

A-Mark Precious Metals, Inc.
Form 10-Q
February 11, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended December 31, 2015

OR

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

For the transition period from _____ to _____

Commission File Number: 001-36347

A-MARK PRECIOUS METALS, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State of Incorporation)
429 Santa Monica Blvd.
Suite 230
Santa Monica, CA 90401
(Address of principal executive offices)(Zip Code)
(310) 587-1477
(Registrant's Telephone Number, Including Area Code)

11-2464169
(IRS Employer I.D. No.)

Securities registered under Section 12(b) of the Exchange Act:

Title of each class

Common Stock, \$0.01 par value

Securities registered under Section 12 (g) of the Exchange Act: None

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

Yes. No.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

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company” in Rule 12b-2 of the Exchange Act:

Large accelerated filer Accelerated filer Non-accelerated filer
(Do not check if a smaller reporting
company) Smaller reporting
company

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

As of February 8, 2016, the registrant had 6,973,549 shares of common stock outstanding, par value \$0.01 per share.

A-MARK PRECIOUS METALS, INC.

QUARTERLY REPORT ON FORM 10-Q
For the Quarter Ended December 31, 2015

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PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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A-MARK PRECIOUS METALS, INC.
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (amounts in thousands, except for share data)
 (unaudited)

	December 31, 2015	June 30, 2015
ASSETS		
Current assets:		
Cash	\$3,375	\$20,927
Receivables, net	22,557	30,025
Derivative assets	17,123	11,364
Secured loans receivables	57,108	48,666
Inventories:		
Inventories	189,275	152,076
Restricted inventories	50,504	39,425
	239,779	191,501
Income taxes receivable	6,982	7,846
Income taxes receivable from Former Parent	—	1,095
Prepaid expenses and other assets	648	1,202
Total current assets	347,572	312,626
Property and equipment, net	3,009	2,850
Goodwill	4,884	4,884
Intangibles, net	2,178	2,369
Long-term secured loans receivables	600	650
Long-term investments	4,836	2,500
Deferred tax assets - non-current	—	23
Total assets	\$363,079	\$325,902
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Lines of credit	\$162,500	\$147,000
Liability on borrowed metals	4,234	9,500
Product financing arrangement	50,504	39,425
Accounts payable	56,059	50,639
Derivative liabilities	19,930	17,897
Accrued liabilities	5,593	5,330
Income taxes payable to Former Parent	510	—
Deferred tax liability - current	1,369	149
Total current liabilities	300,699	269,940
Deferred tax liabilities - non-current	312	—
Total liabilities	301,011	269,940
Commitments and contingencies		
Stockholders' equity:		
	—	—

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Preferred stock, \$0.01 par value, authorized 10,000,000 shares; issued and outstanding: none as of December 31, 2015 and June 30, 2015		
Common Stock, par value \$0.01; 40,000,000 authorized; 6,973,549 and 6,973,549 issued and outstanding as of December 31, 2015 and June 30, 2015, respectively	70	70
Additional paid-in capital	22,577	22,470
Retaining earnings	39,421	33,422
Total stockholders' equity	62,068	55,962
Total liabilities and stockholders' equity	\$363,079	\$325,902

See accompanying Notes to Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF INCOME
 (in thousands, except for share and per share data)
 (unaudited)

	Three Months Ended		Six Months Ended	
	December 31, 2015	December 31, 2014	December 31, 2015	December 31, 2014
Revenues	\$1,529,143	\$1,538,871	\$3,536,079	\$2,992,337
Cost of sales	1,523,467	1,531,678	3,515,979	2,979,414
Gross profit	5,676	7,193	20,100	12,923
Selling, general and administrative expenses	(4,528	) (4,754	) (10,936	) (8,973
Interest income	2,182	1,398	4,115	2,875
Interest expense	(1,322	) (969	) (2,556	) (2,032
Unrealized gains (losses) on foreign exchange	150	(75	) 111	(84
Net income before provision for income taxes	2,158	2,793	10,834	4,709
Provision for income taxes	(827	) (1,131	) (4,139	) (1,909
Net income	\$1,331	\$1,662	\$6,695	\$2,800
Basic and diluted income per share:				
Basic - net income	\$0.19	\$0.24	\$0.96	\$0.40
Diluted - net income	\$0.19	\$0.24	\$0.94	\$0.40
Weighted average shares outstanding:				
Basic	6,973,500	6,962,742	6,973,500	6,962,742
Diluted	7,119,000	7,059,400	7,089,700	7,062,300

See accompanying Notes to Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(in thousands, except for share data)

(unaudited)

	Common Stock (Shares)	Common Stock	Additional Paid-in Capital	Retained Earnings	Total Stockholders' Equity
Balance, June 30, 2015	6,973,549	\$70	\$22,470	\$33,422	\$55,962
Net income	—	—	—	6,695	6,695
Share-based compensation	—	—	107	—	107
Dividends declared	—	—	—	(696)	(696)
Balance, December 31, 2015	6,973,549	\$70	\$22,577	\$39,421	\$62,068

See accompanying Notes to Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(amounts in thousands)

(unaudited)

Six Months Ended	December 31, 2015	December 31, 2014	
Cash flows from operating activities:			
Net income	\$6,695	\$2,800	
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation and amortization	606	455	
Deferred income taxes	1,555	(5,963)
Interest added to principal of secured loans	(46	) (144)
Share-based compensation	107	122	
Changes in assets and liabilities:			
Receivables	7,468	(25,951)
Secured loans	2,361	(255)
Secured loans to Former Parent	(881	) (2,739)
Derivative assets	(5,759	) 4,072	
Income tax receivable	864	(197)
Inventories	(48,278	) (48,217)
Prepaid expenses and other current assets	554	(45)
Accounts payable	5,420	934	
Derivative liabilities	2,033	2,407	
Liabilities on borrowed metals	(5,266	) (3,025)
Accrued liabilities	263	(2,654)
Income tax receivable from/ income taxes payables to Former Parent	1,605	—	
Income taxes payable	—	(2,178)
Net cash used in operating activities	(30,699	) (80,578)
Cash flows from investing activities:			
Capital expenditures for property and equipment	(574	) (76)
Purchase of cost method investment	(2,336	) (1,111)
Secured loans, net	(9,826	) 1,835	
Net cash (used in) provided by investing activities	(12,736	) 648	
Cash flows from financing activities:			
Product financing arrangement, net	11,079	56,050	
Dividends paid	(696) —	
Borrowings under lines of credit, net	15,500	15,800	
Net cash provided by financing activities	25,883	71,850	
Net decrease in cash and cash equivalents	(17,552	) (8,080)
Cash and cash equivalents, beginning of period	20,927	13,193	
Cash and cash equivalents, end of period	\$3,375	\$5,113	
Supplemental disclosures of cash flow information:			
Cash paid during the period for:			
Interest expense	\$2,393	\$1,719	
Income taxes	\$113	\$10,247	

Non-cash investing and financing activities:		
Interest added to principal of secured loans	\$46	\$144

See accompanying Notes to Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

A-Mark Precious Metals, Inc. and its subsidiaries (“A-Mark” or the “Company”) is a full-service precious metals trading company. Its products include gold, silver, platinum and palladium for storage and delivery primarily in the form of coins, bars, wafers and grain. The Company's trading-related services include financing, consignment, logistics, hedging and various customized financial programs.

Through its wholly owned subsidiary, Collateral Finance Corporation (“CFC”), a licensed California Finance Lender, the Company offers loans on precious metals, rare coins and other collectibles collateral to coin dealers, collectors and investors. Through its wholly owned subsidiary, A-Mark Trading AG (“AMTAG”), the Company promotes A-Mark bullion products throughout the European continent. Transcontinental Depository Services (“TDS”), also a wholly owned subsidiary of the Company, offers worldwide storage solutions to institutions, dealers and consumers.

The Company's wholly-owned subsidiary, A-M Global Logistics, LLC (“Logistics”), operates the Company's logistics fulfillment center based in Las Vegas, Nevada, which began operations in July 2015. Logistics provides our customers an array of complementary services, including storage, shipping, handling, receiving, processing, and inventorying of precious metals and custom coins on a secure basis.

Spinoff from Spectrum Group International, Inc.

On March 14, 2014, the Company's former parent, Spectrum Group International, Inc. (“SGI” or the “Former Parent”), effected a spinoff (the “spinoff” or the “Distribution”) of the Company from SGI. As a result of the Distribution, the Company became a publicly traded company independent from SGI. On March 17, 2014, A-Mark’s shares of common stock commenced trading on the NASDAQ Global Select Market under the symbol “AMRK.”

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Principles of Consolidation

The condensed consolidated financial statements reflect the financial condition, results of operations, and cash flows of the Company, and were prepared using accounting principles generally accepted in the United States (“U.S. GAAP”). The Company operated in one segment for all periods presented.

These condensed consolidated financial statements include the accounts of A-Mark, and its wholly owned subsidiaries, CFC, AMTAG, Logistics and TDS (collectively the “Company”). All significant inter-company accounts and transactions have been eliminated in consolidation.

Unaudited Interim Financial Information

The accompanying interim condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”) for interim financial reporting. These interim condensed consolidated financial statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments and accruals) necessary to present fairly the condensed consolidated balance sheets, condensed consolidated statements of income, condensed consolidated statements of stockholders’ equity, and condensed consolidated statements of cash flows for the periods presented in accordance with U.S. GAAP. Operating results for the six months ended December 31, 2015 are not necessarily indicative of the results that may be expected for the year ending June 30, 2016 or for any other interim period during such fiscal year. Certain information and footnote disclosures normally included in annual consolidated financial statements prepared in accordance with U.S. GAAP have been omitted in accordance with the rules and regulations of the SEC. These interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2015 (the “2015 Annual Report”), as filed with the SEC. Amounts related to disclosure of June 30, 2015 balances within these interim condensed consolidated financial statements were derived from the aforementioned audited consolidated financial statements and notes thereto included in the 2015 Annual Report.

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Reclassifications

Certain previously reported amounts have been reclassified to conform to the current fiscal quarter's condensed consolidated financial statement presentation. In the previous reported periods, account receivables included secured loans and derivative assets; these components are shown as separate lines items on the condensed consolidated balance sheets and cash flow statements. Similarly, accounts payables included derivative liabilities; these components are shown as separate lines items on the condensed consolidated balance sheets and cash flow statements.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements, and the reported amounts of revenue and expenses during the reporting periods. These estimates include, among others, determination of fair value, and allowances for doubtful accounts, impairment assessments of long-lived assets and intangible assets, valuation reserve determination on deferred tax assets, and revenue recognition judgments. Significant estimates also include the Company's fair value determination with respect to its financial instruments and precious metals materials. Actual results could materially differ from these estimates.

Concentration of Credit Risk

Cash is maintained at financial institutions and, at times, balances may exceed federally insured limits. The Company has never experienced any losses related to these balances.

Assets that potentially subject the Company to concentrations of credit risk consist principally of receivables, loans of inventory to customers, and inventory hedging transactions. Concentration of credit risk with respect to receivables is limited due to the large number of customers composing the Company's customer base, the geographic dispersion of the customers, and the collateralization of substantially all receivable balances. Based on an assessment of credit risk, the Company typically grants collateralized credit to its customers. The Company enters into inventory hedging transactions, principally utilizing metals commodity futures contracts traded on national futures exchanges or forward contracts with credit worthy financial institutions. Credit risk with respect to loans of inventory to customers is minimal; substantially all inventories loaned under consignment arrangements are collateralized for the benefit of the Company. All of our commodity derivative contracts are under master netting arrangements and include both asset and liability positions. Substantially all of these transactions are secured by the underlying metals positions.

Foreign Currency

The functional currency of the Company is the United States dollar ("USD"). Also, the functional currency of the Company's wholly-owned foreign subsidiary, AMTAG, is USD, but it maintains its books of record in Euros. The Company remeasures the financial statements of AMTAG into USD. The remeasurement of local currency amounts into USD creates remeasurement gains and losses, which are included in the condensed consolidated statements of income.

To manage the effect of foreign currency exchange fluctuations, the Company utilizes foreign currency forward contracts. These derivatives generate gains and losses when they are settled and/or when they are marked to market. The change in the value in the derivative instruments is shown on the face of the condensed consolidated statements of income as unrealized net gains (losses) on foreign exchange.

Cash Equivalents

The Company considers all highly liquid investments with original maturities of three months or less, when purchased, to be cash equivalents.

Inventories

Inventories principally include bullion and bullion coins and are acquired and initially recorded at fair market value. The fair market value of the bullion and bullion coins is comprised of two components: (1) published market values attributable to the costs of the raw precious metal, and (2) a published premium paid at acquisition of the metal. The premium is attributable to the additional value of the product in its finished goods form and the market value attributable solely to the premium may be readily determined, as it is published by multiple reputable sources. The Company's inventories, except for certain lower of cost or market basis products (as discussed below), are subsequently recorded at their fair market values, that is, "marked-to-market". The daily changes in the fair market

value of our inventory are offset by daily changes in the fair market value of hedging derivatives that are taken with respect to our inventory positions; both the change in the fair market value of the inventory and the change in the fair market value of these derivative instruments are recorded in cost of sales in the condensed consolidated statements of income.

While the premium component included in inventories is marked-to-market, our commemorative coin inventory, including its premium component, is held at the lower of cost or market, because the value of commemorative coins is influenced more by

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supply and demand determinants than on the underlying spot price of the precious metal content of the commemorative coins. Unlike our bullion coins, the value of commemorative coins is not subject to the same level of volatility as bullion coins because our commemorative coins typically carry a substantially higher premium over the spot metal price than bullion coins. Neither the commemorative coin inventory nor the premium component of our inventory is hedged (see [Note 6](#).)

Property and Equipment and Depreciation

Property and equipment is stated at cost less accumulated depreciation. Depreciation is calculated using a straight line method based on the estimated useful lives of the related assets, ranging from three years to five years.

Goodwill and Purchased Intangible Assets

Goodwill is recorded when the purchase price paid for an acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired.

Goodwill and other indefinite life intangibles are evaluated for impairment annually in the fourth quarter of the fiscal year (or more frequently if indicators of potential impairment exist) in accordance with the Intangibles - Goodwill and Other Topic 350 of the Accounting Standards Codification ("ASC".) Other purchased intangible assets continue to be amortized over their useful lives and are evaluated for impairment when events or changes in business circumstances indicate that the carrying amount of the assets may not be recoverable. The Company may first qualitatively assess whether relevant events and circumstances make it more likely than not that the fair value of the reporting unit's goodwill is less than its carrying value. If, based on this qualitative assessment, management determines that goodwill is more likely than not to be impaired, the two-step impairment test is performed. This first step in this test includes comparing the fair value of each reporting unit to its carrying value, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, the second step in the test is performed, which is measurement of the impairment loss. The impairment loss is calculated by comparing the implied fair value of goodwill, as if the reporting unit has been acquired in a business combination, to its carrying amount. As of December 31, 2015 and June 30, 2015, the Company had no impairments.

If the Company determines it will quantitatively assess impairment, the Company utilizes the discounted cash flow method to determine the fair value of each of its reporting units. In calculating the implied fair value of the reporting unit's goodwill, the present value of the reporting unit's expected future cash flows is allocated to all of the other assets and liabilities of that unit based on their fair values. The excess of the present value of the reporting unit's expected future cash flows over the amount assigned to its other assets and liabilities is the implied fair value of goodwill. In calculating the implied value of the Company's trade names, the Company uses the present value of the relief from royalty method.

Amortizable intangible assets are being amortized on a straight-line basis which approximates economic use, over periods ranging from three years to fifteen years. The Company considers the useful life of the trademarks to be indefinite. The Company tests the value of the trademarks and trade name annually for impairment.

Long-Lived Assets

Long-lived assets, other than goodwill and purchased intangible assets with indefinite lives are evaluated for impairment when events or changes in business circumstances indicate that the carrying amount of the assets may not be recoverable. In evaluating impairment, the carrying value of the asset is compared to the undiscounted estimated future cash flows expected to result from the use of the asset and its eventual disposition. An impairment loss is recognized when estimated future cash flows are less than the carrying amount. Estimates of future cash flows may be internally developed or based on independent appraisals and significant judgment is applied to make the estimates. Changes in the Company's strategy, assumptions and/or market conditions could significantly impact these judgments and require adjustments to recorded amounts of long-lived assets. As of December 31, 2015 and June 30, 2015, management concluded that an impairment was not required.

Investments

Investments into noncontrolled entities that do not have readily determinable fair values (i.e., non-marketable equity securities) under Cost Method Investments Topic 325-20 of the ASC are initially recorded at cost. Income is recorded for dividends received that are distributed from net accumulated earnings of the noncontrolled entity subsequent to the date of investment. Dividends received in excess of earnings subsequent to the date of investment are considered a

return of investment and are recorded as reductions in the cost of the investment. Investments are written down only when there is clear evidence that a decline in value that is other than temporary has occurred. The Company assesses all cost-method investments for impairment quarterly. Below is a summary of the Company's cost-method investments.

The Company has two investments into non-controlled entities, both of which are online precious metals retailers and customers of the Company. As of December 31, 2015 and June 30, 2015, (i) the aggregate carrying balance of these investments was \$4.8 million and \$2.5 million, respectively, and (ii) the Company's ownership percentage, based on the fully dilutive common shares outstanding, for one of the entities was 2.5% and 15.0%, respectively, and for the other entity, was 2.5% and 9.0%, respectively. Neither of the entities declared dividends or was impaired during the three and six month periods ending December

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31, 2015 and 2014. On January 15, 2016, the Company increased its ownership interest in one of the entities from 15.0% to 20.0% (see [Note 18](#).)

The Company has exclusive supplier agreements with each entity, whereby the customers are required purchase all bullion products required for their business exclusively from A-Mark, subject to certain limitations. The Company also provides fulfillment services to the customer in which it owned a 15% interest as of December 31, 2015.

Fair Value Measurement

The Fair Value Measurements and Disclosures Topic 820 of the ASC ("ASC 820"), creates a single definition of fair value for financial reporting. The rules associated with ASC 820 state that valuation techniques consistent with the market approach, income approach and/or cost approach should be used to estimate fair value. Selection of a valuation technique, or multiple valuation techniques, depends on the nature of the asset or liability being valued, as well as the availability of data (see [Note 3](#).)

Revenue Recognition

Revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable, no obligations remain and collection is probable. The Company records sales of precious metals, which occurs upon receipt by the customer. The Company records revenues from its metal assaying and melting services after the related services are completed and the effects of forward sales contracts are reflected in revenue at the date the related precious metals are delivered or the contracts expire. The Company records revenues from its storage and logistics services after the related services are completed.

The Company accounts for its metals and sales contracts using settlement date accounting. Pursuant to such accounting, the Company recognizes the sale or purchase of the metals at settlement date. During the period between trade and settlement date, the Company has essentially entered into a forward contract that meets the definition of a derivative in accordance with the Derivatives and Hedging Topic 815 of the ASC. The Company records the derivative at the trade date with a corresponding unrealized gain (loss), which is reflected in the cost of sales in the condensed consolidated statements of income. The Company adjusts the derivatives to fair value on a daily basis until the transaction is physically settled. Sales which are physically settled are recognized at the gross amount in the condensed consolidated statements of income.

Interest Income

The Company uses the effective interest method to recognize interest income on its secured loans transactions. For these arrangements, the Company maintains a security interest in the precious metals and records interest income over the terms of the receivable. Recognition of interest income is suspended and the loan is placed on non-accrual status when management determines that collection of future interest income is not probable. The interest income accrual is resumed, and previously suspended interest income is recognized, when the loan becomes contractually current and/or collection doubts are removed. Cash receipts on impaired loans are recorded first against the receivable and then to any unrecognized interest income (see [Note 5](#).)

Also, the Company enters into repurchases agreements, whereby the Company sells products at the prevailing spot price plus a premium, and then repurchases the products back from the customer at the prevailing spot price, thereby earning a fee (recorded as interest income) based on a calculated premium over the spot price, resulting in an open sales commitment to deliver products at the agreed upon date and price.

Interest Expense

The Company incurs interest expense and related fees as a result of usage under its lines of credit, product financing arrangements and liability on borrowed metals.

The Company incurs interest expense based on usage under its Trading Credit Facility recording interest expense using the effective interest method.

The Company incurs financing fees (classified as interest expense) as a result of its product financing arrangements for the transfer and subsequent re-acquisition of gold and silver at a fixed price to a third party finance company. During the term of this type of financing agreement, a third party finance company holds the Company's inventory as collateral, with the intent to return the inventory to the Company at an agreed-upon price based on the spot price on the finance arrangement termination date, pursuant to the guidance in Product Financing Arrangements Topic 470-40 of the ASC. The third party charges a monthly fee as a percentage of the market value of the outstanding obligation. In

addition, the Company incurs a financing fee related to custodial storage facility charges related to the transferred collateral inventory; this collateral is classified as restricted inventory on our condensed consolidated balance sheets. Additionally, the Company incurs interest expense when we borrow precious metals from our suppliers under short-term arrangements, which bear interest at a designated rate. Amounts under these arrangements are due at maturity and require repayment either in the form of precious metals or cash. This liability is reflected in the condensed consolidated balance sheet as a liability on borrowed metals.

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Derivative Instruments

The Company's inventory, and purchase and sale commitments transactions consist of precious metals products. The value of our inventory and these commitments is intimately linked to the prevailing price of the underlying precious metal commodity. The Company seeks to minimize the effect of price changes of the underlying commodity and enters into inventory hedging transactions, principally utilizing metals commodity futures contracts traded on national futures exchanges or forward contracts with only major credit worthy financial institutions. All of our commodity derivative contracts are under master netting arrangements and include both asset and liability positions. Substantially all of these transactions are secured by the underlying metals positions. Notional balances of the Company's derivative instruments, consisting of contractual metal quantities, are expressed at current spot prices of the underlying precious metal commodity.

Commodity futures and forward contract transactions are recorded at fair value on the trade date. The difference between the original contract value and the market value of the open futures and forward contracts are reflected in derivative assets or derivative liabilities in the condensed consolidated balance sheet at fair value.

The Company records the change between market value and trade value of the underlying open commodity contracts as a derivative asset or liability, and the Company correspondingly records the related unrealized gains or losses. The change in unrealized gain (loss) on open commodity contracts from one period to the next is reflected in net gain (loss) on derivative instruments. These unrealized gains and losses are included as a component of cost of sales on the condensed consolidated statements of income. Gains or losses resulting from the termination of commodity contracts are reported as realized gains or losses on commodity contracts, which is recorded as a component of cost of sales on the condensed consolidated statements of income.

The Company enters into derivative transactions solely for the purpose of hedging our inventory holding risk, and not for speculative market purposes. The Company's gains (losses) on derivative instruments are substantially offset by the changes in the fair market value of the underlying precious metals inventory, which is also recorded in cost of sales in the condensed consolidated statements of income (see Note 10.)

Advertising

Advertising costs are expensed as incurred, and are included in selling, general and administrative expenses in the condensed consolidated statements of income. Advertising expense was \$153,000 and \$106,000, respectively, for the three months ended December 31, 2015 and 2014. Advertising expense was \$326,000 and \$250,000, respectively, for the six months ended December 31, 2015 and 2014.

Shipping and Handling Costs

Shipping and handling costs represent costs associated with shipping product to customers, and receiving product from vendors and are included in cost of sales in the condensed consolidated statements of income. Shipping and handling costs incurred totaled \$1.8 million and \$1.8 million, respectively, for the three months ended December 31, 2015 and 2014. Shipping and handling costs incurred totaled \$4.1 million and \$3.2 million, respectively, for the six months ended December 31, 2015 and 2014.

Share-Based Compensation

The Company accounts for equity awards under the provisions of the Compensation - Stock Compensation Topic 718 of the ASC ("ASC 718"), which establishes fair value-based accounting requirements for share-based compensation to employees. ASC 718 requires the Company to recognize the grant-date fair value of stock options and other equity-based compensation issued to employees as expense over the service period in the Company's condensed consolidated financial statements.

Income Taxes

As part of the process of preparing its condensed consolidated financial statements, the Company is required to estimate its provision for income taxes in each of the tax jurisdictions in which it conducts business, in accordance with the Income Taxes Topic 740 of the ASC ("ASC 740"). The Company computes its annual tax rate based on the statutory tax rates and tax planning opportunities available to it in the various jurisdictions in which it earns income. Significant judgment is required in determining the Company's annual tax rate and in evaluating uncertainty in its tax positions. The Company recognizes a benefit for tax positions that it believes will more likely than not be sustained upon examination. The amount of benefit recognized is the largest amount of benefit that the Company believes has

more than a 50% probability of being realized upon settlement. The Company regularly monitors its tax positions and adjusts the amount of recognized tax benefit based on its evaluation of information that has become available since the end of its last financial reporting period. The annual tax rate includes the impact of these changes in recognized tax benefits. When adjusting the amount of recognized tax benefits, the Company does not consider information that has become available after the balance sheet date, but does disclose the effects of new information whenever those effects would be material to the Company's condensed consolidated financial statements. The difference between the amount of benefit taken or expected to be taken in a tax return and the amount of benefit recognized for financial reporting represents unrecognized tax benefits. These unrecognized tax benefits are presented in the condensed consolidated balance sheet principally within accrued liabilities.

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The Company records valuation allowances to reduce deferred tax assets to the amount that is more likely than not to be realized. Significant judgment is applied when assessing the need for valuation allowances. Areas of estimation include the Company's consideration of future taxable income and ongoing prudent and feasible tax planning strategies. Should a change in circumstances lead to a change in judgment about the utilization of deferred tax assets in future years, the Company would adjust related valuation allowances in the period that the change in circumstances occurs, along with a corresponding increase or charge to income. Changes in recognized tax benefits and changes in valuation allowances could be material to the Company's results of operations for any period, but is not expected to be material to the Company's condensed consolidated financial position.

The Company accounts for uncertainty in income taxes under the provisions of ASC 740. These provisions clarify the accounting for uncertainty in income taxes recognized in an enterprise's financial statements, and prescribe a recognition threshold and measurement criteria for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The provisions also provide guidance on de-recognition, classification, interest, and penalties, accounting in interim periods, disclosure, and transition. The potential interest and/or penalties associated with an uncertain tax position are recorded in provision for income taxes on the condensed consolidated statements of income. Please refer to Note 11 for further discussion regarding these provisions.

Income taxes are accounted for using an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. A valuation allowance is provided when it is more likely than not that some portion or all of the net deferred tax assets will not be realized. The factors used to assess the likelihood of realization include the Company's forecast of the reversal of temporary differences, future taxable income and available tax planning strategies that could be implemented to realize the net deferred tax assets. Failure to achieve forecasted taxable income in applicable tax jurisdictions could affect the ultimate realization of deferred tax assets and could result in an increase in the Company's effective tax rate on future earnings.

Based on our assessment it appears more likely than not that most of the net deferred tax assets will be realized through future taxable income. Management has established a valuation allowance against the deferred taxes related to certain state net operating loss carryovers. Management believes the utilization of these losses may be limited. We will continue to assess the need for a valuation allowance for our remaining deferred tax assets in the future.

The Company's condensed consolidated financial statements recognized the current and deferred income tax consequences that result from the Company's activities during the current and preceding periods, as if the Company were a separate taxpayer prior to the date of the Distribution rather than a member of the consolidated income tax return group of its Former Parent, Spectrum Group International, Inc. Following its spin-off, the Company files federal and state income tax filings that are separate from the Former Parent's tax filings. The Company recognizes current and deferred income taxes as a separate taxpayer for periods ending after the date of Distribution.

Income taxes payable to Former Parent reflects balances due to the Former Parent for the Company's share of the income tax assets of the group, net of amounts related to federal and state jurisdictions due to taxable income generated as if the Company were a separate taxpaying entity prior to the Distribution. Income taxes receivable from Former Parent reflects balance due from the Former Parent for the Company's share of the income tax assets of the group, net of amounts related to federal and state jurisdictions due to taxable income generated as if the Company were a separate taxpaying entity prior to the Distribution.

Earnings per Share ("EPS")

The Company computes and reports both basic EPS and diluted EPS. Basic EPS is computed by dividing net earnings by the weighted average number of common shares outstanding for the period. Diluted EPS is computed by dividing net earnings by the sum of the weighted average number of common shares and dilutive common stock equivalents outstanding during the period. Diluted EPS reflects the total potential dilution that could occur from outstanding equity awards, including unexercised stock options, utilizing the treasury stock method.

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A reconciliation of shares used in calculating basic and diluted earnings per common shares follows. There is no dilutive effect of stock appreciation rights ("SARs"), as such obligations are not settled and were out of the money for the three months ended December 31, 2015 and 2014.

in thousands

	Three Months Ended		Six Months Ended	
	December 31, 2015	December 31, 2014	December 31, 2015	December 31, 2014
Basic weighted average shares outstanding ⁽¹⁾	6,974	6,963	6,974	6,963
Effect of common stock equivalents — stock issuable under outstanding equity awards	145	96	116	99
Diluted weighted average shares outstanding	7,119	7,059	7,090	7,062

(1) Basic weighted average shares outstanding include the effect of vested but unissued restricted stock grants. Recent Accounting Pronouncements

In November 2015, the FASB issued Accounting Standards Update ("ASU") No. 2015-17, Income Taxes: Balance Sheet Classification of Deferred Taxes ("ASU 2015-17"), which simplifies the presentation of deferred taxes by requiring deferred tax assets and liabilities be classified as non-current on the balance sheet. This update is effective for fiscal years beginning after December 15, 2016. The guidance may be adopted prospectively or retrospectively and early adoption is permitted. We have not early adopted ASU, and the adoption of this update is not expected to have a material impact on our results of operations, financial position or cash flows. We expect to adopt the provisions of this new guidance in fiscal year 2018 (or July 1, 2017).

In February 2015, the FASB issued ASU No. 2015-2, Consolidation (Topic 820): Amendments to the Consolidation Analysis. ASU 2015-2 provides a revised consolidation model for all reporting entities to use in evaluating whether they should consolidate certain legal entities. All legal entities will be subject to re-ev