in accordance with the following schedule: (i) a total of 25% of the vested stock options may be exercised on and following the date of vesting, (ii) an additional 25% (for a total of 50%) of the vested stock options may be exercised on and following the first anniversary of the date of vesting in July 2025, and (iii) an additional 50% (for a total of 100%) of the vested stock options may be exercised on and following the second anniversary of the date of vesting in July 2026. In connection with the modification, the Company will recognize incremental non-cash equity compensation expense of \$518 from the modification date through July 2026.

The Company recognized \$1,570 and \$3,860 of non-cash equity compensation expense in relation to the stock options and restricted stock units during the three and nine months ended September 30, 2021, respectively.

The Company recognized \$2,226 and \$6,323 of non-cash equity compensation expense in relation to the stock options and restricted stock units during the three and nine months ended September 30, 2022, respectively.

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)****Focus LLC Restricted Common Units and Focus LLC Incentive Units**

The following table provides information relating to the changes in Focus LLC restricted common units during the nine months ended September 30, 2022:

	Restricted Common Units	Weighted Average Grant Date Fair Value
Outstanding—January 1, 2022	193,625	\$ 54.70
Granted	—	—
Forfeited	—	—
Vested	(1,162)	58.50
Outstanding—September 30, 2022	<u>192,463</u>	54.68

The following table provides information relating to the changes in Focus LLC incentive units during the nine months ended September 30, 2022:

	Incentive Units	Weighted Average Hurdle Price
Outstanding—January 1, 2022	16,146,524	\$ 26.44
Granted	60,000	43.07
Exchanged	(40,607)	25.83
Forfeited	—	—
Outstanding—September 30, 2022	<u>16,165,917</u>	26.51
Vested—September 30, 2022	<u>9,827,010</u>	20.54

The Company uses the Black-Scholes option-pricing model to determine the fair value of time-based incentive units. The determination of the fair value using the Black-Scholes option-pricing model is affected by the Company's estimated common unit price, as well as by assumptions regarding a number of complex and subjective variables. These variables include the Company's expected unit price volatility over the term of the incentive unit, expected term, risk-free interest rates and expected dividend yield.

The estimated grant-date fair value of the time-based incentive unit grants during the nine months ended September 30, 2022 was calculated based on the following weighted-average assumptions:

Expected term	5.0 years
Expected stock price volatility	34 %
Risk-free interest rate	1.71 %
Expected dividend yield	— %
Weighted average grant date fair value	\$ 14.16

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)**

Incentive units outstanding and vested at September 30, 2022 were as follows:

Hurdle Rates	Number Outstanding	Vested Incentive Units
\$1.42	421	421
5.50	798	798
6.00	386	386
7.00	1,081	1,081
9.00	708,107	708,107
11.00	813,001	813,001
12.00	513,043	513,043
13.00	540,000	540,000
14.00	10,098	10,098
16.00	45,191	45,191
17.00	20,000	20,000
19.00	527,928	527,928
21.00	3,043,964	3,043,964
22.00	808,917	808,917
23.00	524,828	524,828
26.26	12,500	—
27.00	12,484	12,484
27.90	1,910,483	912,817
28.50	1,436,586	1,047,815
30.48	30,000	20,000
33.00	3,617,500	7,500
36.64	30,000	30,000
43.07	60,000	—
43.50	30,000	30,000
44.71	806,324	203,142
58.50	662,277	5,489
	<u>16,165,917</u>	<u>9,827,010</u>

In connection with the IPO, Focus LLC granted 3,845,000 market-based incentive units with a hurdle rate of \$33.00 that would have vested on the fifth anniversary of the IPO if the 90-day VWAP within such five year period immediately following the IPO reaches at least \$100. In March 2022, these incentive units were modified whereby the incentive units will vest in July 2024, the sixth anniversary of the pricing of the Company's IPO, with vesting based on the highest 90-day VWAP prior to the anniversary, with 0% vesting if the highest 90-day VWAP is \$80.00 or less and 100% vesting if the highest 90-day VWAP is \$110.00 or more, with linear interpolation in between. The vested incentive units can only be exchanged for Class A common stock in accordance with the following schedule: (i) a total of 25% of the vested incentive units may be exchanged on and following the date of vesting, (ii) an additional 25% (for a total of 50%) of the vested incentive units may be exchanged on and following the first anniversary of the date of vesting in July 2025, and (iii) an additional 50% (for a total of 100%) of the vested incentive units may be exchanged on and following the second anniversary of the date of vesting in July 2026. In connection with the modification, the Company will recognize incremental non-cash equity compensation expense of \$10,144 from the modification date through July 2024, the sixth anniversary of the IPO.

The Company recorded \$4,368 and \$20,709 in total non-cash equity compensation expense for incentive units and restricted common units during the three and nine months ended September 30, 2021, respectively.

FOCUS FINANCIAL PARTNERS INC.

Notes to unaudited condensed consolidated financial statements (continued)

(In thousands, except unit data, share and per share amounts)

The Company recorded \$5,754 and \$15,867 of non-cash equity compensation expense for incentive units and restricted common units during the three and nine months ended September 30, 2022, respectively.

10. INCOME TAXES

The estimated annual effective tax rate for the nine months ended September 30, 2022 was 32.1% as compared to 45.1% for the year ended December 31, 2021. Income tax expense for the nine months ended September 30, 2022 is primarily related to federal, state and local income taxes imposed on the Company's allocable portion of taxable income from Focus LLC and reflects an estimated valuation allowance of \$9,298 for deferred tax assets relating to business interest carryforwards. The allocable portion of taxable income primarily differs from the net income attributable to the Company due to permanent differences such as non-deductible equity-based compensation expense of Focus LLC.

During the nine months ended September 30, 2022, there were no changes to the Company's uncertain tax positions.

11. TAX RECEIVABLE AGREEMENTS

In connection with the IPO and the reorganization transactions that occurred in connection with the IPO, Focus Inc. entered into two tax receivable agreements: one with certain entities affiliated with the private equity investors of Focus LLC and the other with certain other continuing and former owners of Focus LLC. In March 2020, Focus Inc. entered into an additional tax receivable agreement (the three agreements, collectively, the "Tax Receivable Agreements") for tax receivable agreement holders that join Focus LLC as members after the closing of the IPO (the parties to the Tax Receivable Agreements, collectively, the "TRA Holders"). New Focus LLC owners in the future may also become party to this additional Tax Receivable Agreement. The Tax Receivable Agreements generally provide for the payment by Focus Inc. to each TRA holder of 85% of the net cash savings, if any, in U.S. federal, state and local income and franchise tax that Focus Inc. actually realizes (computed using simplifying assumptions to address the impact of state and local taxes) or is deemed to realize in certain circumstances in connection with the reorganization transactions that occurred in connection with the IPO and in periods after the IPO or after entering into the Tax Receivable Agreements, as applicable, as a result of certain increases in tax bases and certain tax benefits attributable to imputed interest. Focus Inc. will retain the benefit of the remaining 15% of these cash savings.

As of September 30, 2022, the Company had recorded a liability of \$221,237 relating to the TRA obligations. Future payments under the Tax Receivable Agreements in respect of future exchanges of Focus LLC units for shares of Class A common stock will be in addition to the amount recorded. During the nine months ended September 30, 2022, payments totaling \$3,856 were made under the Tax Receivable Agreements.

12. COMMITMENTS AND CONTINGENCIES

Credit Risk—The Company's broker-dealer subsidiaries clear all transactions through clearing brokers on a fully disclosed basis. Pursuant to the terms of the agreements between the Company's broker-dealer subsidiaries and their clearing brokers, the clearing brokers have the right to charge the Company's broker-dealer subsidiaries for losses that result from a counterparty's failure to fulfill its contractual obligations. This right applies to all trades executed through its clearing brokers, and therefore, the Company believes there is no

FOCUS FINANCIAL PARTNERS INC.

Notes to unaudited condensed consolidated financial statements (continued)

(In thousands, except unit data, share and per share amounts)

maximum amount assignable to the right of the clearing brokers. Accordingly, at December 31, 2021 and September 30, 2022, the Company had recorded no liabilities in connection with this right.

In addition, the Company has the right to pursue collection or performance from the counterparties who do not perform under their contractual obligations. The Company monitors the credit standing of the clearing brokers and counterparties with which they conduct business.

The Company is exposed to credit risk for accounts receivable from clients. Such credit risk is limited to the amount of accounts receivable. The Company is also exposed to credit risk for changes in the benchmark interest rate (LIBOR, SOFR or Base Rate) in connection with its Credit Facility.

The counterparties to the Company's derivative financial instruments are major international financial institutions. The Company is exposed to credit risk for the net exchanges under these agreements, but not for the notional amounts. The Company does not anticipate non-performance by any of its counterparties.

The Company maintains its cash in bank depository accounts, which, at times, may exceed federally insured limits. The Company selects depository institutions based, in part, upon management's review of the financial stability of the institution. At December 31, 2021 and September 30, 2022, a significant portion of cash and cash equivalents were held at a single institution.

Contingent Consideration Arrangements—Contingent consideration is payable in the form of cash and, in some cases, equity. Since the contingent consideration to be paid is based on the growth of forecasted financial performance levels over a number of years, the Company cannot calculate the maximum contingent consideration that may be payable under these arrangements.

Legal and Regulatory Matters— In the ordinary course of business, the Company and its subsidiaries are involved in lawsuits, regulatory matters and other claims. The Company has insurance to cover certain losses that arise in such matters; however, this insurance may not be sufficient to cover these losses. One of the Company's subsidiaries has settled most of the investor demands related to a private fund (that held approximately \$27 million in client assets) during the year ended December 31, 2021. The Company has notified its insurance carriers of the matter. Management, after consultation with legal counsel, currently does not anticipate that the aggregate liability, if any, arising out of any existing legal matters will have a material effect on the Company's consolidated financial position, results of operations or cash flows.

From time to time, the Company and its subsidiaries receive requests for information from governmental authorities regarding business activities. The Company has cooperated and plans to continue to cooperate with all governmental authorities. The Company continues to believe that the resolution of any governmental inquiry will not have a material impact on the Company's consolidated financial position, results of operations or cash flows.

Indemnifications—In the ordinary course of business, the Company enters into contracts pursuant to which it may agree to indemnify third parties in certain circumstances. The terms of these indemnities vary from contract to contract and the amount of indemnification liability, if any, cannot be determined.

Management believes that the likelihood of any material liability arising under these indemnification provisions is remote. Management cannot estimate any potential maximum exposure due to both the remoteness of any potential claims and the fact that items that would be included within any such calculated claim would be beyond the control of the Company. Consequently, no liability has been recorded in the unaudited condensed consolidated balance sheets.

FOCUS FINANCIAL PARTNERS INC.**Notes to unaudited condensed consolidated financial statements (continued)****(In thousands, except unit data, share and per share amounts)****13. CASH FLOW INFORMATION**

	Nine Months Ended September 30,	
	2021	2022
Supplemental disclosures of cash flow information—cash paid for:		
Interest	\$ 36,201	\$ 59,649
Income taxes	\$ 30,567	\$ 30,575
Supplemental non-cash cash flow information:		
Fair market value of estimated contingent consideration in connection with acquisitions	\$ 96,236	\$ 28,869

14. RELATED PARTIES

The Company's Chief Executive Officer, through an entity owned and controlled by him, owns a personal aircraft that was acquired without Company resources that he uses for business travel. The Company reimburses the Company's Chief Executive Officer for certain costs and third party payments associated with the use of his personal aircraft for Company-related business travel. The Company also pays pilot fees for such business travel flights. During the three and nine months ended September 30, 2021, the Company recognized expenses of \$381 and \$1,559, respectively, related to these reimbursements. During the three and nine months ended September 30, 2022, the Company recognized expenses of \$582 and \$3,012, respectively, related to these reimbursements. Given the geography of the Company's partner firms and prospects, the Company believes that the use of private aircraft creates efficiencies to enhance the productivity of the Company's Chief Executive Officer and certain other authorized personnel.

At September 30, 2022, affiliates of certain holders of the Company's Class A common stock and Class B common stock were lenders under the Credit Facility.

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

Unless otherwise indicated or the context requires, all references to “we,” “us,” “our,” the “Company,” “Focus Inc.” refer to Focus Financial Partners Inc. and its consolidated subsidiaries. “Focus LLC” refers to Focus Financial Partners, LLC, a Delaware limited liability company and our consolidated subsidiary.

The term “partner firms” refers to our consolidated subsidiaries engaged in wealth management and related services, the businesses of which are typically managed by the principals. The term “principals” refers to the wealth management professionals who manage the businesses of our partner firms pursuant to the relevant management agreement. The term “our partnership” refers to our business and relationship with our partner firms and is not intended to describe a particular form of legal entity or a legal relationship.

The following discussion and analysis of the financial condition and results of our operations should be read in conjunction with the accompanying unaudited condensed consolidated financial statements as of and for the three and nine months ended September 30, 2021 and 2022.

Forward-Looking Statements

Some of the information in this Quarterly Report on Form 10-Q may contain forward-looking statements. Forward-looking statements give our current expectations, contain projections of results of operations or of financial condition, or forecasts of future events. Words such as “may,” “assume,” “forecast,” “position,” “predict,” “strategy,” “expect,” “intend,” “plan,” “estimate,” “anticipate,” “believe,” “project,” “budget,” “potential,” “continue,” “will” and similar expressions are used to identify forward-looking statements. They can be affected by assumptions used or by known or unknown risks or uncertainties. Consequently, no forward-looking statements can be guaranteed. When considering these forward-looking statements, you should keep in mind the risk factors and other cautionary statements described under “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2021, as filed with the Securities and Exchange Commission (“SEC”) on February 17, 2022, and in our other filings with the SEC. Actual results may vary materially. You are cautioned not to place undue reliance on any forward-looking statements. You should also understand that it is not possible to predict or identify all such factors and should not consider the following list to be a complete statement of all potential risks and uncertainties. Factors that could cause our actual results to differ materially from the results contemplated by such forward-looking statements include:

- fluctuations in wealth management fees;
- our reliance on our partner firms and the principals who manage their businesses;
- our ability to make successful acquisitions;
- unknown liabilities of or poor performance by acquired businesses;
- harm to our reputation;
- our inability to facilitate smooth succession planning at our partner firms;
- our inability to compete;
- our reliance on key personnel and principals;
- our inability to attract, develop and retain talented wealth management professionals;
- our inability to retain clients following an acquisition;
- our reliance on key vendors;
- write down of goodwill and other intangible assets;
- our failure to maintain and properly safeguard an adequate technology infrastructure;
- cyber-attacks and other disruptions;

[Table of Contents](#)

- our inability to recover from business continuity problems;
- inadequate insurance coverage;
- impact of the novel coronavirus (“Covid-19”) outbreak on our business;
- the termination of management agreements by management companies;
- our inability to generate sufficient cash to service all of our indebtedness or our ability to access additional capital;
- the failure of our partner firms to comply with applicable U.S. and non-U.S. regulatory requirements and the highly regulated nature of our business;
- worsening economic conditions, including inflation, in the United States or internationally;
- wars or other geopolitical conflict;
- changes to laws and regulations;
- legal proceedings, governmental inquiries; and
- other factors discussed in this Quarterly Report on Form 10-Q, including in Part II, Item 1A. “Risk Factors”.

All forward-looking statements are expressly qualified in their entirety by the foregoing cautionary statements. Our forward-looking statements speak only as of the date of this Quarterly Report or as of the date as of which they are made. Except as required by applicable law, including federal securities laws, we do not intend to update or revise any forward-looking statements.

Overview

We are a leading partnership of independent, fiduciary wealth management firms operating in the highly fragmented registered investment advisor (“RIA”) industry, with a footprint of over 85 partner firms primarily in the United States. We have achieved this market leadership by positioning ourselves as the partner of choice for many firms in an industry where a number of secular trends are driving consolidation. Our partner firms primarily service ultra-high net worth and high net worth individuals and families by providing highly differentiated and comprehensive wealth management services. Our partner firms benefit from our intellectual and financial resources, operating as part of a scaled business model with aligned economic interests, while retaining their entrepreneurial culture and independence.

Our partnership is comprised of trusted professionals providing comprehensive wealth management services through a largely recurring, fee-based model, which differentiates our partner firms from the traditional brokerage platforms whose revenues are largely derived from commissions. We derive a substantial majority of our revenues from wealth management fees for investment advice, financial and tax planning, consulting, tax return preparation, family office services and other services. We also generate other revenues primarily from recordkeeping and administration service fees, commissions and distribution fees and outsourced services.

We have to date, with limited exceptions, acquired substantially all of the assets of the firms we chose to partner with but only a portion of the underlying economics in order to align the principals’ interests with our own objectives. To determine the acquisition price, we first estimate the operating cash flow of the business based on current and projected levels of revenue and expense, before compensation and benefits to the selling principals or other individuals who become principals. We refer to the operating cash flow of the business as Earnings Before Partner Compensation (“EBPC”) and to this EBPC estimate as Target Earnings (“Target Earnings”). In economic terms, we typically purchase only 40% to 60% of the partner firm’s EBPC. The purchase price is a multiple of the corresponding percentage of Target Earnings and may consist of cash or a combination of cash and equity, and the right to receive contingent consideration. We refer to the corresponding percentage of Target Earnings on which we base the purchase price as Base Earnings (“Base Earnings”). Under a management agreement between our operating subsidiary and the

[Table of Contents](#)

management company and the principals, the management company is entitled to management fees typically consisting of all future EBPC of the acquired wealth management firm in excess of Base Earnings up to Target Earnings, plus a percentage of any EBPC in excess of Target Earnings. Through the management agreement, we create downside protection for ourselves by retaining a preferred position in Base Earnings.

For mergers on behalf of our partner firms, including mergers for Connectus Wealth Advisers (“Connectus”), one of our partner firms, we typically purchase all of the target firms’ EBPC and principals and other personnel of the target firm join our partner firm as employees or may join the related management company as a principal in some instances. There typically is an adjustment to Target Earnings and Base Earnings in the related management agreement if applicable based on the economics of the transaction.

Since 2006, when we began revenue-generating and acquisition activities, we have created a partnership of over 85 partner firms, the substantial majority of which are RIAs registered with the SEC and built a business with revenues of approximately \$1.8 billion for the year ended December 31, 2021 and approximately \$1.6 billion for the nine months ended September 30, 2022. For the year ended December 31, 2021 and the nine months ended September 30, 2022, in excess of 95% of our revenues were fee-based and recurring in nature. We have established a national footprint across the United States and primarily expanded our international footprint into Australia, Canada, Switzerland and the United Kingdom.

Sources of Revenue

Our partner firms provide comprehensive wealth management services through a largely recurring, fee-based model. We derive a substantial majority of our revenue from wealth management fees, which are comprised of fees earned from wealth management services, including investment advice, financial and tax planning, consulting, tax return preparation, family office services and other services. Fees are primarily based either on a contractual percentage of the client’s assets based on the market value of the client’s assets on the predetermined billing date, a flat fee, an hourly rate based on predetermined billing rates or a combination of such fees and are billed either in advance or arrears on a monthly, quarterly or semiannual basis. In certain cases, such wealth management fees may be subject to minimum fee levels depending on the services performed. We also generate other revenues, which primarily include recordkeeping and administration service fees, commissions and distribution fees and outsourced services. The following table summarizes our sources of revenue:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2021		2022		2021		2022	
	Revenues	% of Total Revenues	Revenues	% of Total Revenues	Revenues	% of Total Revenues	Revenues	% of Total Revenues
	(dollars in thousands)							
Wealth management fees	\$ 433,967	95.5 %	\$ 499,017	96.0 %	\$ 1,213,782	95.3 %	\$ 1,531,617	96.0 %
Other	20,568	4.5 %	20,847	4.0 %	60,283	4.7 %	64,025	4.0 %
Total revenues	<u>\$ 454,535</u>	<u>100.0 %</u>	<u>\$ 519,864</u>	<u>100.0 %</u>	<u>\$ 1,274,065</u>	<u>100.0 %</u>	<u>\$ 1,595,642</u>	<u>100.0 %</u>

During the three and nine months ended September 30, 2022, our wealth management fees were impacted by the acquisition of new partner firms and the growth of existing partner firms, which includes the acquisitions of wealth management practices by our existing partner firms. During the three and nine months ended September 30, 2022, we completed the acquisition of two and three partner firms, respectively. During the three months ended September 30, 2022, the new partner firms were Octogone Holding and Icon Wealth Partners. During the nine months ended September 30, 2022, the new partner firms were Azimuth Capital Investment Management, Octogone Holding and Icon Wealth Partners. During the three and nine months ended September 30, 2022, our partner firms completed 7 and 12 acquisitions, respectively, consisting of business acquisitions accounted for in accordance with Financial Accounting Standards Board Accounting Standard Codification (“ASC”) Topic 805: *Business Combinations* and asset acquisitions.

[Table of Contents](#)

See Note 4 to our unaudited condensed consolidated financial statements for additional information about our acquisitions.

For the nine months ended September 30, 2022, in excess of 95% of our revenues were fee-based and recurring in nature. Although the substantial majority of our revenues are fee-based and recurring, our revenues can fluctuate due to macroeconomic factors and the overall state of the financial markets, particularly in the United States. Our partner firms' wealth management fees are primarily based either on a contractual percentage of the client's assets based on the market value of the client's assets on the predetermined billing date, a flat fee, an hourly rate based on predetermined billing rates or a combination of such fees and are billed either in advance or arrears on a monthly, quarterly or semiannual basis. Additionally, we estimate that approximately 24% and 23% of our revenues for the three and nine months ended September 30, 2022, respectively, were not directly correlated to the financial markets. Of the approximately 76% and 77% of our revenues that were directly correlated to the financial markets, primarily equities and fixed income, for the three and nine months ended September 30, 2022, respectively, we estimate that approximately 66% of such revenues were generated from advance billings. These revenues are impacted by market movements as a result of contractual provisions with clients that entitle our partner firms to bill for their services either in advance or arrears based on the value of client assets at such time. Since approximately 66% of our market correlated revenues are set based on the market value of client assets in advance of the respective service period, this generally results in a one quarter lagged effect of any market movements on our revenues. Longer term trends in the financial markets may favorably or unfavorably impact our total revenues, but not in a linear relationship.

Operating Expenses

Our operating expenses consist of compensation and related expenses, management fees, selling, general and administrative expenses, intangible amortization, non-cash changes in fair value of estimated contingent consideration and depreciation and other amortization expense.

Compensation and Related Expenses

Compensation and related expenses include salaries and wages, including variable compensation, related employee benefits and taxes for employees at our partner firms and employees at the Focus LLC company level. Compensation and related expenses also include non-cash compensation expense associated with both Focus Inc.'s and Focus LLC's equity grants to employees and non-employees, including management company principals.

Management Fees

While we have to date, with limited exceptions, acquired substantially all of the assets of a target firm, following our acquisition of a new partner firm, the partner firm continues to be primarily managed by its principals through their 100% ownership of a new management company formed by them concurrently with the acquisition. Our operating subsidiary, the management company and the principals enter into a management agreement that provides for the payment of ongoing management fees to the management company. The terms of the management agreements are generally six years subject to automatic renewals for consecutive one-year terms, unless earlier terminated by either the management company or us in certain limited situations. Under the management agreement, the management company is entitled to management fees typically consisting of all EBPC in excess of Base Earnings up to Target Earnings, plus a percentage of EBPC in excess of Target Earnings.

We generally retain a preferred position in Base Earnings. To the extent earnings of an acquired business in any year are less than Base Earnings, in the following year we are entitled to receive Base Earnings together with the prior years' shortfall before any management fees are earned by the management company.

[Table of Contents](#)

The following table provides an illustrative example of our economics, including management fees earned by the management company, for periods of projected revenues, +10% growth in revenues and -10% growth in revenues. This example assumes (i) Target Earnings of \$3.0 million; (ii) Base Earnings acquired of 60% of Target Earnings or \$1.8 million; and (iii) a percentage of earnings in excess of Target Earnings retained by the management company of 40%.

	<u>Projected Revenues</u>	<u>+10% Growth in Revenues</u>	<u>-10% Growth in Revenues</u>
	(in thousands)		
New Partner Firm			
New partner firm revenues	\$ 5,000	\$ 5,500	\$ 4,500
Less:			
Operating expenses (excluding management fees)	(2,000)	(2,000)	(2,000)
EBPC	\$ 3,000	\$ 3,500	\$ 2,500
Base Earnings to Focus Inc. (60%)	1,800	1,800	1,800
Management fees to management company (40%)	1,200	1,200	700
EBPC in excess of Target Earnings:			
To Focus Inc. (60%)	—	300	—
To management company as management fees (40%)	—	200	—
Focus Inc.			
Focus Inc. revenues	\$ 5,000	\$ 5,500	\$ 4,500
Less:			
Operating expenses (excluding management fees)	(2,000)	(2,000)	(2,000)
Less:			
Management fees to management company	(1,200)	(1,400)	(700)
Operating income	<u>\$ 1,800</u>	<u>\$ 2,100</u>	<u>\$ 1,800</u>

As a result of our economic arrangements with the various management company entities, 100% of management fees are variable expenses.

Selling, General and Administrative

Selling, general and administrative expenses include rent, insurance premiums, professional fees, travel and entertainment and other costs.

Intangible Amortization

Amortization of intangibles consists of the amortization of intangibles we acquired through our various acquisitions of new partner firms and acquisitions by our partner firms.

Non-Cash Changes in Fair Value of Estimated Contingent Consideration

We have typically incorporated into our acquisition structure contingent consideration paid to the sellers upon the satisfaction of specified financial thresholds, and the purchase price for a typical acquisition is comprised of a base purchase price and the right to receive such contingent consideration in the form of earn out payments. The contingent consideration for acquisitions of new partner firms is generally paid over a six-year period upon the satisfaction of specified growth thresholds, in years three and six. These growth thresholds are typically tied to the compound annual growth rate (“CAGR”) of the partner firm’s earnings. Such growth thresholds can be set annually or for different time frames as well, for example, annually over a six-year period. The contingent consideration for acquisitions made by our partner firms is paid upon the satisfaction of specified financial thresholds. These thresholds are generally tied to revenue as adjusted for certain criteria or other operating metrics based on the retention or growth of the business

[Table of Contents](#)

acquired. These arrangements may result in the payment of additional purchase price consideration to the sellers for periods following the closing of an acquisition. Contingent consideration payments are typically payable in cash and, in some cases, equity.

For business acquisitions, we recognize the fair value of estimated contingent consideration at the acquisition date as part of the consideration transferred in exchange for substantially all of the assets of the wealth management firm. The contingent consideration is remeasured to fair value at each reporting date until the contingency is resolved. Any changes in fair value are recognized each reporting period in non-cash changes in fair value of estimated contingent consideration in our consolidated statements of operations.

Depreciation and Other Amortization

Depreciation and other amortization expense primarily represents the benefits we received from using long-lived assets such as computers and equipment, leasehold improvements and furniture and fixtures. Those assets primarily consist of purchased fixed assets as well as fixed assets acquired through our acquisitions.

Business Acquisitions

We completed 11 business acquisitions during the nine months ended September 30, 2022, consisting of both new partner firms and acquisitions by partner firms. Such business acquisitions were accounted for in accordance with ASC Topic 805: *Business Combinations*.

The purchase price is comprised of a base purchase price and a right to receive contingent consideration in the form of earn out payments. The base purchase price typically consists of an upfront cash payment and may include equity. The contingent consideration for acquisitions of new partner firms generally consists of earn outs over a six-year period following the closing, with payment upon the satisfaction of specified growth thresholds in years three and six. The growth thresholds are typically tied to the CAGR of the partner firm's earnings. Such growth thresholds can be set annually or for different time frames as well, for example, annually over a six-year period. The contingent consideration for acquisitions made by our partner firms generally is earned upon the satisfaction of specified financial thresholds, typically annually. These thresholds are generally tied to revenue as adjusted for certain criteria or other operating metrics based on the retention or growth of the business acquired. The contingent consideration is typically payable in cash and, in some cases, equity.

The following table summarizes our business acquisitions for the nine months ended September 30, 2022 (dollars in thousands):

Number of business acquisitions closed	11
Consideration:	
Cash due at closing	\$ 356,854
Estimated working capital adjustment and other	889
Cash due subsequent to closing at net present value	9,611
Fair market value of Focus LLC common units issued at closing	23,432
Fair market value of estimated contingent consideration	28,869
Total consideration	<u>\$ 419,655</u>

During the nine months ended September 30, 2022, our acquisitions have been paid for with a combination of cash on hand, cash generated by our operations, borrowings under the Credit Facility and Focus LLC common units.

Recent Developments

From October 1, 2022 to the date of this Quarterly Report, in aggregate we completed eight acquisitions consisting of asset acquisitions and business acquisitions (accounted for in accordance with ASC Topic 805: *Business Combinations*), consisting of the acquisition of one new partner firm and acquisitions by partner firms. The estimated

[Table of Contents](#)

Acquired Base Earnings associated with the acquisition of the new partner firm during this period is \$2.0 million. Furthermore, we have signed a definitive purchase agreement to acquire an additional partner firm with Acquired Base Earnings of approximately \$5.3 million. This pending transaction is generally on terms and in a structure consistent with past transactions, and the closing is subject to customary closing conditions. Among other risks and uncertainties, there can be no guarantee that this pending acquisition will be completed. For additional information regarding Acquired Base Earnings, please see “—How We Evaluate Our Business.”

How We Evaluate Our Business

We focus on several key financial metrics in evaluating the success of our business, the success of our partner firms and our resulting financial position and operating performance. Key metrics for the three and nine months ended September 30, 2021 and 2022 include the following:

[Table of Contents](#)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2022	2021	2022
(dollars in thousands, except per share data)				
Revenue Metrics:				
Revenues	\$ 454,535	\$ 519,864	\$ 1,274,065	\$ 1,595,642
Revenue growth (1) from prior period	37.1 %	14.4 %	29.8 %	25.2 %
Organic revenue growth (2) from prior period	28.8 %	3.4 %	23.1 %	13.3 %
Management Fees Metrics (operating expense):				
Management fees	\$ 127,166	\$ 122,971	\$ 345,443	\$ 397,612
Management fees growth (3) from prior period	47.2 %	(3.3)%	39.8 %	15.1 %
Organic management fees growth (4) from prior period	38.7 %	(11.6)%	32.5 %	5.1 %
Net Income Metrics:				
Net income	\$ 1,849	\$ 38,289	\$ 9,505	\$ 126,689
Net income growth from prior period	(53.1)%	*	(77.0)%	*
Income per share of Class A common stock:				
Basic	\$ 0.01	\$ 0.45	\$ 0.05	\$ 1.40
Diluted	\$ 0.01	\$ 0.44	\$ 0.05	\$ 1.39
Income per share of Class A common stock growth from prior period:				
Basic	(66.7)%	*	(90.2)%	*
Diluted	(66.7)%	*	(90.2)%	*
Adjusted EBITDA Metrics:				
Adjusted EBITDA (5)	\$ 113,512	\$ 128,689	\$ 322,296	\$ 400,790
Adjusted EBITDA growth (5) from prior period	45.0 %	13.4 %	39.5 %	24.4 %
Adjusted Net Income Excluding Tax Adjustments Metrics:				
Adjusted Net Income Excluding Tax Adjustments (5)	\$ 68,521	\$ 70,052	\$ 199,770	\$ 234,804
Adjusted Net Income Excluding Tax Adjustments growth (5) from prior period	42.9 %	2.2 %	44.2 %	17.5 %
Tax Adjustments				
Tax Adjustments (5)(6)	\$ 11,835	\$ 16,664	\$ 33,365	\$ 47,454
Tax Adjustments growth from prior period (5)(6)	27.4 %	40.8 %	21.8 %	42.2 %
Adjusted Net Income Excluding Tax Adjustments Per Share and Tax Adjustments Per Share Metrics:				
Adjusted Net Income Excluding Tax Adjustments Per Share (5)	\$ 0.84	\$ 0.86	\$ 2.44	\$ 2.88
Tax Adjustments Per Share (5)(6)	\$ 0.14	\$ 0.20	\$ 0.41	\$ 0.58
Adjusted Net Income Excluding Tax Adjustments Per Share growth (5) from prior period	33.3 %	2.4 %	34.1 %	18.0 %
Tax Adjustments Per Share growth from prior period (5)(6)	16.7 %	42.9 %	13.9 %	41.5 %
Adjusted Shares Outstanding				
Adjusted Shares Outstanding (5)	81,829,784	81,597,322	81,708,469	81,509,075
Other Metrics:				
Net Leverage Ratio (7) at period end	3.54x	3.98x	3.54x	3.98x
Acquired Base Earnings (8)	\$ 10,950	\$ 7,849	\$ 21,913	\$ 19,299
Number of partner firms at period end (9)	76	87	76	87

* Not meaningful

[Table of Contents](#)

- (1) Represents period-over-period growth in our GAAP revenue.
- (2) Organic revenue growth represents the period-over-period growth in revenue related to partner firms, including growth related to acquisitions of wealth management practices and customer relationships by our partner firms, including Connectus, and partner firms that have merged, that for the entire periods presented, are included in our consolidated statements of operations for each of the entire periods presented. We believe these growth statistics are useful in that they present full-period revenue growth of partner firms on a “same store” basis exclusive of the effect of the partial period results of partner firms that are acquired during the comparable periods.
- (3) The terms of our management agreements entitle the management companies to management fees typically consisting of all EBPC in excess of Base Earnings up to Target Earnings, plus a percentage of any EBPC in excess of Target Earnings. Management fees growth represents the period-over-period growth in GAAP management fees earned by management companies. While an expense, we believe that growth in management fees reflect the strength of the partnership.
- (4) Organic management fees growth represents the period-over-period growth in management fees earned by management companies related to partner firms, including growth related to acquisitions of wealth management practices and customer relationships by our partner firms and partner firms that have merged, that for the entire periods presented, are included in our consolidated statements of operations for each of the entire periods presented. We believe that these growth statistics are useful in that they present full-period growth of management fees on a “same store” basis exclusive of the effect of the partial period results of partner firms that are acquired during the comparable periods.
- (5) For additional information regarding Adjusted EBITDA, Adjusted Net Income Excluding Tax Adjustments, Adjusted Net Income Excluding Tax Adjustments Per Share, Tax Adjustments, Tax Adjustments Per Share and Adjusted Shares Outstanding, including a reconciliation of Adjusted EBITDA, Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share to the most directly comparable GAAP financial measure, please read “—Adjusted EBITDA” and “—Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share.”
- (6) Tax Adjustments represent the tax benefits of intangible assets, including goodwill, associated with deductions allowed for tax amortization of intangible assets in the respective periods based on a pro forma 27% income tax rate. Such amounts were generated from acquisitions completed where we received a step-up in basis for tax purposes. Acquired intangible assets may be amortized for tax purposes, generally over a 15-year period. Due to our acquisitive nature, tax deductions allowed on acquired intangible assets provide additional significant supplemental economic benefit. The tax benefit from amortization is included to show the full economic benefit of deductions for acquired intangible assets with the step-up in tax basis. As of September 30, 2022, estimated Tax Adjustments from intangible asset related income tax benefits from closed acquisitions based on a pro forma 27% income tax rate for the next 12 months is \$65,666.
- (7) Net Leverage Ratio represents the First Lien Leverage Ratio (as defined in the Credit Facility), and means the ratio of amounts outstanding under the First Lien Term Loan and First Lien Revolver plus other outstanding debt obligations secured by a lien on the assets of Focus LLC (excluding letters of credit other than unpaid drawings thereunder) minus unrestricted cash and cash equivalents to Consolidated EBITDA (as defined in the Credit Facility).
- (8) The terms of our management agreements entitle the management companies to management fees typically consisting of all future EBPC of the acquired wealth management firm in excess of Base Earnings up to Target Earnings, plus a percentage of any EBPC in excess of Target Earnings. Acquired Base Earnings is equal to our collective preferred position in Base Earnings or comparable measures. We are entitled to receive these earnings notwithstanding any earnings that we are entitled to receive in excess of Target Earnings. Base Earnings may change in future periods for various business or contractual matters. For example, from time to time when a partner firm consummates an acquisition, the management agreement among the partner firm, the management company

[Table of Contents](#)

and the principals is amended to adjust Base Earnings and Target Earnings to reflect the projected post-acquisition earnings of the partner firm.

(9) Represents the number of partner firms on the last day of the period presented.

Adjusted EBITDA

Adjusted EBITDA is a non-GAAP measure. Adjusted EBITDA is defined as net income excluding interest income, interest expense, income tax expense, amortization of debt financing costs, intangible amortization and impairments, if any, depreciation and other amortization, non-cash equity compensation expense, non-cash changes in fair value of estimated contingent consideration, other income (expense)-net and secondary offering expenses, if any. We believe that Adjusted EBITDA, viewed in addition to and not in lieu of, our reported GAAP results, provides additional useful information to investors regarding our performance and overall results of operations for various reasons, including the following:

- non-cash equity grants made to employees or non-employees at a certain price and point in time do not necessarily reflect how our business is performing at any particular time; stock-based compensation expense is not a key measure of our operating performance;
- contingent consideration or earn outs can vary substantially from company to company and depending upon each company's growth metrics and accounting assumption methods; the non-cash changes in fair value of estimated contingent consideration is not considered a key measure in comparing our operating performance; and
- amortization expenses can vary substantially from company to company and from period to period depending upon each company's financing and accounting methods, the fair value and average expected life of acquired intangible assets and the method by which assets were acquired; the amortization of intangible assets obtained in acquisitions are not considered a key measure in comparing our operating performance.

We use Adjusted EBITDA:

- as a measure of operating performance;
- for planning purposes, including the preparation of budgets and forecasts;
- to allocate resources to enhance the financial performance of our business;
- to evaluate the effectiveness of our business strategies; and
- as a consideration in determining compensation for certain employees.

Adjusted EBITDA does not purport to be an alternative to net income or cash flows from operating activities. The term Adjusted EBITDA is not defined under GAAP, and Adjusted EBITDA is not a measure of net income, operating income or any other performance or liquidity measure derived in accordance with GAAP. Therefore, Adjusted EBITDA has limitations as an analytical tool and should not be considered in isolation or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are:

- Adjusted EBITDA does not reflect all cash expenditures, future requirements for capital expenditures or contractual commitments;
- Adjusted EBITDA does not reflect changes in, or cash requirements for, working capital needs; and
- Adjusted EBITDA does not reflect the interest expense on our debt or the cash requirements necessary to service interest or principal payments.

[Table of Contents](#)

In addition, Adjusted EBITDA can differ significantly from company to company depending on strategic decisions regarding capital structure, the tax jurisdictions in which companies operate and capital investments. We compensate for these limitations by relying also on the GAAP results and using Adjusted EBITDA as supplemental information.

Set forth below is a reconciliation of net income to Adjusted EBITDA for the three and nine months ended September 30, 2021 and 2022:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2022	2021	2022
	(in thousands)			
Net income	\$ 1,849	\$ 38,289	\$ 9,505	\$ 126,689
Interest income	(206)	(126)	(310)	(146)
Interest expense	16,543	26,491	37,893	63,999
Income tax expense	2,678	12,120	6,038	59,965
Amortization of debt financing costs	1,102	949	2,856	2,999
Intangible amortization	46,055	67,331	133,041	192,256
Depreciation and other amortization	3,622	4,016	10,835	11,454
Non-cash equity compensation expense	5,938	7,980	24,569	22,190
Non-cash changes in fair value of estimated contingent consideration	36,243	(30,708)	96,241	(82,450)
Other (income) expense—net	(312)	2,347	219	3,834
Secondary offering expenses	—	—	1,409	—
Adjusted EBITDA	<u>\$ 113,512</u>	<u>\$ 128,689</u>	<u>\$ 322,296</u>	<u>\$ 400,790</u>

Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share

We analyze our performance using Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share. Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share are non-GAAP measures. We define Adjusted Net Income Excluding Tax Adjustments as net income excluding income tax expense, amortization of debt financing costs, intangible amortization and impairments, if any, non-cash equity compensation expense, non-cash changes in fair value of estimated contingent consideration and secondary offering expenses, if any. The calculation of Adjusted Net Income Excluding Tax Adjustments also includes adjustments to reflect a pro forma 27% income tax rate reflecting the estimated U.S. Federal, state, local and foreign income tax rates applicable to corporations in the jurisdictions we conduct business.

Adjusted Net Income Excluding Tax Adjustments Per Share is calculated by dividing Adjusted Net Income Excluding Tax Adjustments by the Adjusted Shares Outstanding. Adjusted Shares Outstanding includes: (i) the weighted average shares of Class A common stock outstanding during the periods, (ii) the weighted average incremental shares of Class A common stock related to stock options and restricted stock units outstanding during the periods, (iii) the weighted average number of Focus LLC common units outstanding during the periods (assuming that 100% of such Focus LLC common units, including contingently issuable Focus LLC common units, if any, have been exchanged for Class A common stock), (iv) the weighted average number of Focus LLC restricted common units outstanding during the periods (assuming that 100% of such Focus LLC restricted common units have been exchanged for Class A common stock) and (v) the weighted average number of common unit equivalents of Focus LLC vested and unvested incentive units outstanding during the periods based on the closing price of our Class A common stock on the last trading day of the periods (assuming that 100% of such Focus LLC common units have been exchanged for Class A common stock).

We believe that Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share, viewed in addition to and not in lieu of, our reported GAAP results, provide additional useful

[Table of Contents](#)

information to investors regarding our performance and overall results of operations for various reasons, including the following:

- non-cash equity grants made to employees or non-employees at a certain price and point in time do not necessarily reflect how our business is performing at any particular time; stock-based compensation expense is not a key measure of our operating performance;
- contingent consideration or earn outs can vary substantially from company to company and depending upon each company's growth metrics and accounting assumption methods; the non-cash changes in fair value of estimated contingent consideration is not considered a key measure in comparing our operating performance; and
- amortization expenses can vary substantially from company to company and from period to period depending upon each company's financing and accounting methods, the fair value and average expected life of acquired intangible assets and the method by which assets were acquired; the amortization of intangible assets obtained in acquisitions are not considered a key measure in comparing our operating performance.

Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share do not purport to be an alternative to net income or cash flows from operating activities. The terms Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share are not defined under GAAP, and Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share are not a measure of net income, operating income or any other performance or liquidity measure derived in accordance with GAAP. Therefore, Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share have limitations as an analytical tool and should not be considered in isolation or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are:

- Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share do not reflect all cash expenditures, future requirements for capital expenditures or contractual commitments;
- Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share do not reflect changes in, or cash requirements for, working capital needs; and
- Other companies in the financial services industry may calculate Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share differently than we do, limiting its usefulness as a comparative measure.

In addition, Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share can differ significantly from company to company depending on strategic decisions regarding capital structure, the tax jurisdictions in which companies operate and capital investments. We compensate for these limitations by relying also on the GAAP results and use Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share as supplemental information.

Tax Adjustments and Tax Adjustments Per Share

Tax Adjustments represent the tax benefits of intangible assets, including goodwill, associated with deductions allowed for tax amortization of intangible assets in the respective periods based on a pro forma 27% income tax rate. Such amounts were generated from acquisitions completed where we received a step-up in basis for tax purposes. Acquired intangible assets may be amortized for tax purposes, generally over a 15-year period. Due to our acquisitive nature, tax deductions allowed on acquired intangible assets provide additional significant supplemental economic

[Table of Contents](#)

benefit. The tax benefit from amortization is included to show the full economic benefit of deductions for acquired intangible assets with the step-up in tax basis.

Tax Adjustments Per Share is calculated by dividing Tax Adjustments by the Adjusted Shares Outstanding.

Set forth below is a reconciliation of net income to Adjusted Net Income Excluding Tax Adjustments and Adjusted Net Income Excluding Tax Adjustments Per Share for the three and nine months ended September 30, 2021 and 2022:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2021	2022	2021	2022
	(dollars in thousands, except per share data)			
Net income	\$ 1,849	\$ 38,289	\$ 9,505	\$ 126,689
Income tax expense	2,678	12,120	6,038	59,965
Amortization of debt financing costs	1,102	949	2,856	2,999
Intangible amortization	46,055	67,331	133,041	192,256
Non-cash equity compensation expense	5,938	7,980	24,569	22,190
Non-cash changes in fair value of estimated contingent consideration	36,243	(30,708)	96,241	(82,450)
Secondary offering expenses (1)	—	—	1,409	—
Subtotal	93,865	95,961	273,659	321,649
Pro forma income tax expense (27%) (2)	(25,344)	(25,909)	(73,889)	(86,845)
Adjusted Net Income Excluding Tax Adjustments	\$ 68,521	\$ 70,052	\$ 199,770	\$ 234,804
Tax Adjustments (3)	\$ 11,835	\$ 16,664	\$ 33,365	\$ 47,454
Adjusted Net Income Excluding Tax Adjustments Per Share	\$ 0.84	\$ 0.86	\$ 2.44	\$ 2.88
Tax Adjustments Per Share (3)	\$ 0.14	\$ 0.20	\$ 0.41	\$ 0.58
Adjusted Shares Outstanding	81,829,784	81,597,322	81,708,469	81,509,075
Calculation of Adjusted Shares Outstanding:				
Weighted average shares of Class A common stock outstanding—basic (4)	59,940,166	65,599,493	55,978,639	65,441,151
Adjustments:				
Weighted average incremental shares of Class A common stock related to stock options and restricted stock units (5)	498,344	221,735	468,431	288,188
Weighted average Focus LLC common units outstanding (6)	12,609,173	11,898,233	16,263,935	11,899,456
Weighted average Focus LLC restricted common units outstanding (7)	71,374	192,627	71,374	193,289
Weighted average common unit equivalent of Focus LLC incentive units outstanding (8)	8,710,727	3,685,234	8,926,090	3,686,991
Adjusted Shares Outstanding	81,829,784	81,597,322	81,708,469	81,509,075

(1) Relates to offering expenses associated with the March 2021 and June 2021 secondary equity offerings.

(2) The pro forma income tax rate of 27% reflects the estimated U.S. Federal, state, local and foreign income tax rates applicable to corporations in the jurisdictions we conduct business.

(3) Tax Adjustments represent the tax benefits of intangible assets, including goodwill, associated with deductions allowed for tax amortization of intangible assets in the respective periods based on a pro forma 27% income tax rate. Such amounts were generated from acquisitions completed where we received a step-up in basis for tax purposes. Acquired intangible assets may be amortized for tax purposes, generally over a 15-year period. Due to our

[Table of Contents](#)

acquisitive nature, tax deductions allowed on acquired intangible assets provide additional significant supplemental economic benefit. The tax benefit from amortization is included to show the full economic benefit of deductions for acquired intangible assets with the step-up in tax basis. As of September 30, 2022, estimated Tax Adjustments from intangible asset related income tax benefits from closed acquisitions based on a pro forma 27% income tax rate for the next 12 months is \$65,666.

- (4) Represents our GAAP weighted average Class A common stock outstanding—basic.
- (5) Represents the incremental shares related to stock options and restricted stock units as calculated under the treasury stock method.
- (6) Assumes that 100% of the Focus LLC common units, including contingently issuable Focus LLC common units, if any, were exchanged for Class A common stock.
- (7) Assumes that 100% of the Focus LLC restricted common units were exchanged for Class A common stock.
- (8) Assumes that 100% of the vested and unvested Focus LLC incentive units were converted into Focus LLC common units based on the closing price of our Class A common stock at the end of the respective period and such Focus LLC common units were exchanged for Class A common stock.

Results of Operations

Three Months Ended September 30, 2021 Compared to Three Months Ended September 30, 2022

The following discussion presents an analysis of our results of operations for the three months ended September 30, 2021 and 2022. Where appropriate, we have identified specific events and changes that affect comparability or trends and, where possible and practical, have quantified the impact of such items.

	Three Months Ended September 30,		\$ Change	% Change
	2021	2022		
	(dollars in thousands)			
Revenues:				
Wealth management fees	\$ 433,967	\$ 499,017	\$ 65,050	15.0 %
Other	20,568	20,847	279	1.4 %
Total revenues	<u>454,535</u>	<u>519,864</u>	<u>65,329</u>	14.4 %
Operating expenses:				
Compensation and related expenses	144,249	186,320	42,071	29.2 %
Management fees	127,166	122,971	(4,195)	(3.3)%
Selling, general and administrative	75,637	89,915	14,278	18.9 %
Intangible amortization	46,055	67,331	21,276	46.2 %
Non-cash changes in fair value of estimated contingent consideration	36,243	(30,708)	(66,951)	*
Depreciation and other amortization	3,622	4,016	394	10.9 %
Total operating expenses	<u>432,972</u>	<u>439,845</u>	<u>6,873</u>	1.6 %
Income from operations	<u>21,563</u>	<u>80,019</u>	<u>58,456</u>	*
Other income (expense):				
Interest income	206	126	(80)	(38.8)%
Interest expense	(16,543)	(26,491)	(9,948)	(60.1)%
Amortization of debt financing costs	(1,102)	(949)	153	13.9 %
Other income (expense)—net	312	(2,347)	(2,659)	*
Income from equity method investments	91	51	(40)	(44.0)%
Total other expense—net	<u>(17,036)</u>	<u>(29,610)</u>	<u>(12,574)</u>	(73.8)%
Income before income tax	4,527	50,409	45,882	*
Income tax expense	2,678	12,120	9,442	*
Net income	<u>\$ 1,849</u>	<u>\$ 38,289</u>	<u>\$ 36,440</u>	*

* Not meaningful

Revenues

Wealth management fees increased \$65.1 million, or 15.0%, for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. New partner firms added subsequent to the three months ended September 30, 2021 that are included in our results of operations for the three months ended September 30, 2022 include Ancora Holdings, Sonora Investment Management, Cardinal Point, Ullmann Wealth Partners, Mosaic Family Wealth, Alley Company, Cassaday & Company, Provident Financial Management, Azimuth Capital Investment Management, Octogone Holding and Icon Wealth Partners. Additionally, our partner firms completed 25 acquisitions subsequent to the three months ended September 30, 2021. The new partner firms contributed approximately \$47.5 million in revenue during the three months ended September 30, 2022. The balance of the increase of \$17.6 million was due to the revenue growth at our existing partner firms, including Connectus, associated with wealth management services, which includes partner firm-level acquisitions.

Other revenues increased \$0.3 million, or 1.4%, for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. Other revenues from new partner firms was approximately \$0.9 million.

[Table of Contents](#)

Operating Expenses

Compensation and related expenses increased \$42.1 million, or 29.2%, for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. The increase related to new partner firms was approximately \$13.5 million. Non-cash equity compensation increased \$2.0 million primarily from equity grants in 2021 and incremental non-cash equity compensation expense from the modification of certain equity awards in 2022. The balance of the increase of \$26.6 million was due primarily to an increase in salaries and related expense due to the growth of existing partner firms, including Connecticut, and partner firm-level acquisitions.

Management fees decreased \$4.2 million, or 3.3%, for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. This reflects an increase related to new partner firms of approximately \$10.3 million. Management fees are variable and a function of earnings during the period. This increase was offset by a \$14.5 million decrease in profitability splits with the management companies during the three months ended September 30, 2022 compared to the three months ended September 30, 2021.

Selling, general and administrative expenses increased \$14.3 million, or 18.9%, for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. New partner firms added approximately \$8.2 million. The balance of the increase of \$6.1 million was due primarily to an increase in expenses related to travel and entertainment and information technology expenses related to the growth of our existing partner firms, including Connecticut, and partner firm-level acquisitions.

Intangible amortization increased \$21.3 million, or 46.2%, for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. The increase related to new partner firms was approximately \$12.2 million. The balance of the increase of \$9.1 million was due primarily to partner firm-level acquisitions.

Non-cash changes in fair value of estimated contingent consideration decreased \$67.0 million for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. During the three months ended September 30, 2022, the probability that certain contingent consideration payments would be achieved decreased due to Monte Carlo Simulation changes associated with market conditions and forecasts, resulting in a decrease in the fair value of the contingent consideration liability.

Other income (expense)

Interest expense increased \$9.9 million, or 60.1%, for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. The increase was due primarily to higher average outstanding borrowings and higher average interest rates during the three months ended September 30, 2022 compared to the three months ended September 30, 2021.

Income Tax Expense

Income tax expense increased \$9.4 million for the three months ended September 30, 2022 compared to the three months ended September 30, 2021. For the three months ended September 30, 2022, we recorded tax expense based on an estimated annual effective tax rate of 32.1%. The estimated annual effective tax rate is primarily related to federal, state and local income taxes imposed on Focus Inc.'s allocable portion of taxable income from Focus LLC and reflects an estimated valuation allowance of \$9.3 million for deferred tax assets relating to business interest carryforwards.

Nine Months Ended September 30, 2021 Compared to Nine Months Ended September 30, 2022

The following discussion presents an analysis of our results of operations for the nine months ended September 30, 2021 and 2022. Where appropriate, we have identified specific events and changes that affect comparability or trends and, where possible and practical, have quantified the impact of such items.

	Nine Months Ended September 30,		\$ Change	% Change
	2021	2022		
	(dollars in thousands)			
Revenues:				
Wealth management fees	\$ 1,213,782	\$ 1,531,617	\$ 317,835	26.2 %
Other	60,283	64,025	3,742	6.2 %
Total revenues	<u>1,274,065</u>	<u>1,595,642</u>	<u>321,577</u>	25.2 %
Operating expenses:				
Compensation and related expenses	424,337	546,251	121,914	28.7 %
Management fees	345,443	397,612	52,169	15.1 %
Selling, general and administrative	208,481	273,336	64,855	31.1 %
Intangible amortization	133,041	192,256	59,215	44.5 %
Non-cash changes in fair value of estimated contingent consideration	96,241	(82,450)	(178,691)	*
Depreciation and other amortization	10,835	11,454	619	5.7 %
Total operating expenses	<u>1,218,378</u>	<u>1,338,459</u>	<u>120,081</u>	9.9 %
Income from operations	<u>55,687</u>	<u>257,183</u>	<u>201,496</u>	*
Other income (expense):				
Interest income	310	146	(164)	(52.9)%
Interest expense	(37,893)	(63,999)	(26,106)	(68.9)%
Amortization of debt financing costs	(2,856)	(2,999)	(143)	(5.0)%
Other expense—net	(219)	(3,834)	(3,615)	*
Income from equity method investments	514	157	(357)	(69.5)%
Total other expense—net	<u>(40,144)</u>	<u>(70,529)</u>	<u>(30,385)</u>	(75.7)%
Income before income tax	15,543	186,654	171,111	*
Income tax expense	6,038	59,965	53,927	*
Net income	<u>\$ 9,505</u>	<u>\$ 126,689</u>	<u>\$ 117,184</u>	*

Revenues

Wealth management fees increased \$317.8 million, or 26.2%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. New partner firms added subsequent to the nine months ended September 30, 2021 that are included in our results of operations for the nine months ended September 30, 2022 include Ancora Holdings, Sonora Investment Management, Cardinal Point, Ullmann Wealth Partners, Mosaic Family Wealth, Alley Company, Cassaday & Company, Provident Financial Management, Azimuth Capital Investment Management, Octogone Holding and Icon Wealth Partners. Additionally, our partner firms completed 25 acquisitions subsequent to the nine months ended September 30, 2021. The new partner firms contributed approximately \$127.1 million in revenue during the nine months ended September 30, 2022. The balance of the increase of \$190.7 million was due to the revenue growth at our existing partner firms, including Connectus, associated with wealth management services, which includes partner firm-level acquisitions, as well as a full period of revenue recognized during the nine months ended September 30, 2022 for partner firms that were acquired during the nine months ended September 30, 2021.

[Table of Contents](#)

Other revenues increased \$3.7 million, or 6.2%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. Other revenues from new partner firms was approximately \$2.4 million. The balance of the increase of \$1.3 million was due primarily to an increase in recordkeeping and administration fees.

Operating Expenses

Compensation and related expenses increased \$121.9 million, or 28.7%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. The increase related to new partner firms was approximately \$34.3 million. The balance of the increase of \$87.6 million was due primarily to an increase in salaries and related expense due to the growth of existing partner firms, including Connectus, and partner firm-level acquisitions offset in part by a decrease in non-cash equity compensation expense of \$2.4 million.

Management fees increased \$52.2 million, or 15.1%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. The increase related to new partner firms was approximately \$30.0 million. Management fees are variable and a function of earnings during the period. The balance of the increase of \$22.2 million was primarily due to partner firm-level acquisitions as well as a full period of management fees during the nine months ended September 30, 2022 for partner firms that were acquired during the nine months ended September 30, 2021.

Selling, general and administrative expenses increased \$64.9 million, or 31.1%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. New partner firms added approximately \$20.4 million. The balance of the increase of \$44.5 million was due primarily to an increase in expenses related to travel and entertainment, professional fees, information technology expenses and referral fees related to the growth of our existing partner firms, including Connectus, and partner firm-level acquisitions.

Intangible amortization increased \$59.2 million, or 44.5%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. The increase related to new partner firms was approximately \$31.9 million. The balance of the increase of \$27.3 million was due primarily to partner firm-level acquisitions.

Non-cash changes in fair value of estimated contingent consideration decreased \$178.7 million for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. During the nine months ended September 30, 2022, the probability that certain contingent consideration payments would be achieved decreased due to Monte Carlo Simulation changes associated with market conditions and forecasts, resulting in a decrease in the fair value of the contingent consideration liability.

Other income (expense)

Interest expense increased \$26.1 million, or 68.9%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. The increase was due primarily to higher average outstanding borrowings and higher average interest rates during the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021.

[Table of Contents](#)

Income Tax Expense

Income tax expense increased \$53.9 million for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. For the nine months ended September 30, 2022, we recorded tax expense based on an estimated annual effective tax rate of 32.1%. The estimated annual effective tax rate is primarily related to federal, state and local income taxes imposed on Focus Inc.'s allocable portion of taxable income from Focus LLC and reflects an estimated valuation allowance of \$9.3 million for deferred tax assets relating to business interest carryforwards.

Liquidity and Capital Resources

Sources of Liquidity

During the nine months ended September 30, 2022, we met our cash and liquidity needs primarily through cash on hand, cash generated by our operations and borrowings under our Credit Facility. Over the next twelve months, and in the longer term, we expect that our cash and liquidity needs will be met by cash generated by our operations and borrowings under our Credit Facility, especially for acquisition activities. If our acquisition activity continues at an accelerated pace, or for larger acquisition opportunities, we may decide to issue equity either as consideration or, if market conditions are favorable, in an offering. For information regarding the Credit Facility, please read “—Credit Facilities.”

Tax Receivable Agreements

Our Tax Receivable Agreements with the TRA holders generally provide for the payment by Focus Inc. to each TRA holder of 85% of the net cash savings, if any, in U.S. federal, state and local income and franchise tax that Focus Inc. actually realizes (computed using simplifying assumptions to address the impact of state and local taxes) or is deemed to realize in certain circumstances in periods after the initial public offering as a result of certain increases in tax basis and certain tax benefits attributable to imputed interest. Focus Inc. will retain the benefit of the remaining 15% of these cash savings.

The payment obligations under the Tax Receivable Agreements are Focus Inc.'s obligations and not obligations of Focus LLC, and we expect that such payments required to be made under the Tax Receivable Agreements will be substantial. Estimating the amount and timing of payments that may become due under the Tax Receivable Agreements is by its nature imprecise. For purposes of the Tax Receivable Agreements, cash savings in tax generally are calculated by comparing Focus Inc.'s actual tax liability (determined by using the actual applicable U.S. federal income tax rate and an assumed combined state and local income and franchise tax rate) to the amount Focus Inc. would have been required to pay had it not been able to utilize any of the tax benefits subject to the Tax Receivable Agreements. During the nine months ended September 30, 2022, payments totaling \$3.9 million were made under the Tax Receivable Agreements. As of September 30, 2022, we expect that future payments to the TRA holders that have already exchanged Focus LLC units will be \$221.2 million, in aggregate. Future payments under the Tax Receivable Agreements in respect of subsequent exchanges will be in addition to this amount.

The actual increases in tax basis, as well as the amount and timing of any payments under the Tax Receivable Agreements, will vary depending upon a number of factors, including the timing of any redemption of units, the price of our Class A common stock at the time of each redemption, the extent to which such redemptions are taxable transactions, the amount of Focus LLC's assets that consist of equity in entities taxed as corporations at the time of each redemption, the amount and timing of the taxable income we generate in the future, the U.S. federal income tax rates then applicable and the portion of the payments under the Tax Receivable Agreements that constitute imputed interest or give rise to depreciable or amortizable tax basis.

The foregoing amount of expected future payments to TRA holders is an estimate and the actual payments could differ materially. It is possible that future transactions or events could increase or decrease the actual tax benefits realized and the corresponding payments under the Tax Receivable Agreements as compared to the foregoing estimates. Moreover, there may be a negative impact on our liquidity if, as a result of timing discrepancies or otherwise, (i) the payments under the Tax Receivable Agreements exceed the actual benefits realized in respect of the tax attributes

[Table of Contents](#)

subject to the Tax Receivable Agreements and/or (ii) distributions to Focus Inc. by Focus LLC are not sufficient to permit Focus Inc. to make payments under the Tax Receivable Agreements after it has paid its taxes and other obligations.

The payments under the Tax Receivable Agreements will not be conditioned upon a TRA holder's having a continued ownership interest in either Focus Inc. or Focus LLC.

We expect that future unitholders may become party to one or more Tax Receivable Agreements entered into in connection with future acquisitions by Focus LLC or issuances of units of Focus LLC to employees, principals and directors.

Cash Flows

The following table presents information regarding our cash flows and cash and cash equivalents for the nine months ended September 30, 2021 and 2022:

	Nine Months Ended September 30,		\$ Change	% Change
	2021	2022		
Cash provided by (used in):				
Operating activities	\$ 237,848	\$ 230,316	\$ (7,532)	(3.2)%
Investing activities	(310,595)	(380,059)	(69,464)	(22.4)%
Financing activities	649,664	(29,889)	(679,553)	(104.6)%
Cash and cash equivalents—end of period	642,207	128,528	(513,679)	(80.0)%

Operating Activities

Net cash provided by operating activities includes net income adjusted for non-cash expenses such as intangible amortization, depreciation and other amortization, amortization of debt financing costs, non-cash equity compensation expense, non-cash changes in fair value of estimated contingent consideration, other non-cash items and changes in cash resulting from changes in operating assets and liabilities. Operating assets and liabilities include receivables from our clients, prepaid expenses and other assets, accounts payable and accrued expenses, deferred revenues and other assets and liabilities.

Net cash provided by operating activities decreased \$7.5 million, or 3.2%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. The decrease was principally related to changes in working capital including the timing of due to affiliate payments and an increase in interest payments, which were partially offset by an increase in Adjusted EBITDA of \$78.5 million during the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021.

Investing Activities

Net cash used in investing activities increased \$69.4 million, or 22.4%, for the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021. The increase was due primarily to an increase in cash paid for acquisitions and contingent consideration of \$74.9 million offset in part by a decrease in investment and other, net of \$12.0 million during the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021.

Financing Activities

Net cash provided by financing activities for the nine months ended September 30, 2022 decreased \$679.6 million, or 104.6%, compared to the nine months ended September 30, 2021. The decrease was primarily due to a

[Table of Contents](#)

decrease in net borrowings under our Credit Facility of \$718.9 million offset in part by a decrease in contingent consideration paid of \$31.8 million during the nine months ended September 30, 2022 compared to the nine months ended September 30, 2021.

Adjusted Free Cash Flow

To supplement our statements of cash flows presented on a GAAP basis, we use a non-GAAP liquidity measure on a trailing 4-quarter basis to analyze cash flows generated from our operations. We consider Adjusted Free Cash Flow to be a liquidity measure that provides useful information to investors about the amount of cash generated by the business and is one factor in evaluating the amount of cash available to pay contingent consideration and deferred acquisition consideration, make strategic acquisitions and repay outstanding borrowings. Adjusted Free Cash Flow does not represent our residual cash flow available for discretionary expenditures as it does not deduct our mandatory debt service requirements and other non-discretionary expenditures. We define Adjusted Free Cash Flow as net cash provided by operating activities, less purchase of fixed assets, distributions for Focus LLC unitholders and payments under Tax Receivable Agreements (if any). Adjusted Free Cash Flow is not defined under GAAP and should not be considered as an alternative to net cash from operating, investing or financing activities. Adjusted free cash flow may not be calculated the same for us as for other companies. The table below reconciles net cash provided by operating activities, as reflected on our cash flow statement, to our adjusted free cash flow.

	Trailing 4-Quarters Ended September 30,	
	2021	2022
	(in thousands)	
Net cash provided by operating activities (1)(2)	\$ 310,742	\$ 306,386
Purchase of fixed assets	(13,218)	(17,610)
Distributions for unitholders	(33,083)	(26,439)
Payments under tax receivable agreements	(4,423)	(3,856)
Adjusted Free Cash Flow	\$ 260,018	\$ 258,481

- (1) A portion of contingent consideration paid is classified as operating cash outflows in accordance with GAAP, with the balance reflected in investing and financing cash flows. Contingent consideration paid classified as operating cash outflows for each quarter in the trailing 4-quarters ended September 30, 2021 was \$2.4 million, \$5.3 million, \$11.6 million and \$20.4 million, respectively, totaling \$39.7 million for the trailing 4-quarters ended September 30, 2021. Contingent consideration paid classified as operating cash outflows for each quarter in the trailing 4-quarters ended September 30, 2022 was \$16.4 million, \$23.1 million, \$18.2 million and \$29.6 million, respectively, totaling \$87.3 million for the trailing 4-quarters ended September 30, 2022. See Note 6 to our unaudited condensed consolidated financial statements for additional information.
- (2) A portion of deferred acquisition consideration paid is classified as operating cash outflows in accordance with GAAP, with the balance reflected in financing cash outflows. Deferred acquisition consideration paid classified as operating cash outflows was \$16.0 thousand for the three months ended September 30, 2022.

Credit Facilities

As of September 30, 2022, our credit facility (the "Credit Facility") consisted of a \$2.4 billion first lien term loan (the "First Lien Term Loan"), consisting of a tranche A ("Tranche A") and tranche B ("Tranche B"), and a \$650.0 million first lien revolving credit facility (the "First Lien Revolver").

Tranche A bears interest (at our option) at: (i) the London Interbank Offering Rate ("LIBOR") plus a margin of 2.00% or (ii) the lender's Base Rate (as defined in the Credit Facility) plus a margin of 1.00%. Tranche A requires quarterly installment repayments of \$4.2 million and has a maturity date of July 2024.

[Table of Contents](#)

Tranche B bears interest (at our option) at: (i) LIBOR plus a margin of 2.50% with a 0.50% LIBOR floor or (ii) the lender's Base Rate plus a margin of 1.50%. Tranche B requires quarterly installment repayments of \$2.0 million and has a maturity date of June 2028.

In April 2022, we amended the First Lien Revolver to extend the maturity date to June 2024 and change the benchmark interest rate from LIBOR to the Secured Overnight Financing Rate ("SOFR"). As amended, the First Lien Revolver bears interest (at our option) at SOFR, including a credit adjustment spread, plus a margin of 2.00% with step downs to 1.75%, 1.50% and 1.25% or the lender's Base Rate plus a margin of 1.00% with step downs to 0.75%, 0.50% and 0.25%, based on achievement of a specified First Lien Leverage Ratio. The First Lien Revolver unused commitment fee is 0.50% with step downs to 0.375% and 0.25% based on achievement of a specified First Lien Leverage Ratio. Up to \$30.0 million of the First Lien Revolver is available for the issuance of letters of credit, subject to certain limitations.

Our obligations under the Credit Facility are collateralized by the majority of our assets. The Credit Facility contains various customary covenants, including, but not limited to: (i) incurring additional indebtedness or guarantees, (ii) creating liens or other encumbrances on property or granting negative pledges, (iii) entering into a merger or similar transaction, (iv) selling or transferring certain property and (v) declaring dividends or making other restricted payments.

We are required to maintain a First Lien Leverage Ratio (as defined in the Credit Facility) of not more than 6.25:1.00 as of the last day of each fiscal quarter. At September 30, 2022, our First Lien Leverage Ratio was 3.98:1.00, which satisfied the maximum ratio of 6.25:1.00. First Lien Leverage Ratio means the ratio of amounts outstanding under the First Lien Term Loan and First Lien Revolver plus other outstanding debt obligations secured by a lien on the assets of Focus LLC (excluding letters of credit other than unpaid drawings thereunder) minus unrestricted cash and cash equivalents to Consolidated EBITDA (as defined in the Credit Facility). Consolidated EBITDA for purposes of the Credit Facility was \$579.9 million at September 30, 2022. Focus LLC is also subject on an annual basis to contingent principal payments based on an excess cash flow calculation (as defined in the Credit Facility) for any fiscal year if the First Lien Leverage Ratio exceeds 3.75:1.00. No contingent principal payments were required to be made in 2021. Based on the excess cash flow calculation for the year ended December 31, 2021, no contingent principal payments are required to be made in 2022.

We defer and amortize our debt financing costs over the respective terms and tranches of the First Lien Term Loan and First Lien Revolver. The debt financing costs related to the First Lien Term Loan are recorded as a reduction of the carrying amount of the First Lien Term Loan in the unaudited condensed consolidated balance sheets. The debt financing costs related to the First Lien Revolver are recorded in debt financing costs-net in the unaudited condensed consolidated balance sheets.

At September 30, 2022, outstanding stated value borrowings under the First Lien Term Loan and First Lien Revolver were approximately \$2.4 billion. The weighted-average interest rate for outstanding borrowings was approximately 3% for the nine months ended September 30, 2022. As of September 30, 2022, the First Lien Revolver available unused commitment line was \$590.1 million. At September 30, 2022, we had outstanding letters of credit in the amount of \$9.9 million bearing interest at an annual rate of approximately 2%.

In March 2020, we entered into a 4 year floating to fixed interest rate swap with a notional amount of \$400.0 million. The interest rate swap effectively fixes the variable interest rate applicable to \$400.0 million of borrowings outstanding on the First Lien Term Loan. The terms of the interest rate swap provide that we pay interest to the counterparty each month at a rate of 0.713% and receive interest from the counterparty each month at the 1 month USD LIBOR rate, subject to a 0% floor.

In April 2020, we entered into two 4 year floating to fixed interest rate swap agreements with notional amounts of \$250.0 million and \$200.0 million. These swaps effectively fix the variable interest rate applicable to associated amount of borrowings outstanding on the First Lien Term Loan. The terms of these swaps provide that we pay interest to the counterparty each month at a rate of 0.537% and 0.5315%, respectively, and receive interest from the counterparty each month at the 1 month USD LIBOR rate, subject to a 0% floor.

[Table of Contents](#)

The interest rate swaps effectively fix the variable interest rate applicable to \$850.0 million or approximately 36% of the First Lien Term Loan borrowings outstanding, resulting in a weighted average interest rate on these borrowings of approximately 0.62% plus a margin of 2%.

Our First Lien Term Loan uses LIBOR as a benchmark for establishing the interest rate. 1-, 3-, 6- and 12-month LIBOR are expected to be replaced by SOFR in 2023. We expect SOFR to be a reasonable replacement for LIBOR and do not expect any material impact on the interest rates we pay.

Critical Accounting Policies

As of September 30, 2022, there have been no significant changes to our critical accounting policies previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2021.

Recent Accounting Pronouncements

The effects of new accounting pronouncements are discussed in the notes to our unaudited condensed consolidated financial statements included elsewhere in this Quarterly Report on Form 10-Q.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market Risk

Our exposure to market risk is primarily related to our partner firms' wealth management services. For the nine months ended September 30, 2022, over 95% of our revenues were fee-based and recurring in nature. Although the substantial majority of our revenues are fee-based and recurring, our revenues can fluctuate due to macroeconomic factors and the overall state of the financial markets, particularly in the United States. The substantial majority of our revenues are derived from the wealth management fees charged by our partner firms for providing clients with investment advice, financial and tax planning, consulting, tax return preparation, family office services and other services. The majority of our wealth management fees are based on the value of the client assets and we expect those fees to increase over time as the assets increase. A decrease in the aggregate value of client assets across our partner firms may cause our revenue and income to decline.

Interest Rate Risk

Interest payable on our Credit Facility is variable. Interest rate changes will therefore affect the amount of our interest payments, future earnings and cash flows. We entered into interest rate swap agreements in March and April 2020 to manage interest rate exposure in connection with our variable interest rate borrowings. As of September 30, 2022, we had total stated value borrowings outstanding under our First Lien Term Loan and First Lien Revolver of approximately \$2.4 billion. At September 30, 2022, interest payments associated with \$850.0 million of these borrowings was effectively converted to a fixed rate through the use of interest rate swaps and interest on the remaining borrowings under our First Lien Term Loan and First Lien Revolver remained subject to variable rates based on LIBOR and SOFR, respectively. If LIBOR and SOFR in effect were each 1.0% higher throughout the nine months ended September 30, 2022, our interest expense would have increased by approximately \$11.4 million.

Our First Lien Term Loan uses LIBOR as a benchmark for establishing the interest rate. 1-, 3-, 6- and 12-month LIBOR are expected to be replaced by SOFR in 2023. We expect SOFR to be a reasonable replacement for LIBOR and do not expect any material impact on the interest rates we pay.

Item 4. Controls and Procedures

Our management, with the participation of our principal executive officer and principal financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of September 30, 2022. Our disclosure controls and procedures are designed to provide reasonable assurance that

[Table of Contents](#)

information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that such information is accumulated and communicated to management, including the principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure. Based on such evaluation, our principal executive officer and principal financial officer concluded that, as of September 30, 2022, our disclosure controls and procedures were effective, at the reasonable assurance level. Any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving the desired control objective, and management necessarily applies its judgment in evaluating the cost-benefit relationship of all possible controls and procedures.

There were no changes in our internal control over financial reporting during the quarter ended September 30, 2022 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II: OTHER INFORMATION

Item 1. Legal Proceedings

We are, from time to time, involved in various legal claims and regulatory matters arising out of our operations in the normal course of business. A partner firm has settled most of the investor demands related to a private fund (that held approximately \$27 million in client assets) during the year ended December 31, 2021. We have notified our insurance carriers of the matter. After consultation with legal counsel, we do not believe that the resolutions of any matters we are currently involved in, individually or in the aggregate, will have a material adverse impact on our financial condition, results of operations or cash flows. However, we can provide no assurance that any pending or future matters will not have a material effect on our financial condition, results of operations or cash flows in future reporting periods.

From time to time, we and our partner firms receive requests for information from governmental authorities. For example, in 2021, we received an inquiry from the SEC asking us to provide materials principally related to policies, procedures and communications concerning Adjusted Net Income, a non-GAAP financial measure, which was disaggregated in the third quarter of 2020 to separate certain tax adjustments in response to earlier comments from the SEC. We are cooperating with this inquiry and intend to continue to cooperate with all governmental authorities. While we are unable to determine the ultimate outcome of any matter, we believe that the resolution of all current governmental inquiries will not have a material impact on our financial condition, results of operations or cash flows.

Item 1A. Risk Factors

In addition to the other information set forth in this report, readers should carefully consider the risks under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2021. Except as set forth below, there has been no material change in our risk factors from those described in our Annual Report on Form 10-K for the year ended December 31, 2021. These risks, as updated below, are not the only risks that we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial may materially adversely affect our business, financial condition or results of operations.

The ongoing conflict in Ukraine has, and will likely continue to, negatively impact the global economy and may have a material adverse effect on our business, operations and financial results.

The military conflict in Ukraine and the ongoing geopolitical tensions have created significant volatility, uncertainty and economic disruption. The United States, European Union and other countries have announced economic sanctions against Russia. While it has not had a material adverse effect on our business, operations and financial results, the extent to which the conflict impacts our business, operations and financial results going forward will depend on numerous evolving factors that we may not be able to accurately predict, including: the duration and scope of the conflict; governmental and business actions that have been and continue to be taken in response to the conflict, the impact of the conflict on economic activity and any retaliatory actions taken by Russia.

[Table of Contents](#)

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

In August 2022, we issued an aggregate of 396,731 shares of Class A common stock and retired 381,573 shares of Class B common stock and 36,357 incentive units in Focus LLC, and acquired 396,731 common units in Focus LLC, in each case as part of the regular quarterly exchanges offered to holders of units in Focus LLC.

The issuance of such securities was made in reliance upon an exemption from the registration requirements of the Securities Act of 1933, as amended, pursuant to Section 4(a)(2) thereof.

Each Focus LLC common unit, together with a corresponding share of our Class B common stock, and Focus LLC incentive unit (after conversion into a number of common units taking into account the then-current value of the common units and such incentive unit's aggregate hurdle amount) is exchangeable, pursuant to the terms and subject to the conditions set forth in the Operating Agreement, for one share of our Class A common stock, or, if either we or Focus LLC so elects, cash.

Item 6. Exhibits

Exhibit Number	Description
3.1	Amended and Restated Certificate of Incorporation of Focus Financial Partners Inc.(1)
3.2	Amended and Restated Bylaws of Focus Financial Partners Inc.(1)
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS*	Inline XBRL Instance Document
101.SCH*	Inline XBRL Taxonomy Extension Schema Document
101.CAL*	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB*	Inline XBRL Taxonomy Extension Label Linkbase Document
101.PRE*	Inline XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF*	Inline XBRL Taxonomy Extension Definition Linkbase Document
104*	Cover Page Interactive Data File - the cover page iXBRL tags are embedded within the inline XBRL document.

* Filed or furnished herewith.

(1) Incorporated by reference to the Registrant's Current Report on Form 8-K (File No. 001-38604) filed with the SEC on July 31, 2018.

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Ruediger Adolf, certify that:

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

/s/ RUEDIGER ADOLF

Ruediger Adolf

Chairman and Chief Executive Officer

Date: November 3, 2022

CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, James Shanahan, certify that:

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

/s/ JAMES SHANAHAN

James Shanahan
Chief Financial Officer

Date: November 3, 2022

**CERTIFICATION OF
CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
UNDER SECTION 906 OF THE
SARBANES OXLEY ACT OF 2002, 18 U.S.C. § 1350**

In connection with the Quarterly Report on Form 10-Q of Focus Financial Partners Inc. (the "Company"), as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Ruediger Adolf, Chief Executive Officer of the Company, and James Shanahan, Chief Financial Officer of the Company, each certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to his knowledge:

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

/s/ RUEDIGER ADOLF

Ruediger Adolf
Chairman and Chief Executive Officer

/s/ JAMES SHANAHAN

James Shanahan
Chief Financial Officer

Date: November 3, 2022

Date: November 3, 2022
