



Robert W. Baird & Co. Incorporated

**Unaudited Consolidated Statement of Financial Condition
As of June 30, 2016**

Robert W. Baird & Co. Incorporated

Consolidated Statement of Financial Condition
As of June 30, 2016

(In Thousands)

<u>Assets</u>	
Cash and Cash Equivalents	\$ 159,614
Cash Segregated Under Federal Regulations	25,000
Cash Held by Baird Private Equity Partnerships	10,234
Securities Purchased Under Agreements to Resell	332,121
Deposits with Clearing Corporations	56,670
Receivables:	
Clients, Net	230,408
Brokers and Dealers	49,429
Deposits Paid on Securities Borrowed	277,935
Notes Receivable, Net	110,152
Other	126,918
	<u>794,842</u>
Securities Owned, at Fair Value	735,203
Securities Owned by Baird Private Equity Partnerships, at Fair Value	407,558
Furniture, Equipment, Leasehold Improvements and Capital Leases at Cost, Less Accumulated Depreciation and Amortization of \$117,034	71,493
Goodwill	89,229
Intangible Assets, at Cost, Less Accumulated Amortization of \$13,665	18,425
Net Deferred Tax Assets	24,950
Other Assets	<u>50,893</u>
Total Assets	<u><u>\$ 2,776,232</u></u>

The accompanying notes are an integral part of this financial statement.

Robert W. Baird & Co. Incorporated

Consolidated Statement of Financial Condition
As of June 30, 2016

(In Thousands)

(Continued)

Liabilities and Stockholder's Equity

Liabilities:

Money Borrowed:

Book Credit Balances in Bank Accounts \$ 26,024

Securities Sold Under Agreements to Repurchase 683,969

Payables:

Clients 180,559

Brokers and Dealers 52,287

Deposits Received on Securities Loaned 18,402

251,248

Securities Sold, Not Yet Purchased, at Fair Value 281,432

Accounts Payable, Accrued Expenses and Other Liabilities 313,914

Subordinated Liabilities 226,187

Total Liabilities 1,782,774

Stockholder's Equity:

Common Stock 26,502

Additional Paid-In Capital 196,184

Retained Earnings 377,971

Treasury Stock, at Cost (1,486)

Accumulated Other Comprehensive Income (194)

Total Robert W. Baird & Co. Incorporated Stockholder's Equity 598,977

Noncontrolling Interests in Baird Private Equity Partnerships 394,481

Total Stockholder's Equity 993,458

Total Liabilities and Stockholder's Equity \$ 2,776,232

The accompanying notes are an integral part of this financial statement.

Robert W. Baird & Co. Incorporated

Notes to Consolidated Statement of Financial Condition
June 30, 2016

(In Thousands, Except Share and Per Share Amounts)

(1) Organization and Description of Business

The Consolidated Statement of Financial Condition includes Robert W. Baird & Co. Incorporated (“RWB”), Baird Insurance Services, Inc. and RWB’s consolidated private equity partnerships as more fully discussed in Footnote 14 (together, the “Company”). The Company is registered as a securities broker dealer and an investment adviser with the Securities and Exchange Commission (“SEC”) under the Securities and Exchange Act of 1934 and the Investment Advisers Act of 1940, and is also a member of the Financial Industry Regulatory Authority (“FINRA”) and various securities exchanges. The Company engages in a broad range of activities in the private wealth management, equity and fixed income capital markets, asset management and private equity businesses, including securities brokerage; investment advisory and asset management services; institutional equity and fixed income sales; research services; origination of and participation in underwritings and distribution of corporate and municipal securities issuances; municipal advisory services; merger and acquisition advisory services; private equity and venture capital investing; and market making and trading activities in equity, municipal and other fixed income securities. The Company is a wholly-owned subsidiary of Baird Financial Corporation (“BFC”), which is a wholly-owned subsidiary of Baird Holding Company (“BHC”), which is a wholly-owned subsidiary of Baird Financial Group, Inc. (“BFG” or the “Parent”).

The Company owns a 48% ownership interest in Baird UK Ltd. (“Baird UK”), located principally in London, England. Baird UK is the parent company of Robert W. Baird Group Limited, located in London, which provides investment banking, private equity and institutional U.S. equity services. Robert W. Baird Group Limited conducts its business through three principal operating subsidiaries: Robert W. Baird Limited, based in London and regulated by the Financial Conduct Authority (“FCA”), which is engaged in transatlantic mergers and acquisitions advisory services and institutional U.S. equity sales; Robert W. Baird GmbH, based in Frankfurt, Germany which is engaged in transatlantic mergers and acquisitions advisory services; and Baird Capital Partners Europe Limited, based in London and regulated by the FCA, which is engaged in private equity activities in the United Kingdom.

On January 15, 2016, BFC completed the acquisition of all of the outstanding equity interests of Chautauqua Capital Management, LLC (“CCM”), an international equity manager located in Boulder, CO, which was immediately merged into RWB. Refer to Footnote 6 for further information on the impact of this acquisition on the Consolidated Statement of Financial Condition.

(2) Summary of Significant Accounting Policies

The following is a summary of the significant accounting policies followed by the Company in the preparation of its Consolidated Statement of Financial Condition:

(a) Estimates

The preparation of the Consolidated Statement of Financial Condition in conformity with accounting principles generally accepted in the United States of America (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 Consolidated Statement of Financial Condition. Actual results may differ from those estimates.

(b) Cash and Cash Equivalents

Cash equivalents are defined as short-term investments with maturities of generally three months or less at the time of purchase.

(c) Cash Segregated Under Federal Regulations

Cash segregated under federal regulations represents cash segregated in a special reserve bank account for the benefit of U.S. customers under SEC Rule 15c3-3.

(d) Cash Held by Baird Private Equity Partnerships

Cash Held by Baird Private Equity Partnerships represents cash and cash equivalents held by consolidated private equity partnerships. Such amounts are not available to fund the general liquidity needs of RWB.

(e) Securities Purchased Under Agreements to Resell and Securities Sold Under Agreements to Repurchase

The Company enters into short-term securities purchased under agreements to resell (“reverse repurchase agreements”) and short-term securities sold under agreements to repurchase (“repurchase agreements”). Both reverse repurchase and repurchase agreements are accounted for as collateralized financings and are carried at contractual amounts. Interest receivable and interest payable is included within Receivables Other and Accounts Payable, Accrued Expenses and Other Liabilities, respectively, on the Consolidated Statement of Financial Condition. Amounts are recorded when earned or due. It is the Company’s policy to obtain possession of collateral with a market value equal to or in excess of the principal amount loaned under the reverse repurchase agreements. To ensure the market value of the underlying collateral remains sufficient, the collateral is valued daily, and the Company may require counterparties to deposit additional collateral (or may return collateral to counterparties) when necessary. Reverse repurchase and repurchase agreements with the same counterparty are reported on a gross basis on the Consolidated Statement of Financial Condition. Refer to Footnote 17 for additional information on collateralized transactions.

(f) Receivables and Payables

Clients, Net - receivables include amounts receivable on cash and margin transactions, including from officers and directors and certain other affiliates of the Company, which are generally collateralized by securities owned by clients. When a receivable is considered to be impaired, the amount of impairment is generally measured based on the fair value of the securities acting as collateral, which is measured based on current prices from independent sources such as listed market prices or broker-dealer price quotations. Payables include amounts owed to clients on cash and margin transactions.

Brokers and Dealers – include amounts receivable and payable to clearing organizations, and receivable and payable to other brokers and dealers for securities failed-to-deliver or receive and trade date commissions not yet settled.

Deposits Paid on Securities Borrowed and Deposits Received on Securities Loaned - reported as collateral financings and are recorded at the amount of cash collateral advanced or received. Securities borrowed transactions require the Company to deposit cash, letters of credit or other collateral with the lender. With respect to securities loaned, the Company receives collateral in the form of cash in an amount in excess of the market value of securities loaned. The Company monitors the market value of securities borrowed and loaned on a daily basis. Additional collateral is obtained or refunded as necessary. Securities borrowed or securities loaned transactions with the same counterparty are reported on a gross basis on the Consolidated Statement of Financial Condition. Refer to Footnote 17 for additional information on collateralized transactions.

Notes Receivable, Net – are loans or pay advances to associates primarily for recruiting purposes. These associate advances are generally forgiven over a three to nine year period. In determining the allowance for doubtful accounts related to those advances, management considers a number of factors including amounts due from associates, the number of terminated associates, as well as the Company’s historical loss experience. This involves the use of estimates and the actual amounts may be substantially higher or lower than the recorded amounts.

Refer to Footnote 4 for further information on receivables and payables.

(g) Fair Value Measurements

The Company follows Accounting Standards Codification (“ASC”) 820, “Fair Value Measurements.” ASC 820 defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the inputs used to measure fair value and enhances disclosure requirements for fair value measurements. ASC 820 prescribes the methodology of observable inputs by requiring that the observable inputs be used when available.

Observable inputs are inputs that market participants would use in pricing the asset or liability based on market data obtained from independent sources. Unobservable inputs reflect assumptions that market participants would use in pricing the asset or liability based on the best information available in the circumstances. The hierarchy, as defined by ASC 820, is broken down into three levels based on the transparency of inputs as follows:

Level I - Quoted prices are available in active markets for identical assets or liabilities as of the report date. A quoted price for an identical asset or liability in an active market provides the most reliable fair value measurement because it is directly observable to the market.

Level II - Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the report date. The nature of these securities include investments for which quoted prices are available but traded less frequently and investments that are fair valued using other securities, the parameters of which can be directly observed.

Level III - Securities that have little to no pricing observability as of the report date. These securities are measured using management’s best estimate of fair value, where the inputs into the determination of fair value are not observable and require significant management judgment or estimation.

The fair value of securities owned is the amount at which the security could be exchanged in an orderly transaction between market participants at the measurement date. Based on the nature of the Company’s business and its role as a dealer in the securities industry, the fair values of its securities are determined internally. When available, the Company values securities at observable market prices, observable market parameters, or broker or dealer prices (bid and ask prices). In the case of securities transacted on recognized exchanges, the observable market prices represent quotations for completed transactions from the exchange on which the securities are principally traded.

The Company's securities owned and securities sold, not yet purchased are based on observable market prices, observable market parameters, or derived from broker or dealer prices. The availability of observable market prices and pricing parameters can vary from product to product. Where available, observable market prices and pricing, or market parameters in a product may be used to derive a price without requiring significant judgment. In certain markets, observable market prices or market parameters are not available for all products, and fair value is determined using techniques appropriate for each particular product. These techniques involve some degree of judgment.

For investments in illiquid or privately held securities that do not have readily determinable fair values, the determination of fair value requires the Company to estimate the value of the securities using the best information available. Among the factors considered by the Company in determining the fair value of such securities are the cost, terms and liquidity of the investment, the financial condition and operating results of the issuer, the quoted market price of publicly traded securities with similar quality and yield, and other factors generally pertinent to the valuation of the investments. In addition, even where the Company derives the value of a security based on information from an independent source, certain assumptions may be required to determine the security's fair value.

Investments in corporate stocks are included within other securities and are primarily publicly traded with observable prices in active markets. These investments are included within Level I in the fair value hierarchy. Any corporate stock not actively traded is valued by the Company and included within Level II or Level III depending on the nature and observability of the inputs used in the valuation. Investments in U.S government and agency obligations, municipal bonds, corporate bonds, collateralized mortgage obligations and auction rate securities, which include securities backed by pools of student loans, securities issued by municipalities, and auction rate preferred securities issued by closed end mutual funds, are generally valued using quoted prices from external data providers and market participants and included within Level II of the fair value hierarchy. Valuation information provided by external data providers and market participants generally includes a derived fair value utilizing a model where inputs to the model are directly observed by the market, or can be derived principally from or corroborated by observable market data, or fair value using other financial instruments, the parameters of which can be directly observed. For certain investments where there is limited activity or less transparency around significant inputs, the investments are valued as determined by the Company utilizing available market information and included within Level III of the fair value hierarchy.

The Company makes investments in certain private companies which are included within other securities and generally fair valued by management. In the absence of readily ascertainable market values, these investments may be valued using the market approach or the income approach, or a combination thereof. Under the market approach, fair value may be determined by reference to multiples of market-comparable companies or transactions, including earnings before interest, taxes, depreciation and amortization ("EBITDA") multiples. Under the income approach fair value may be determined by discounting the cash flows to a single present amount using current market expectations about those future amounts. These valuation techniques require inputs that are both significant to the fair value and unobservable, and thus are included within Level III of the fair value hierarchy.

Securities Owned by Baird Private Equity Partnerships include investments in private companies, which are consolidated as the Company has a controlling interest in a limited liability company which is the general partner and determined to be the primary beneficiary of a variable interest entity ("VIE"). In the absence of readily ascertainable market values, these investments may be valued using the market approach or the income approach, or a combination thereof, as described above. These investments are generally included within Level II or Level III of the fair value hierarchy, depending on the availability of the significant inputs into the valuation.

The Company employs specific control processes to determine the reasonableness of the fair value of its securities owned and securities sold, not yet purchased. The Company's processes are designed to ensure that the internally estimated fair values are accurately recorded and that the data inputs and the valuation techniques used are appropriate, consistently applied, and that the assumptions are reasonable and consistent with the objective of determining fair value. Individuals outside of the trading departments perform independent pricing verification reviews. The Company has established parameters which set forth when securities are independently verified. The selection parameters are generally based on the type of security, the level of estimation of risk of a security, the materiality of the security, the age of the security in the Company's securities portfolio, and other specific facts and circumstances of the Company's securities portfolio.

Cash and cash equivalents, cash segregated under federal regulations, cash held by Baird Private Equity partnerships, deposits with clearing corporations and receivables are financial assets with carrying values that approximate fair value due to their relatively short-term nature. Money borrowed, payables, accounts payable, accrued expenses and other liabilities are financial liabilities with carrying values that approximate fair value due to their relatively short-term nature. The carrying amount of subordinated liabilities approximates fair value based on current market conditions and interest rates available to the Company for similar financial instruments. Securities either purchased or sold under agreements to resell or repurchase are carried at contractual amounts.

Refer to Footnote 8 for further information.

(h) Income Taxes

Certain income and expense items are accounted for in different periods for financial reporting purposes than for income tax purposes. Appropriate provisions are made in the Company's Consolidated Statement of Financial Condition for deferred income taxes in recognition of these temporary differences as more fully disclosed in Footnote 11.

(i) Furniture, Equipment, Leasehold Improvements, and Capital Leases

Furniture, equipment, leasehold improvements, and capital leases are stated at cost less accumulated depreciation. Depreciation is provided by using the straight-line method over the estimated useful lives of the assets, which range from three years for software and computer equipment to ten years for certain leasehold improvements.

Additions, improvements and expenditures for repairs and maintenance that significantly extend the useful life of an asset are capitalized, as more fully disclosed in Footnote 5. Other expenditures for repairs and maintenance are charged to expense in the period incurred.

(j) Goodwill and Intangible Assets

Goodwill and intangible assets with indefinite lives are not amortized but are reviewed at least annually for impairment. The Company has the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more-likely-than-not that the fair value of a reporting unit is less than the carrying amount. If the Company determines it is more-likely-than-not that the fair value of a reporting unit is greater than the carrying amount it would not be required to perform the two-step impairment test for that reporting unit. As of June 30, 2016, the Company determined it was more-likely-than-not that the reporting units' fair value was greater than the carrying value as it relates to goodwill and intangible assets and therefore no impairment was identified. Intangibles with finite lives are amortized on a straight-line basis over their respective lives as more fully disclosed in Footnote 6.

(k) Foreign Currency Translation

The Company's investment in Baird UK, disclosed in Footnote 15, is translated at the current exchange rate. Net exchange gains or losses resulting from the translation of the Baird UK investment are credited or charged directly to Accumulated Other Comprehensive Income, a separate component of Stockholders' Equity. These gains or losses are the only component of Accumulated Other Comprehensive Income.

(l) Commitments and Contingencies

The Company regularly enters into office space and other equipment lease arrangements, some of which are non-cancelable for the term of the lease. In addition, the Company is occasionally involved in legal and regulatory proceedings, arbitrations, underwriting commitments, private equity capital commitments and various other contingent obligations as more fully disclosed in Footnote 16.

(m) Consolidation

The Consolidated Statement of Financial Condition includes the accounts of those entities in which RWB has a controlling financial interest or is the primary beneficiary of a VIE. In determining which entities are required to be consolidated, the Company first evaluates whether each entity is a voting interest entity or VIE.

Voting interest entities are entities that have (i) total equity investment at risk sufficient to fund expected future operations independently, and (ii) equity holders that have the obligation to absorb losses or receive residual returns and the right to make decisions about the entity's activities. The Company consolidates voting interest entities when it has a controlling financial interest, which is generally ownership of a majority of the voting interest.

VIEs are entities that lack one or more of the characteristics of a voting interest entity. The Company consolidates VIEs when it is determined to be the primary beneficiary. The primary beneficiary is the entity that has (i) the power to direct activities that most significantly impact the economic performance of the VIE, and (ii) the obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE.

In determining if the Company is the primary beneficiary of a VIE both qualitative and quantitative analysis is performed including, analysis of the VIE control structure, including rights of other interest holders, expected benefits and losses and residual returns, contractual terms, ownerships interests and design of the VIE.

During the year, the Company adopted ASU 2015-02, *Consolidation (Topic 810) – Amendments to the Consolidation Analysis*, which provided updated guidance on evaluating limited partnerships and similar entities for consolidation under the VIE model. Prior to adoption, limited partnerships that did not contain substantive kick-out or participation rights for limited partners were considered voting interest entities and consolidated by the general partner, which was presumed to control the partnership if it had substantive equity at risk. The ASU changed the evaluation of limited partnerships such that when limited partners do not have substantive kick-out or participation rights, the limited partnership is considered a VIE, and consolidated by the primary beneficiary. Generally, the Baird private equity partnerships do not contain substantive kick-out or participation rights for the limited partners and therefore the adoption of this ASU had a material impact on the Company's Statement of Financial Condition, resulting in fewer partnerships requiring consolidation as of June 30, 2016.

Refer to Footnote 14 for further information on certain private equity partnerships the Company has consolidated as of June 30, 2016.

All material intercompany accounts and transactions have been eliminated in consolidation.

(n) Noncontrolling Interests in Baird Private Equity Partnerships

Noncontrolling Interests in Baird Private Equity Partnerships represent the component of partnership capital in consolidated entities held by third party investors.

(o) Legal Liabilities

The Company recognizes liabilities for contingencies when there is an exposure that, when analyzed, indicates it is both probable that a liability has been incurred, and the amount of loss can be reasonably estimated. Whether a loss is probable, and if so, the estimated range of possible loss is based on currently available information and is subject to significant judgment, a variety of assumptions, and uncertainties. When a range of possible loss can be estimated, the Company will accrue the most likely amount within that range. If the most likely amount of possible loss within that range is not determinable, the Company will accrue the minimum of the range of possible loss. No liability is recognized for those matters which, in management's judgment, the determination of a reasonable estimate of loss is not possible.

The Company records liabilities related to legal proceedings in Accounts Payable, Accrued Expenses, and Other Liabilities on the Consolidated Statement of Financial Condition. The determination of these liability amounts requires significant judgment on the part of management. Management considers many factors including, but not limited to: the amount of the claim; the amount of the loss in the client's account; the basis and validity of the claim; the possibility of wrongdoing by an associate; previous results in similar cases; and legal precedents and case law. Each legal proceeding is reviewed and the liability balance is adjusted as deemed appropriate by management. The actual costs of resolving legal proceedings may be substantially higher or lower than the recorded liability amounts for those matters.

Refer to Footnote 16 for further information.

(p) Upcoming Accounting Pronouncements

In February 2016, ASU 2016-02, *Leases* was issued, which requires lessees to recognize a right-of-use asset and a lease liability on the balance sheet for all leases with the exception of short-term leases. For lessees, leases will continue to be classified as either operating or finance leases in the income statement. New qualitative and quantitative disclosures are also required to provide information about amounts recorded in the financial statements. The standard is effective for annual and interim periods beginning after December 15, 2018. Early adoption is permitted. The standard must be adopted using a modified retrospective approach and requires application at the beginning of the earliest comparative period presented. The Company is currently evaluating the impact of the new standard on the Consolidated Statement of Financial Condition.

In June 2016, ASU 2016-13, *Financial Instruments – Credit Losses* was issued, which significantly changes how entities measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. The standard replaces the current “incurred loss” model for measuring credit losses with an “expected loss” model. The standard is effective for annual and interim periods beginning after December 15, 2020. Early adoption is permitted beginning with annual periods beginning after December 15, 2018. The standard must be adopted as a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the standard is effective. The Company is currently evaluating the impact of the new standard on the Consolidated Statement of Financial Condition.

(3) Related-Party Transactions

The Company serves as an investment advisor and provides administrative services to the Baird Funds, Inc. and various affiliated Baird private equity partnerships under management agreements (together, “Affiliated Funds”). Receivable from Affiliated Funds was \$13,708 at June 30, 2016 and is included within Receivables Other on the Consolidated Statement of Financial Condition.

The Company has invested \$23,253 into Affiliated Funds at June 30, 2016. Other amounts receivable from affiliates includes \$24,530 at June 30, 2016 which is included within Receivables Other on the Consolidated Statement of Financial Condition. Other amounts payable to affiliates includes \$1,557 at June 30, 2016 which is included within Accounts Payable, Accrued Expenses and Other Liabilities on the Consolidated Statement of Financial Condition.

Amounts receivable from associates, including the related allowance for doubtful accounts as of June 30, 2016 consists of the following:

Notes Receivable	\$ 117,347
Allowance for Doubtful Accounts	<u>(7,195)</u>
Notes Receivable, Net	<u><u>\$ 110,152</u></u>

(4) Receivables and Payables

Amounts receivable from brokers and dealers as of June 30, 2016 consists of the following:

Securities Failed-to-Deliver	\$ 43,848
Commissions Receivable	<u>5,581</u>
Receivables from Brokers and Dealers	<u><u>\$ 49,429</u></u>

Amounts payable to brokers and dealers as of June 30, 2016 consists entirely of securities failed-to-receive of \$52,287.

Securities failed-to-deliver and receive represent the contract value of securities that have not been delivered or received on settlement date.

(5) Furniture, Equipment, Leasehold Improvements, and Capital Leases

Furniture, Equipment, Leasehold Improvements, and Capital Leases as of June 30, 2016 consists of the following:

Furniture and Fixtures	\$	38,591
Equipment		44,914
Software		24,667
Leasehold Improvements		75,560
Capital Leases		4,795
Total Fixed Assets		<u>188,527</u>
Less:		
Accumulated Depreciation		(113,932)
Accumulated Amortization		(3,102)
Total Accumulated		<u>(117,034)</u>
Furniture, Equipment, Leasehold Improvements and Capital Leases, Net	\$	<u>71,493</u>

(6) Goodwill and Intangible Assets

Goodwill and Intangible Assets as of June 30, 2016 consists of the following:

	<u>Useful Life</u>		
Finite Life Intangibles			
Client lists	5 -14 Years	\$	21,544
Trademark	4 Years		603
Noncompete agreements	1-5 Years		310
Leasehold	6 Years		308
			<u>22,765</u>
Accumulated Amortization			
Client lists			(12,877)
Trademark			(377)
Noncompete agreements			(310)
Leasehold			(101)
			<u>(13,665)</u>
Net Finite Life Intangibles			9,100
Indefinite Life Intangibles			
Trade Names	N/A		9,325
Net Intangibles			<u>18,425</u>
Goodwill	N/A		89,229
			<u><u>\$ 107,654</u></u>

The CCM acquisition (described in Footnote 1) added \$3,160 to goodwill and \$1,770 to client list intangibles.

(7) Money Borrowed

(a) Bank Loans

At June 30, 2016, the Company had available a \$250,000 committed unsecured credit facility. The weighted average interest rate on the line of credit during the year was 1.94%. The line of credit expires on November 25, 2016. At June 30, 2016, there were no amounts outstanding on the available line of credit.

(b) Book Credit Balances in Bank Accounts

At June 30, 2016, the Company had \$26,024 in credit balances at certain banks with which it does business. The Company does not have a right of offset regarding these balances and, as a result, they are classified as Money Borrowed on the Consolidated Statement of Financial Condition.

(8) Fair Value of Financial Instruments

The following table summarizes the fair value of Financial Instruments as of June 30, 2016:

	Level I	Level II	Level III	Total
Cash Equivalents				
Money Market Funds	\$ 70,000	\$ -	\$ -	\$ 70,000
Securities Owned				
Certificates of Deposit	\$ -	\$ 3,964	\$ -	\$ 3,964
U.S. Government and Agency Obligations	-	153,449	-	153,449
Municipal Bonds	-	148,186	-	148,186
Private Label Mortgage Backed Securities	-	19,606	-	19,606
Other Asset Backed Securities	-	83,293	-	83,293
Corporate Obligations	-	248,459	-	248,459
Auction Rate Securities	-	-	344	344
Other Securities ⁽¹⁾	71,301	-	6,601	77,902
Total Securities Owned	\$ 71,301	\$ 656,957	\$ 6,945	\$ 735,203
Securities Owned by Baird Private Equity Partnerships ⁽²⁾	\$ -	\$ -	\$ 407,558	\$ 407,558
Securities Sold, Not Yet Purchased				
Certificates of Deposit	\$ -	\$ 3,787	\$ -	\$ 3,787
U.S. Government and Agency Obligations	-	76,493	-	76,493
Corporate Obligations	-	198,030	-	198,030
Other Securities ⁽¹⁾	3,122	-	-	3,122
Total Securities Sold, Not Yet Purchased	\$ 3,122	\$ 278,310	\$ -	\$ 281,432

⁽¹⁾ Other Securities in Level I consist principally of corporate stocks and mutual funds with observable prices in active markets. Other securities in Level III consist of certain private company investments.

⁽²⁾ The valuation of equity ownership in privately owned companies, the type of investment principally included in Securities Owned by Baird Private Equity Partnerships, requires significant management judgment due to the absence of quoted market prices, inherent lack of liquidity and long-term nature of these assets. As a result, these values cannot be determined with precision and the calculated fair value estimates may not be realizable in a current sale or immediate settlement of the instruments, and as such are included within Level III.

The following table summarizes the change in fair values of Level III assets during 2016:

	Auction Rate Securities	Other Securities	Securities Owned by Baird Private Equity Partnerships
Balance, January 1, 2016	\$ 411	\$ 6,070	\$ 495,629
Deconsolidation of Private Equity Partnerships ⁽¹⁾	-	-	(97,043)
Purchases	-	11	23,991
Sales / Pay-downs	-	(82)	(17,839)
Dividends Received	-	-	5,227
Realized Gains/(Losses)	-	-	1,915
Unrealized Gains/(Losses)	(67)	602	(4,322)
Balance, June 30, 2016	<u>\$ 344</u>	<u>\$ 6,601</u>	<u>\$ 407,558</u>
Change in Unrealized Gain/(Loss) on Securities Still Held as of June 30, 2016	<u>\$ (67)</u>	<u>\$ 602</u>	<u>\$ (4,322)</u>

⁽¹⁾ The Company adopted ASU 2015-02, *Consolidation – Amendments to the Consolidation Analysis*, as of January 1, 2016 which resulted in the deconsolidation of certain private equity partnerships as the Company was determined not to be the primary beneficiary. As of January 1, 2016 the value of the securities owned of these partnerships was deconsolidated.

The following table summarizes quantitative information related to the significant unobservable inputs utilized in the fair value measurements of the Level III assets as of June 30, 2016:

	Fair Value	Valuation Technique	Unobservable Input(s)	Range (Weighted Average)
Auction Rate Securities	\$ 344	Recent trades	Trades in inactive markets of in-portfolio securities	90% of par - 100% of par (95% of par)
Other Securities	\$ 6,601	Market comparable companies	EBITDA multiple	6.5 - 8.5 (6.7)
Securities Owned by Baird Private Equity Partnerships	\$ 407,558	Market comparable companies	EBITDA multiple	5.0 - 10.0 (7.6)
			Revenue multiple	1.1 - 2.0 (1.6)
			Multiples	1.0 - 11.1 (4.4)
		Discounted cash flow	Discount rate	13% - 16% (14.8%)
		Terminal multiple range	6.0 - 9.0 (7.6)	
		Precedent transactions	N/A	N/A

For auction rate securities the significant unobservable input used in the fair value measurement relates to judgments regarding whether the level of observable trading activity is sufficient to conclude the markets are active. Where insufficient levels of trading activity are determined to exist as of the reporting date, management's assessment of how much weight to apply to trading prices in inactive markets may vary, and significantly impact the fair value measurement of auction rate securities.

For other securities and securities owned by Baird Private Equity Partnerships, where the discounted cash flow method is used, a significant increase or decrease in the discount rate or terminal multiple range in isolation could result in a significantly lower or higher fair value measurement, respectively. Where the market comparable companies approach is used a significant increase or decrease in the EBITDA, revenue, or net income multiples in isolation could result in a significantly higher or lower fair value measurement, respectively.

(9) Net Capital Requirements

The Company is subject to the requirements of Rule 15c3-1 (the "net capital rule") under the Securities Exchange Act of 1934. The basic concept of the net capital rule is liquidity, its objective being to require a broker and dealer to maintain adequate net capital, as defined. The Company has elected to operate under the alternative net capital requirement as allowed by the net capital rule, which requires that net capital exceed 2% of aggregate debit items as those terms are defined. Withdrawal of equity capital may be restricted if net capital is less than 5% of such aggregate debit items.

As of June 30, 2016, the Company's net capital percentage was 91% of aggregate debit items, and net capital, as defined, was \$225,152, which was \$220,223 in excess of the required minimum amount. As of June 30, 2016 net capital after anticipated withdrawals as a percentage of aggregate debits was 83%.

(10) Subordinated Liabilities

As of June 30, 2016, the Company had \$226,187 of subordinated notes, including \$158,675 payable to BFC, and \$67,512 payable to associates, all of which are covered by agreements approved by FINRA that are available in computing adjusted net capital under the net capital rule.

The following schedule discloses the major components of subordinated debt including repayment terms:

Subordinated Note, variable interest rate (5.0%, plus 1 month LIBOR), due November 2018. Quarterly principal payments began in February 2015.	\$ 65,875
Subordinated Note, variable interest rate (7.5%, plus 3 month LIBOR), due November 2020. Quarterly principal payments begin in February 2018.	45,000
Subordinated Note, variable interest rate (5.0%, plus 1 month LIBOR), due June 2018.	30,000
Subordinated Note, variable interest rate (5.0%, plus 1 month LIBOR), due May 2019. Quarterly principal payments began in August 2015.	17,800
	<hr/>
	158,675
Payable to Associates	67,512
	<hr/>
	<u>\$ 226,187</u>

Subordinated Liabilities mature as follows as of December 31:

2016	\$ 21,442
2017	39,375
2018	73,562
2019	43,840
2020	24,267
Thereafter	23,701
	<hr/>
	<u>\$ 226,187</u>

To the extent that such notes are required for the Company's continued compliance with minimum net capital requirements, they may not be repaid. As of June 30, 2016, the Company had sufficient capital that such restrictions did not apply. The right of the note holders to receive any payment from the Company under the terms of the notes is subordinated to the claims of all present and future creditors of the Company that arise prior to maturity and is dependent on approval by FINRA.

(11) Income Taxes

(a) Uncertain Tax Positions

The Company recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more-likely-than-not sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the Consolidated Statement of Financial Condition is the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority.

The Company is included in the consolidated income tax returns of BFG in the U.S. Federal jurisdiction and various consolidated states. The Company's 2013 and 2014 corporate income tax returns are currently being audited by the Internal Revenue Service. The Company also files separate income tax returns in various states and local jurisdictions. The federal income tax returns for the years prior to 2012 are no longer subject to examination by income tax authorities, unless subsequently amended.

The Company's unrecognized tax benefits are analyzed and monitored to ensure they are adequate and reflective of known events. The Company does not believe there will be a material change in the balance within the subsequent 12 month period.

(b) Deferred Income Tax

The major deferred tax items are as follows:

Deferred Tax Assets:

Deferred Compensation Plans	\$ 35,603
Accrued Expenses	13,540
Tax Credit Carryforward	2,795
	<u>51,938</u>

Deferred Tax Liabilities:

Margin Debt	1,880
Goodwill and Intangibles	5,017
Equipment and Leasehold Improvements	11,646
Foreign Unremitted Earnings	7,826
Flow Through Investments	619
	<u>26,988</u>
Net Deferred Tax Assets	<u>\$ 24,950</u>

Pre-tax earnings of non-U.S. subsidiaries are subject to U.S. taxation when effectively repatriated, unless those earnings are indefinitely reinvested outside the U.S. Baird has recorded a deferred tax liability for foreign unremitted earnings to reflect the cumulative amount of earnings not indefinitely reinvested.

No valuation allowance is required as management believes it is more-likely-than-not that the deferred tax assets are realizable.

(12) Stockholders' Equity

As of June 30, 2016 the Company had 26,501,574 shares of common stock and 47,086 shares of common treasury stock outstanding. The Company has authorized 72,450,000 shares of \$1 stated value common stock and 1,000 shares of no par value, cumulative, nonvoting preferred stock. No shares of preferred stock were issued or outstanding as of June 30, 2016. The shares of the Company are subject to strict transfer restrictions.

(13) Associate Compensation and Retirement Plans

(a) The Baird Profit Sharing and Savings Plan

Substantially all associates of the Company are eligible to participate in the Robert W. Baird & Co. Incorporated Profit Sharing and Savings Plan. The plan complies with Section 401(k) of the Internal Revenue Code. The Company matches 100% of the first two thousand dollars contributed by each eligible participant annually. Employer profit sharing contributions are made annually at the discretion of the Company's board of directors.

(b) Non-Qualified Compensation

The Company has three non-qualified compensation plans, entitled the Baird Capital Participation Plan ("BCPP"), the Baird Financial Advisors Deferred Compensation Plan ("FADCP") and the Baird Long Term Incentive Plan ("LTIP"). The BCPP no longer grants awards and all balances in the Plan are fully vested. For services performed, the FADCP and LTIP grant awards to certain associates. The awards, which vest after seven years, are expensed at the date of grant as no future services are required, subject to continued employment. Associates have the ability to allocate their awards among several investment options.

The Company has established an allowance for unvested award forfeitures. In determining the allowance, management considers the Company's historical forfeiture experience which involves the use of estimates. The actual amounts may be substantially higher or lower than the recorded amounts.

Certain BCPP participants own restricted stock units ("RSUs"). The RSUs are fully vested in accordance with the terms of the BCPP and are ultimately convertible into BFG common stock. BCPP participants owning RSUs are entitled to cumulative distributions and dividends issued by BFG on its common stock. The RSUs become payable in full upon a change in control, as defined in the plan. The RSUs and the subsequent shares issued on conversion of the RSUs are subject to strict transfer restrictions.

(14) Partnership Consolidation

The following table presents information about the carrying value of the assets, liabilities and equity of the partnerships which are consolidated and included within the Consolidated Statement of Financial Condition. The noncontrolling interests presented in this table represent the portion of net assets not owned by the Company.

Assets:

Cash Held by Baird Private Equity Partnerships	\$ 10,234
Receivables, Other	2,121
Securities Owned by Baird Private Equity Partnerships, at Fair Value	407,558
Other Assets	3,778
Total Assets	<u>\$ 423,691</u>

Liabilities and Partners' Equity:

Accounts Payable, Accrued Expenses and Other Liabilities	\$ 24,495
Intercompany Payable	2,032
Total Liabilities	<u>26,527</u>
Partners' Equity Attributable to the Company	2,683
Partners' Equity Attributable to Noncontrolling Interests	
in Baird Private Equity Partnerships	394,481
Total Partners' Equity	<u>397,164</u>
Total Liabilities and Partners' Equity	<u>\$ 423,691</u>

Certain Baird Private Equity Partnerships are not consolidated pursuant to the accounting rules previously mentioned under the consolidation footnote. The Company's interest in non-consolidated partnerships is included within Securities Owned on the Consolidated Statement of Financial Condition. Net assets of the partnerships not consolidated were \$211,141 as of June 30, 2016. These partnerships were determined to be VIEs and the general partner (an affiliate) was determined not to be the primary beneficiary. The Company's economic interest in these partnerships was less than 10% as of June 30, 2016.

The Company has controlling interests in limited liability companies that serve as general partner in various partnerships. The Company has committed a total of \$29,231, in amounts generally ranging up to \$16,378 in 11 different private equity partnerships. As of June 30, 2016, the Company has invested \$27,796 of committed amounts.

(15) Baird UK

The Company reports the results of its investment in Baird UK using the equity method of accounting. As of June 30, 2016, the Company's investment in Baird UK was \$29,532, and is included in Other Assets on the Consolidated Statement of Financial Condition.

(16) Commitments and Contingencies

(a) Leases

The Company occupies office space and leases equipment under cancelable and non-cancelable operating lease arrangements. These lease arrangements include escalating clauses which are recognized on a straight-line basis over the life of the lease. Capital leases consist of computers, servers and other computer related items. Future minimum lease payments are as follows:

	<u>Capital</u>	<u>Operating</u>	<u>Total</u>
2016	\$ 928	\$ 13,519	\$ 14,447
2017	1,073	26,477	27,550
2018	85	22,829	22,914
2019	9	19,700	19,709
2020	-	17,038	17,038
Thereafter	-	72,210	72,210
	<u>2,095</u>	<u>\$ 171,773</u>	<u>\$ 173,868</u>
Less amounts representing interest	(29)		
Present value of minimum lease payments	<u>\$ 2,066</u>		

The capital lease obligation was \$2,066 as of June 30, 2016, and is included within Accounts Payable, Accrued Expenses and Other Liabilities on the Consolidated Statement of Financial Condition.

(b) Other

The Company is involved in legal actions from time to time that are incidental to its securities business, including without limitation, client complaints and arbitrations, employment related disputes, regulatory investigations and proceedings, securities class action claims arising from underwriting activity, and claims brought against the Company in connection with its recruitment of associates from other firms. The Company has established reserves against such contingencies. Based on its understanding of the facts and the advice of legal counsel, management believes that resolution of these various actions will not result, after taking into account the reserves, in any material adverse effect on the financial condition of the Company. As of June 30, 2016 the estimated aggregate range of possible loss related to these matters is from \$0 to \$20,000 in excess of the accrued reserve.

In the normal course of business, the Company enters into underwriting commitments. Transactions relating to underwriting commitments that were open as of June 30, 2016 were not material.

The Company is a member of numerous exchanges and clearinghouses. Under the membership agreements, members are generally required to guarantee performance of other members. Additionally, if a member becomes unable to satisfy its obligations to the clearinghouse, other members would be required to meet these shortfalls. To mitigate these performance risks, the exchanges and clearinghouses often require members to post collateral. The Company's maximum potential liability under these agreements cannot be quantified. However, the potential for the Company to be required to make payments under these agreements is remote. Accordingly, no contingent liability is recorded on the Consolidated Statement of Financial Condition for these agreements.

(17) Collateralized Transactions

The Company enters into reverse repurchase agreements, repurchase agreements, securities borrowed and securities loaned transactions in order to, among other things, acquire securities to cover short positions, accommodate customers' needs, earn residual interest rate spreads and finance the Company's inventory positions. Under these transactions, the Company either receives or provides collateral, including securities. The Company receives collateral in connection with reverse repurchase agreements and securities borrowed transactions, and pledges collateral, including cash and securities, to collateralize repurchase agreements and enter into securities lending transactions. Under many agreements, the Company is permitted to re-pledge securities held as collateral. As of June 30, 2016 the fair value of securities accepted as collateral was \$600,060, of which, \$318,568 was re-pledged to other counterparties.

Substantially all reverse repurchase agreements and repurchase agreements are transacted under legally enforceable master repurchase agreements and substantially all securities borrowed and securities lending transactions are transacted under legally enforceable master securities lending agreements. In the event of default by a counterparty, these agreements give the Company the right to liquidate securities held as collateral and to offset receivables and payables with the defaulting counterparty.

The table below reconciles the gross amounts of assets and liabilities on these transactions on the Consolidated Statement of Financial Condition to the net exposure to the Company, considering all effects of legally enforceable master netting agreements as of June 30, 2016:

	Gross Amounts ⁽¹⁾	Amounts Offset on the Consolidated Statement of Financial Condition	Net Amounts Presented on the Consolidated Statement of Financial Condition ⁽¹⁾	Amounts Not Offset on the Consolidated Statement of Financial Condition		Net Amounts
				Financial Instruments ⁽²⁾	Collateral Received/ Pledged ⁽³⁾	
Assets:						
Securities Purchased Under Agreements to Resell	\$ 332,121	\$ -	\$ 332,121	\$ (146,694)	\$ (171,468)	\$ 13,959
Deposits Paid on Securities Borrowed	277,935	-	277,935	(1,452)	(266,514)	9,969
Liabilities:						
Securities Sold Under Agreements to Repurchase	\$ 683,969	\$ -	\$ 683,969	\$ (146,694)	\$ (537,275)	\$ -
Deposits Received on Securities Loaned	18,402	-	18,402	(1,452)	(16,512)	438

⁽¹⁾ Amounts include all financial instruments, irrespective of whether there is a legally enforceable master netting agreement in place. The Company reports gross assets and liabilities on the Consolidated Statement of Financial Condition.

⁽²⁾ Amounts relate to master netting arrangements which have been determined by the Company to be legally enforceable in the event of default.

⁽³⁾ Collateral received on Securities Purchased Under Agreements to Resell and Deposits Paid on Securities Borrowed, includes securities received from the counterparty. These securities are not included on the Consolidated Statement of Financial Condition, unless there is an event of default.

Collateral pledged on Securities Sold Under Agreements to Repurchase and Deposits Received on Securities Loaned, includes the fair value of securities pledged to the counterparty. These securities are included on the Consolidated Statement of Financial Condition, unless there is an event of default.

The following table presents the remaining contractual maturity of repurchase agreements and securities lending transactions disaggregated by type of collateral, accounted for as secured borrowings as of June 30 2016:

	Remaining Contractual Maturity		
	Overnight & Continuous	Up to 30 Days	Total
Securities Sold Under Agreements to Repurchase			
U.S. Government and Agency Obligations	\$ 200,654	\$ 177,801	\$ 378,455
Corporate Bonds	244,453	61,061	305,514
Total Securities Sold Under Agreements to Repurchase	<u>\$ 445,107</u>	<u>\$ 238,862</u>	<u>\$ 683,969</u>
Deposits Received on Securities Loaned Equity Securities	<u>\$ 18,402</u>	<u>\$ -</u>	<u>\$ 18,402</u>

Repurchase agreements and securities lending activities are entered into and conducted as components of the financing of certain operating activities. In the event the market value of the securities pledged as collateral declines, additional collateral may need to be posted or borrowing amounts may need to be reduced.

(18) Financial Instruments with Off-Balance Sheet Risk

In the normal course of business, the Company's client securities activities involve the execution, settlement and financing of various client securities transactions. These activities may expose the Company to off-balance sheet risk in the event the client or other broker is unable to fulfill its contracted obligations and the Company has to purchase or sell the financial instrument underlying the contract at a loss.

The Company seeks to control the risks associated with its client activities by requiring clients to maintain margin collateral in compliance with various regulatory and internal guidelines. The Company monitors required margin levels daily and, pursuant to such guidelines, requires the client to deposit additional collateral or to reduce security positions when necessary. Such collateral is not reflected in the accompanying Consolidated Statement of Financial Condition.

The Company enters into various transactions involving derivatives and other off-balance sheet financial instruments. These financial instruments include TBA mortgage-backed securities, as well as securities purchased and sold on a when-issued basis (when-issued securities). These financial instruments are used to meet the needs of customers, conduct trading activities, and manage market risks and are, therefore, subject to varying degrees of market and credit risk.

TBAs and when-issued securities provide for the delayed delivery of the underlying instrument. The contractual or notional amounts related to these financial instruments reflect the volume and activity and do not reflect the amounts at risk. The gain or loss on these transactions is recognized on a trade date basis. The credit risk for TBAs, options, and when-issued securities is limited to the unrealized fair valuation gains and losses recorded in the Consolidated Statement of Financial Condition. The Company's exposure to market risk is determined by a number of factors, including but not limited to the size, composition and diversification of positions held, the absolute and relative levels of interest rates, and market volatility.

In addition, the Company has sold securities that it does not currently own (securities sold, not yet purchased) and will therefore be obligated to purchase such securities at a future date. The Company has recorded these obligations in the Consolidated Statement of Financial Condition as of June 30, 2016, at the fair values of the related securities and will incur a loss if the fair value of the securities increases.

The Company's customer securities activities are transacted on either a cash or margin basis. In margin transactions, the Company extends credit to its customers, subject to various regulatory and internal margin requirements, collateralized by cash and securities in the customers' accounts. In connection with these activities, the Company executes and clears customer transactions involving the sale of securities not yet purchased, substantially all of which are transacted on a margin basis subject to individual exchange regulations. Such transactions may expose the Company to significant off-balance-sheet risk in the event margin requirements are not sufficient to fully cover losses that customers may incur. In the event the customer fails to satisfy its obligations, the Company may be required to purchase or sell financial instruments at prevailing market prices to fulfill the customer's obligations. The Company seeks to control the risks associated with its customer activities by requiring clients to maintain margin collateral in compliance with various regulatory and internal guidelines. The Company monitors required margin levels daily, and pursuant to such guidelines, requires the clients to deposit additional collateral or to reduce positions when necessary.

In conjunction with certain borrowing transactions, the Company's client financing and securities settlement activities require the Company to pledge certain securities. In the event the counterparty is unable to meet its contractual obligation to return securities pledged as collateral, the Company may be exposed to the risk of acquiring the securities at prevailing market prices in order to satisfy its obligations. The Company controls this risk by monitoring the fair value of securities pledged on a daily basis and by requiring adjustments of collateral levels in the event of excess market exposure. In addition, the Company establishes monitoring limits for such activities and monitors them on a daily basis.

The Company may use financial futures and options to manage market risk related to trading securities. The Company did not have open futures or options positions as of June 30, 2016.

(19) Federal Deposit Insurance Corporation

The Company has certain cash deposit accounts with financial institutions in which the balances occasionally exceed the Federal Deposit Insurance Corporation ("FDIC") insured limit. The Company has not experienced any losses in such accounts and management believes it is not exposed to any significant risk.

(20) Subsequent Events

The Company evaluated its June 30, 2016 Consolidated Statement of Financial Condition for subsequent events through August 29, 2016, the date the Consolidated Statement of Financial Condition was available to be issued. The Company is not aware of any subsequent events which would require recognition or disclosure in the Consolidated Statement of Financial Condition.