CBOE Holdings, Inc.
Form 10-Q
May 06, 2015
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 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 No. 001-34774
CBOE HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	20-5446972 (I.R.S. Employer Identification No.)
400 South LaSalle Street Chicago, Illinois (Address of principal executive offices)	60605 (Zip Code)

Registrant's telephone number, including area code
(312) 786-5600

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 ý 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 ý 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 company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ý	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 Act). Yes ¨ No ý
Indicate the number of shares outstanding of each of the registrant's classes of unrestricted common stock, as of the latest practicable date:

Class	April 24, 2015
Unrestricted Common Stock, par value $0.01	83,473,311 shares

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CERTAIN DEFINED TERMS

Throughout this document, unless otherwise specified or the context so requires:

- "CBOE Holdings," "we," "us," "our" or "the Company" refers to CBOE Holdings, Inc. and its subsidiaries.
- "CBOE" refers to Chicago Board Options Exchange, Incorporated, a wholly-owned subsidiary of CBOE Holdings, Inc.
- "C2" refers to C2 Options Exchange, Incorporated, a wholly-owned subsidiary of CBOE Holdings, Inc.
- "CFE" refers to CBOE Futures Exchange, LLC, a wholly-owned subsidiary of CBOE Holdings, Inc.
- "CFTC" refers to the U.S. Commodity Futures Trading Commission.
- "FASB" refers to the Financial Accounting Standards Board.
- "GAAP" refers to Generally Accepted Accounting Principles in the United States.
- "OPRA" refers to the Options Price Reporting Authority, which is a limited liability company of member exchanges and is authorized by the SEC to provide consolidated options information.
- "Our exchanges" refers to CBOE, C2 and CFE.
- "SEC" refers to the U.S. Securities and Exchange Commission.
- "SPX" refers to our S&P 500 Index exchange-traded options products.
- "VIX" refers to the CBOE Volatility Index methodology.

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FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involve a number of risks and uncertainties. You can identify these statements by forward-looking words such as "may," "might," "should," "expect," "plan," "anticipate," "believe," "estimate," "predict," "potential" or "continue," and the negative of these terms and other comparable terminology. All statements that reflect our expectations, assumptions or projections about the future other than statements of historical fact are forward-looking statements, including statements in the "Business" and "Management's Discussion and Analysis of Financial Condition and Results of Operations sections of this report." These forward-looking statements, which are subject to known and unknown risks, uncertainties and assumptions about us, may include projections of our future financial performance based on our growth strategies and anticipated trends in our business. These statements are only predictions based on our current expectations and projections about future events. There are important factors that could cause our actual results, level of activity, performance or achievements to differ materially from that expressed or implied by the forward-looking statements. In particular, you should consider the risks and uncertainties described under "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2014, Part II, Item 1A of this Quarterly Report on Form 10-Q and our other filings with the SEC.

While we believe we have identified the risks that are material to us, these risks and uncertainties are not exhaustive. Moreover, we operate in a very competitive and rapidly changing environment. New risks and uncertainties emerge from time to time, and it is not possible to predict all risks and uncertainties, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

Some factors that could cause actual results to differ include:

- the loss of our right to exclusively list and trade certain index options and futures products;
- increasing price competition in our industry;
- compliance with legal and regulatory obligations, including our obligations under the Consent Order;
- decreases in trading volumes or a shift in the mix of products traded on our exchanges;
- legislative or regulatory changes;
- increasing competition by foreign and domestic entities;
- our dependence on third party service providers;
- our index providers ability to perform under our agreements;
- our ability to operate our business without violating the intellectual property rights of others and the costs associated with protecting our intellectual property rights;
- our ability to accommodate trading volume and transaction traffic, including significant increases, without failure or degradation of performance of our systems;
- our ability to protect our systems and communication networks from security risks, including cyber-attacks;
- the accuracy of our estimates and expectations;
- economic, political and market conditions;
- our ability to maintain access fee revenues;
- our ability to meet our compliance obligations, including managing potential conflicts between our regulatory responsibilities and our for-profit status;
- our ability to attract and retain skilled management and other personnel;
- our ability to manage our growth effectively; and
- the ability of our compliance and risk management methods to effectively monitor and manage our risks.

We caution you not to place undue reliance on the forward-looking statements, which speak only as of the date of this filing. We undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements (Unaudited)

CBOE Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Income
Three Months Ended March 31, 2015 and 2014

(in thousands, except per share amounts)	Three Months Ended March 31, 2015 (unaudited)	2014
Operating Revenues:		
Transaction fees	$98,723	$112,790
Access fees	13,686	15,232
Exchange services and other fees	9,728	9,492
Market data fees	8,012	7,158
Regulatory fees	8,382	9,857
Other revenue	4,308	3,356
Total Operating Revenues	142,839	157,885
Operating Expenses:		
Compensation and benefits	25,439	33,374
Depreciation and amortization	10,402	8,604
Technology support services	5,325	4,721
Professional fees and outside services	11,950	7,378
Royalty fees	14,150	15,902
Order routing	787	1,126
Travel and promotional expenses	2,501	1,987
Facilities costs	1,384	1,313
Other expenses	1,348	1,442
Total Operating Expenses	73,286	75,847
Operating Income	69,553	82,038
Other Income/(Expense):		
Investment income	51	14
Net loss from investment in affiliates	(81)	(509)
Impairment of advance to affiliate	(246)	—
Total Other Income/(Expense)	(276)	(495)
Income Before Income Taxes	69,277	81,543
Income tax provision	27,018	32,519
Net Income	42,259	49,024
Net Income Allocated to Participating Securities	(180)	(496)
Net Income Allocated to Common Stockholders	$42,079	$48,528
Net Income Per Share Allocated to Common Stockholders:		
Basic	$0.50	$0.56
Diluted	0.50	0.56
Weighted average shares used in computing income per share:		
Basic	83,956	86,453
Diluted	83,956	86,453

See notes to condensed consolidated financial statements

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CBOE Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Comprehensive Income
Three Months Ended March 31, 2015 and 2014

	Three Months Ended March 31,	
(in thousands)	2015	2014
	(unaudited)	
Net Income	$42,259	$49,024
Comprehensive Income (Loss) - net of tax:		
Post-retirement benefit obligation	(181)	315
Comprehensive Income	42,078	49,339
Comprehensive Income allocated to participating securities	(180)	(496)
Comprehensive Income allocated to common stockholders	$41,898	$48,843

See notes to condensed consolidated financial statements

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CBOE Holdings, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
March 31, 2015 and December 31, 2014

(in thousands, except share amounts)	March 31, 2015 (unaudited)	December 31, 2014
Assets		
Current Assets:		
Cash and cash equivalents	$137,558	$147,927
Accounts receivable—net allowances of 2015 - $298 and 2014 - $285	51,986	58,386
Marketing fee receivable	8,789	10,697
Income taxes receivable	1,120	21,503
Other prepaid expenses	8,588	4,622
Other current assets	1,344	972
Total Current Assets	209,385	244,107
Investments in and Advances to Affiliates	42,740	12,351
Land	4,914	4,914
Property and Equipment:		
Construction in progress	—	—
Building	68,117	68,019
Furniture and equipment	285,223	286,723
Less accumulated depreciation and amortization	(290,615)	(287,886)
Total Property and Equipment—Net	62,725	66,856
Other Assets:		
Software development work in progress	11,337	7,817
Data processing software and other assets (less accumulated amortization—2015, $167,925; 2014, $163,486)	44,696	47,856
Total Other Assets—Net	56,033	55,673
Total	$375,797	$383,901
Liabilities and Stockholders' Equity		
Current Liabilities:		
Accounts payable and accrued liabilities	$44,593	$58,566
Marketing fee payable	9,320	11,236
Deferred revenue and other liabilities	14,073	1,988
Post-retirement benefit obligation - current	72	101
Income tax payable	2,654	1,774
Total Current Liabilities	70,712	73,665
Long-term Liabilities:		
Post-retirement benefit obligation - long-term	1,938	1,612
Income tax liability	41,932	40,683
Other long-term liabilities	3,312	4,197
Deferred income taxes	14,168	13,677
Total Long-term Liabilities	61,350	60,169
Commitments and Contingencies		
Total Liabilities	132,062	133,834
Stockholders' Equity:		
Preferred stock, $0.01 par value: 20,000,000 shares authorized, no shares issued and outstanding at March 31, 2015 or December 31, 2014	—	—
	927	926

Unrestricted common stock, $0.01 par value: 325,000,000 shares authorized; 92,717,568 issued and 83,701,811 outstanding at March 31, 2015; 92,569,189 issued and 84,114,475 outstanding at December 31, 2014		
Additional paid-in-capital	113,960	110,112
Retained earnings	496,539	472,005
Treasury stock at cost – 9,015,757 shares at March 31, 2015 and 8,454,714 shares at December 31, 2014	(366,821)	(332,287)
Accumulated other comprehensive loss	(870)	(689)
Total Stockholders' Equity	243,735	250,067
Total	$375,797	$383,901

See notes to condensed consolidated financial statements

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CBOE Holdings, Inc. and Subsidiaries
Condensed Consolidated Statement of Stockholders' Equity
Three Months Ended March 31, 2015
(Unaudited)

(in thousands)	Preferred Stock	Unrestricted Common Stock	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance—January 1, 2015	$—	$926	$110,112	$472,005	$(332,287)	$ (689)	$ 250,067
Cash dividends on common stock				(17,725)			(17,725)
Stock-based compensation			2,655				2,655
Excess tax benefits from stock-based compensation plan			1,194				1,194
Issuance of vested restricted stock granted to employees		1	(1)				—
Purchase of unrestricted common stock from employees to fulfill employee tax obligations					(3,119)		(3,119)
Purchase of unrestricted stock under announced program					(31,415)		(31,415)
Net income				42,259			42,259
Post-retirement benefit obligation adjustment—net of tax benefit $110						(181)	(181)
Balance—March 31, 2015	$—	$927	$113,960	$496,539	$(366,821)	$ (870)	$ 243,735

See notes to condensed consolidated financial statements

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CBOE Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
Three Months Ended March 31, 2015 and 2014

	Three Months Ended	
(in thousands)	March 31, 2015	March 31, 2014
	(unaudited)	
Cash Flows from Operating Activities:		
Net income	$42,259	$49,024
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	10,402	8,604
Other amortization	11	18
Provision for deferred income taxes	601	25
Stock-based compensation	2,655	6,913
Loss on disposition of property	170	253
(Gain)/Loss on investment in affiliate	(37)	509
Impairment of investment in affiliate	118	—
Change in assets and liabilities:		
Accounts receivable	6,154	(7,968)
Marketing fee receivable	1,908	(1,307)
Income taxes receivable	20,383	21,307
Prepaid expenses	(3,966)	(3,264)
Other current assets	(372)	1,795
Accounts payable and accrued expenses	(13,239)	(12,342)
Marketing fee payable	(1,916)	1,301
Deferred revenue and other liabilities	11,200	13,045
Post-retirement benefit obligations	(5)	(7)
Income tax liability	1,249	2,346
Income tax payable	880	8,064
Net Cash Flows provided by Operating Activities	78,455	88,316
Cash Flows from Investing Activities:		
Capital and other assets expenditures	(7,536)	(12,172)
Investment in and advances to affiliates	(30,469)	(500)
Other	246	—
Net Cash Flows used in Investing Activities	(37,759)	(12,672)
Cash Flows from Financing Activities:		
Payment of quarterly dividends	(17,725)	(15,727)
Payment of special dividend	—	(43,831)
Excess tax benefit from stock-based compensation	1,194	765
Purchase of unrestricted common stock from employees	(3,119)	(1,990)
Purchase of unrestricted common stock under announced program	(31,415)	(37,137)
Net Cash Flows used in Financing Activities	(51,065)	(97,920)
Net Decrease in Cash and Cash Equivalents	(10,369)	(22,276)
Cash and Cash Equivalents at Beginning of Period	147,927	221,341
Cash and Cash Equivalents at End of Period	$137,558	$199,065
Supplemental Disclosure of Cash Flow Information		
Cash paid for income taxes	$2,695	$10
Non-cash activities:		
Unpaid liability to acquire equipment and software	2,034	3,835

See notes to condensed consolidated financial statements

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CBOE HOLDINGS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
For the three months ended March 31, 2015 and 2014
(Unaudited)

NOTE 1 —DESCRIPTION OF BUSINESS
CBOE Holdings, Inc. is the holding company for Chicago Board Options Exchange, Incorporated, CBOE Futures Exchange, LLC, C2 Options Exchange, Incorporated and other subsidiaries.
The Company's principal business is operating markets that offer for trading options on various market indexes (index options) and futures contracts, mostly on an exclusive basis, as well as on non-exclusive "multiply-listed" options, such as options on the stocks of individual corporations (equity options) and options on other exchange-traded products (ETP options), such as exchange-traded funds (ETF options) and exchange-traded notes (ETN options). The Company operates three stand-alone exchanges, but reports the results of its operations in one reporting segment.
CBOE is our primary options market and offers trading in listed options through a single system that integrates electronic trading and traditional open outcry trading on our trading floor in Chicago. This integration of electronic trading and traditional open outcry trading into a single exchange is known as our Hybrid trading model. CFE, our all-electronic futures exchange, offers trading of futures on the VIX Index and other products. C2 is our all-electronic exchange that also offers trading for listed options, and may operate with a different market model and fee structure than CBOE. All of our exchanges operate on our proprietary technology platform known as CBOE Command.
Recent Accounting Pronouncements

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers. This standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. In addition, the ASU provides guidance on accounting for certain revenue-related costs including when to capitalize costs associated with obtaining and fulfilling a contract. ASU 2014-09 provides companies with two implementation methods. Companies can choose to apply the standard retrospectively to each prior reporting period presented (full retrospective application) or retrospectively with the cumulative effect of initially applying the standard as an adjustment to the opening balance of retained earnings of the annual reporting period that includes the date of initial application (modified retrospective application). This guidance is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. On April 1, 2015, the FASB proposed deferring the effective date by one year to December 15, 2017 for annual reporting periods beginning after that date. The FASB also proposed permitting early adoption of the standard, but not before the original effective date of December 15, 2016. The Company is in the process of evaluating this guidance, though we do not expect it will materially impact our consolidated balance sheets, statements of income, comprehensive income or cash flows.

NOTE 2 — BASIS OF PRESENTATION

These interim unaudited condensed consolidated financial statements have been prepared in accordance with GAAP for interim financial information and with the instructions to Form 10-Q and should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company’s Annual Report on Form 10-K for the year ended December 31, 2014.

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities and reported amounts of revenues and expenses. On an ongoing basis, management evaluates its estimates based upon historical experience, observance of trends, information available from outside sources and various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different conditions or assumptions.

In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of financial position, results of operations and cash flows at the dates and for the periods presented have been included.

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The results of operations for interim periods are not necessarily indicative of the results of operations for the full year.

We have updated certain line item descriptions on our condensed consolidated statement of income. The table below highlights the changes:

Prior description	Current description
Employee costs	Compensation and benefits
Data processing	Technology support services
Outside services	Professional fees and outside services
Trading volume incentives	Order routing

Excluding the change in line item descriptions, there have been no other material changes in the manner or basis for presenting the items.

NOTE 3 — SHARE REPURCHASE PROGRAM

In 2011, the board of directors approved an initial authorization for the Company to repurchase shares of its outstanding unrestricted common stock of $100 million and approved additional authorizations of $100 million in each of 2012, 2013 and 2014 for a total authorization of $400 million. The program permits the Company to purchase shares through a variety of methods, including in the open market or through privately negotiated transactions, in accordance with applicable securities laws. It does not obligate the Company to make any repurchases at any specific time or situation.

Under the program, for the three months ended March 31, 2015, the Company repurchased 510,951 shares of unrestricted common stock at an average cost per share of $61.48, totaling $31.4 million.

Since inception of the program through March 31, 2015, the Company has repurchased 8,366,021 shares of unrestricted common stock at an average cost per share of $40.85, totaling $341.8 million.

NOTE 4 — NET INCOME PER COMMON SHARE

The computation of basic net income allocated to common stockholders is calculated by reducing net income for the period by dividends paid or declared and undistributed net income for the period that are allocated to participating securities to arrive at net income allocated to common stockholders. Net income allocated to common stockholders is divided by the weighted average number of common shares outstanding during the period to determine net income per share allocated to common stockholders.

The computation of diluted earnings per share is calculated by dividing net income allocated to common stockholders by the sum of the weighted average number of common shares outstanding plus all additional common shares that would have been outstanding if the potentially dilutive common shares had been issued. The dilutive effect is calculated using the more dilutive of the two-class or treasury stock method.

The following table reconciles net income allocated to common stockholders and the number of shares used to calculate the basic and diluted net income per common share for the three months ended March 31, 2015 and 2014:

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	Three Months Ended March 31,	
(in thousands, except per share amounts)	2015	2014
Basic EPS Numerator:		
Net Income	$42,259	$49,024
Less: Earnings allocated to participating securities	(180)	(496)
Net Income allocated to common stockholders	$42,079	$48,528
Basic EPS Denominator:		
Weighted average shares outstanding	83,956	86,453
Basic net income per common share	$0.50	$0.56
Diluted EPS Numerator:		
Net Income	$42,259	$49,024
Less: Earnings allocated to participating securities	(180)	(496)
Net Income allocated to common stockholders	$42,079	$48,528
Diluted EPS Denominator:		
Weighted average shares outstanding	83,956	86,453
Dilutive common shares issued under restricted stock program	—	—
Diluted net income per common share	$0.50	$0.56

For the periods presented, the Company did not have shares of restricted stock or restricted stock units that would have an anti-dilutive effect on the computation of diluted net income per common share.

NOTE 5 — STOCK-BASED COMPENSATION

Stock-based compensation is based on the fair value of the award on the date of grant, which is recognized over the related service period, net of estimated forfeitures. The service period is the period over which the related service is performed, which is generally the same as the vesting period.

On February 19, 2015, the Company granted 158,661 restricted stock units ("RSUs"), each of which entitles the holders to one share of common stock upon vesting, to certain officers and employees at a fair value of $61.96 per share. The RSUs vest ratably over three years, with one-third vesting on each anniversary of the grant date, and vesting accelerates upon the occurrence of a change in control. Unvested restricted stock units will be forfeited if the officer or employee leaves the company prior to the applicable vesting date, except in limited circumstances. The restricted stock units have no voting rights but are able to participate in the payment of dividends.

In addition, on February 19, 2015, the Company granted 45,932 RSUs contingent on the achievement of performance conditions including 22,966 RSUs, at a fair value of $61.96 per RSU, related to earnings per share during the performance period and 22,966 RSUs, at a fair value of $74.00 per RSU, related to total shareholder return during the performance period. The Company used the Monte Carlo valuation model method to estimate the fair value of the total shareholder return RSUs which incorporated the following assumptions: risk free interest rate (1.02%), three-year volatility (19.9%) and three-year correlation with S&P 500 Index (0.44). Each of these performance shares has a performance condition under which the number of units ultimately awarded will vary from 0% to 200% of the original grant, with each unit representing the contingent right to receive one share of our common stock. The vesting period for the shares contingent on the achievement of performance is three years. For each of the performance awards, the restricted stock units will be settled in shares of our common stock following vesting of the restricted stock unit assuming that the participant has been continuously employed during the vesting period, subject to acceleration in the event of a change of control of the Company or in the event of a participant’s earlier death or disability. Participants shall have no voting rights with respect to shares until the issuance of the shares of stock. Dividends are accrued by the Company and will be paid once the RSUs contingent on the achievement of performance conditions vest.

For the three months ended March 31, 2015 and 2014, the Company recognized $2.7 million and $6.9 million in stock-based compensation expense, respectively. The three months ended March 31, 2014 included $2.5 million of accelerated stock-based compensation expense for certain executives due to provisions contained in their employment arrangements. Stock-based compensation expense is included in employee costs in the condensed consolidated statements of income.

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As of March 31, 2015, the Company had unrecognized stock-based compensation of $22.7 million. The remaining unrecognized stock-based compensation is expected to be recognized over a weighted average period of 27.4 months.

The activity in the Company's restricted stock and restricted stock units for the three months ended March 31, 2015 was as follows:

	Number of Shares	Weighted Average Grant-Date Fair Value
Unvested at January 1, 2015	414,749	$46.44
Granted	204,593	63.31
Vested	(148,864)	41.78
Forfeited	(732)	52.97
Unvested at March 31, 2015	469,746	$48.29

NOTE 6 — INVESTMENTS IN AND ADVANCES TO AFFILIATES

At March 31, 2015 and December 31, 2014, the investments in affiliates were composed of the following (in thousands):

	March 31, 2015	December 31, 2014
Investment in OCC	$333	$333
Advance to OCC (1)	30,000	—
Investment in Signal Trading Systems, LLC	12,407	11,900
Investment in IPXI Holdings, LLC (2)	—	118
Investment in CBOE Stock Exchange, LLC (3)	—	—
Investments in and Advances to Affiliates	$42,740	$12,351

(1) In December 2014, OCC announced a newly formed capital plan. The OCC capital plan was designed to strengthen OCC's capital base and facilitate its compliance with proposed SEC regulations for Systemically Important Financial Market Utilities (SIFMUs) as well as international standards applicable to financial market infrastructures. On February 26, 2015, the SEC issued a notice of no objection to OCC's advance notice filing regarding the capital plan, and OCC and OCC's existing exchange stockholders, which include CBOE, subsequently executed agreements effecting the capital plan. Under the plan, each of OCC's existing exchange stockholders agreed to contribute its pro-rata share, based on ownership percentage, of $150 million in equity capital, which would increase OCC's shareholders' equity, and to provide its pro rata share in replenishment capital, up to a maximum of $40 million, if certain capital thresholds are breached. On March 3, 2015, in accordance with the plan, CBOE contributed $30 million to OCC. On March 6, 2015, OCC informed CBOE that the SEC had approved OCC's proposed rule filing for the capital plan. The SEC approval order was stayed on March 13, 2015 automatically as a result of the initiation of petitions to review the order. OCC has filed a motion to lift the automatic stay. If the plan does not go forward, OCC will return each exchange stockholder's capital contribution with interest. The contribution has been recorded under investments in and advances to affiliates in the balance sheet at March 31, 2015.

(2) IPXI Holdings, LLC ceased operations on March 23, 2015.

(3) CBOE Stock Exchange, LLC ceased trading operations on April 30, 2014.

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NOTE 7 — ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

At March 31, 2015 and December 31, 2014, accounts payable and accrued liabilities consisted of the following (in thousands):

	March 31, 2015	December 31, 2014
Compensation and benefit-related liabilities (1)	$8,014	$23,032
Royalties	12,315	17,624
Contract services (2)	7,488	2,335
Accounts payable	2,800	2,779
Purchase of unrestricted common stock (3)	2,246	1,159
Facilities	1,482	1,942
Legal	1,687	1,355
Market linkage	1,179	1,183
Other	7,382	7,157
Total	$44,593	$58,566

(1) For the period ended March 31, 2015, primarily reflects costs for 2015 incentive compensation expense and self-insurance expenses. Prior year primarily reflects 2014 annual incentive compensation expense which was paid in the first quarter of 2015.

(2) Reflects costs primarily for certain regulatory functions and contract programming work related to projects that are in process. For comparability purposes, contract services balances previously reflected in other as of December 31, 2014 have been included on this line.

(3) Reflects shares purchased at the end of the period that are not settled until three trading days after the trade occurs.

NOTE 8 — MARKETING FEE

CBOE facilitates the collection and payment of marketing fees assessed on certain trades taking place at CBOE. Funds resulting from the marketing fees are made available to Designated Primary Market Makers and Preferred Market Makers as an economic inducement to route orders to CBOE. Pursuant to ASC 605-45, Revenue Recognition—Principal Agent Considerations, the Company reflects the assessments and payments on a net basis, with no impact on revenues or expenses.

As of March 31, 2015 and December 31, 2014, amounts assessed by the Company on behalf of others included in current assets totaled $8.8 million and $10.7 million, respectively, and payments due to others included in current liabilities totaled $9.3 million and $11.2 million, respectively.

NOTE 9 — DEFERRED REVENUE

The following table summarizes the activity in deferred revenue for the three months ended March 31, 2015 (in thousands):

	Balance at December 31, 2014	Cash Additions	Revenue Recognition	Balance at March 31, 2015
Other – net	$1,988	$4,050	$(2,765)	$3,273

Liquidity provider sliding scale (1)	—	14,400	(3,600)	10,800
Total deferred revenue	$1,988	$18,450	$(6,365)	$14,073

(1) Liquidity providers are eligible to participate in the sliding scale program, which involves prepayment of transaction fees, and receive reduced fees based on the achievement of certain volume thresholds within a calendar month. The prepayment of 2015 transaction fees totaled $14.4 million. This amount is amortized and recorded ratably, as transaction fees, over the respective twelve month period.

NOTE 10 — EMPLOYEE BENEFITS

Employees are eligible to participate in the Chicago Board Options Exchange SMART Plan ("SMART Plan"). The SMART Plan is a defined contribution plan, which is qualified under Internal Revenue Code Section 401(k). In addition, eligible employees may participate in the Supplemental Employee Retirement Plan, Executive Retirement Plan and Deferred Compensation Plan. Each plan is a defined contribution plan that is non-qualified under Internal Revenue Code. The Company contributed $1.1 million and $1.4 million to the defined contribution plans for the three months ended March 31, 2015 and 2014, respectively.

The Company has a post-retirement medical plan for former members of senior management. The Company recorded immaterial post-retirement benefits expense for the three months ended March 31, 2015 and 2014.

NOTE 11 — INCOME TAXES

For the three months ended March 31, 2015 and 2014, the Company recorded income tax provisions of $27.0 million and $32.5 million, respectively. The effective tax rate for the three months ended March 31, 2015 and 2014 was 39.0% and 39.9%, respectively. The decrease in the effective tax rate for the three months ended March 31, 2015 primarily resulted from the recognition of a discrete tax charge in 2014, which accounted for the higher effective tax rate versus the first quarter of 2015.

As of March 31, 2015 and December 31, 2014, the Company had $35.8 million and $35.4 million, respectively, of uncertain tax positions excluding interest and penalties, which, if recognized in the future, would affect the annual effective income tax rate. Reductions to uncertain tax positions primarily from the lapse of the applicable statutes of limitations during the next twelve months are estimated to be approximately $10.5 million, not including any potential new additions.

Estimated interest costs and penalties, which are classified as part of the provision for income taxes in the Company's condensed consolidated statements of income, were $0.9 million and $0.6 million for the three months ended March 31, 2015 and 2014, respectively. Accrued interest and penalties were $6.1 million and $5.3 million as of March 31, 2015 and December 31, 2014, respectively.

The Company is subject to U.S. federal tax, Illinois, New Jersey, and New York state taxes and Washington, D.C. taxes, as well as taxes in other local jurisdictions. The Company has open tax years from 2007 on for New York, 2008 on for Federal, 2010 on for New Jersey, 2011 on for Washington, D.C and 2013 on for Illinois. The Internal Revenue Service is currently auditing 2010 and is looking at specific line items from 2008 to 2013 due to the filing by the Company of amended returns containing the recognition of certain credits and deductions. The New York State Department of Taxation and Finance is currently auditing the 2007 through 2012 tax years and the New Jersey Division of Taxation is currently auditing the 2010 through 2012 tax years.

NOTE 12 — FAIR VALUE MEASUREMENTS

Fair value is the price that would be received upon the sale of an asset or paid upon the transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity. In addition, the fair value of liabilities should include consideration of non-performance risk, including the Company's own credit risk.

The Company applied FASB ASC 820, Fair Value Measurement and Disclosure (formerly, FASB Statement No. 157, Fair Value Measurements), which provides guidance for using fair value to measure assets and liabilities by defining fair value and establishing the framework for measuring fair value. ASC 820 applies to financial and non-financial instruments that are measured and reported on a fair value basis. The three-level hierarchy of fair value measurements is based on whether the inputs to those measurements are observable or unobservable. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company’s market assumptions. The fair-value hierarchy requires the use of observable market data when available and consists of the following levels:

- Level 1—Unadjusted inputs based on quoted markets for identical assets or liabilities.
- Level 2—Observable inputs, either direct or indirect, not including Level 1, corroborated by market data or based upon quoted prices in non-active markets.

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- Level 3—Unobservable inputs that reflect management’s best assumptions of what market participants would use in valuing the asset or liability.

The Company has included a tabular disclosure for financial assets that are measured at fair value on a recurring basis in the condensed consolidated balance sheet as of March 31, 2015 and December 31, 2014. The Company holds no financial liabilities that are measured at fair value on a recurring basis.

(amounts in thousands)	Level 1	Level 2	Level 3	Total
Assets at fair value:				
Money market funds	$123,000	$—	$—	$123,000
Total assets at fair value at March 31, 2015	$123,000	$—	$—	$123,000

(amounts in thousands)	Level 1	Level 2	Level 3	Total
Assets at fair value:				
Money market funds	$135,000	$—	$—	$135,000
Total assets at fair value at December 31, 2014	$135,000	$—	$—	$135,000

Our investment and equity interest in IPXI as of December 31, 2014 were valued at $0.1 million and approximately 5.0%, respectively. On March 23, 2015, IPXI ceased operations. In the three months ended March 31, 2015, we recorded an impairment of $0.1 million which represented our remaining investment balance.

NOTE 13 — LEGAL PROCEEDINGS

As of March 31, 2015, the end of the period covered by this report, the Company was subject to various legal proceedings and claims, as well as certain other legal proceedings and claims that have not been fully resolved and that have arisen in the ordinary course of business. For a description of each of these proceedings, please see Note 11 to our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2014.

The Company reviews its legal proceedings and claims, regulatory reviews and inspections and other legal proceedings on an ongoing basis and follows appropriate accounting guidance when making accrual and disclosure decisions. The Company establishes accruals for those contingencies where the incurrence of a loss is probable and can be reasonably estimated, and we disclose the amount accrued and the amount of a reasonably possible loss in excess of the amount accrued, if such disclosure is necessary for our financial statements to not be misleading. The Company does not record liabilities when the likelihood that the liability has been incurred is probable, but the amount cannot be reasonably estimated, or when the liability is believed to be only reasonably possible or remote. The Company's assessment of whether a loss is reasonably possible or probable is based on its assessment of the ultimate outcome of the matter following all appeals.

Estimates of probable losses resulting from patent litigation involving the Company are inherently difficult to make, particularly when the Company's view of the case is significantly different than that expressed by the plaintiff. The Company has not recorded a liability related to damages in connection with these matters.

As of March 31, 2015, the Company does not believe that there is a reasonable possibility that any material loss exceeding the amounts already recognized for these reviews, inspections or other legal proceedings, if any, has been incurred. While the consequences of certain unresolved proceedings are not presently determinable, the outcome of any litigation is inherently uncertain and an adverse outcome from certain matters could have a material effect on our earnings in any given reporting period. However, in the opinion of management, the ultimate liability is not expected to have a material effect on our financial position, liquidity or capital resources.

The following information updates the legal proceedings disclosures in our Annual Report on Form 10-K for the year ended December 31, 2014.

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ISE -- QRM

On November 12, 2012, CBOE brought suit against International Securities Exchange, LLC ("ISE") in the United States District Court for the Northern District of Illinois alleging that ISE infringes three of its patents (United States Patent Nos. 7,356,498; 7,980,457; and 8,266,044 (the “QRM patents”)) related to quote risk monitor ("QRM") technology. CBOE has requested injunctive relief and monetary damages. On February 20, 2013, the court ruled that the case be transferred to the United States District Court for the Southern District of New York. On October 31, 2013, the court stayed the litigation pending resolution of Covered Business Method ("CBM") Patent Reviews at the United States Patent and Trademark Office ("USPTO") that ISE had petitioned for. On March 4, 2014, the USPTO instituted CBM Patent Reviews on CBOE’s three QRM patents. On May 22, 2014, the USPTO instituted Inter Parties Review (“IPR”) Proceedings, which ISE had petitioned for, on some but not all claims of two of CBOE’s QRM patents (United States Patent Nos. 7,356,498 and 7,980,457). On March 2, 2015, the USPTO ruled in the CBM proceedings, finding that the subject matter of the patents is not eligible for patent protection, and in the IPR proceedings, finding for CBOE that the claims were not invalidated by the asserted prior art. On April 30, 2015, ISE filed notice of its appeal of the IPR decisions, and on May 1, 2015, CBOE filed notice of its appeal of the CBM decisions. The appeals will be handled by the United States Court of Appeals for the Federal Circuit.

Lanier Litigation

On May 23, 2014, Harold R. Lanier sued 14 securities exchanges, including CBOE, in the United States District Court for the Southern District of New York on behalf of himself and a putative class consisting of all persons in the United States who entered into contracts to receive market data through certain data plans at any time since May 19, 2008 to the present. The complaint alleged that the market data provided under the CQ Plan and CTA Plans was inferior to the data that the exchanges provided to those that directly receive other data from the exchanges, which the plaintiffs alleged is a breach of their “subscriber contracts” and a violation of the exchanges’ obligations under the CQ and CTA Plans. The plaintiffs sought monetary and injunctive relief. On May 30, 2014, Mr. Lanier filed two additional suits in the same Court, alleging substantially the same claims and requesting the same types of relief against the exchanges who participate in the UTP and the OPRA data plans. CBOE was a defendant in each of these suits, while C2 was only a defendant in the suit regarding the OPRA Plan. On April 28, 2015, the Court dismissed Lanier’s complaint with prejudice because it was preempted by the federal regulatory scheme and because the claims were precluded by the terms of the applicable subscriber agreements.

NOTE 14 — SUBSEQUENT EVENTS

On April 29, 2015, the Company announced that its board of directors declared a quarterly cash dividend of $0.21 per share. The dividend is payable June 19, 2015 to stockholders of record at the close of business on May 29, 2015.

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CBOE HOLDINGS, INC. AND SUBSIDIARIES

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

The following discussion should be read in conjunction with the accompanying unaudited condensed consolidated financial statements and the notes thereto, included in Item 1 in this Quarterly Report on Form 10-Q, and the audited consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2014, and as contained in that report, the information under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations." This discussion contains forward-looking information. Please see "Forward-Looking Statements" for a discussion of the uncertainties, risks and assumptions associated with these statements.

RESULTS OF OPERATIONS

Three months ended March 31, 2015 compared to the three months ended March 31, 2014

Overview

The following summarizes our financial performance for the three months ended March 31, 2015 compared to the same period in 2014.

	2015	2014	Inc./(Dec.)	Percent Change
	(in millions, except per share amounts)			
Total Operating Revenues	$142.8	$157.9	$(15.1)	(9.5)%
Total Operating Expenses	73.3	75.9	(2.6)	(3.4)%
Operating Income	69.5	82.0	(12.5)	(15.2)%
Total Other Income/(Expense)	(0.3)	(0.5)	0.2	(44.2)%
Income Before Income Taxes	69.2	81.5	(12.3)	(15.1)%
Income tax provision	27.0	32.5	(5.5)	(16.9)%
Net Income	$42.2	$49.0	$(6.8)	(13.9)%
Net Income Allocated to Common Stockholders	$42.1	$48.5	$(6.4)	(13.3)%
Operating Margin	48.7%	52.0%		
Net income percentage	29.6%	31.0%		
Diluted Net Income Per Share Allocated to Common Stockholders	$0.50	$0.56		

- Total operating revenues decreased primarily due to lower transaction fees, resulting from lower trading volume. Additionally, we experienced lower access fees and regulatory fees, partially offset by higher market data fees.

- Total operating expenses decreased primarily due to lower compensation and benefits and royalty fees, partially offset by higher depreciation and amortization and professional fees and outside services.

Operating Revenues

Total operating revenues for the three months ended March 31, 2015 were $142.8 million, a decrease of $15.1 million, or 9.5%, compared with the same period in 2014. The following summarizes changes in total operating revenues for the three months ended March 31, 2015 compared to the same period in 2014.

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	2015	2014	Inc./(Dec.)	Percent Change
		(in millions)		
Transaction fees	$98.7	$112.8	$(14.1)	(12.5)%
Access fees	13.7	15.2	(1.5)	(10.1)%
Exchange services and other fees	9.7	9.5	0.2	2.5%
Market data fees	8.0	7.1	0.9	11.9%
Regulatory fees	8.4	9.9	(1.5)	(15.2)%
Other revenue	4.3	3.4	0.9	28.4%
Total Operating Revenues	$142.8	$157.9	$(15.1)	(9.5)%

Transaction Fees

Transaction fees decreased 12.5% to $98.7 million for the three months ended March 31, 2015, compared with $112.8 million for the same period in 2014. The decrease was due to a 15.2% decrease in total trading volume, partially offset by an increase in average revenue per contract of 3.3%. The increase in average revenue per contract resulted primarily from certain fee changes implemented in 2015, partially offset by a shift in the mix of products. As a percent of total trading volume, index options and futures contracts, which generated our highest options and overall average revenue per contract, accounted for 33.3% of trading volume during the first quarter of 2015 down from 34.7% in the first quarter of 2014. This shift primarily resulted from trading volume decreases of 45.1% and 7.7% in VIX options and VIX futures, respectively, which is partially offset by a 1.3% increase SPX options.

Average revenue per contract, discussed in more detail below, is impacted by our fee structure, which includes volume based incentive programs, mix of products traded, the account type (customer, firm, market-maker, etc.) and the manner in which a trade is executed (electronic, open-outcry, etc.). The implementation of fee changes, which may increase or decrease our average revenue per contract, is primarily to ensure that we are competitive in the options marketplace and to ultimately improve and continue to drive order flow to our exchanges. We cannot predict the trading patterns of exchange participants, which may be based on factors outside our control, but we can attempt to price our products at levels that are competitive in our market.

Trading volume is impacted by many factors, including: macroeconomic events, market volatility, regulatory actions or considerations, availability of capital, competition and pricing.

The following summarizes transaction fees by product category for the three months ended March 31, 2015 compared to the same period in 2014.

	2015	2014	Inc./(Dec.)	Percent Change
		(in millions)		
Equities	$8.5	$10.7	$(2.2)	(20.1)%
Indexes	60.8	71.3	(10.5)	(14.7)%
Exchange-traded products	9.9	10.8	(0.9)	(7.9)%
Total options transaction fees	79.2	92.8		