

VIRTUS INVESTMENT PARTNERS, INC.

Form 10-Q

November 07, 2014

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

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

**For the quarterly period ended September 30, 2014**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number: 001-10994**

**VIRTUS INVESTMENT PARTNERS, INC.**

**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or other jurisdiction of**  
**incorporation or organization)**  
**100 Pearl St., Hartford, CT 06103**  
**(Address of principal executive offices) (Zip Code)**  
**(800) 248-7971**  
**(Registrant's telephone number, including area code)**

**95-4191764**  
**(I.R.S. Employer**  
**Identification No.)**

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 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 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

The number of shares outstanding of the registrant's common stock was 9,059,976 as of October 27, 2014.

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We, us, our, the Company and Virtus as used in this Quarterly Report on Form 10-Q, refer to Virtus Investment Partners, Inc., a Delaware corporation, and its subsidiaries.

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements****Virtus Investment Partners, Inc.****Condensed Consolidated Balance Sheets****(Unaudited)**

|  | <b>September 30,<br/>2014</b> | <b>December 31,<br/>2013</b> |
|--|-------------------------------|------------------------------|
| <i>(\$ in thousands, except share data)</i>  |                               |                              |
| <b>Assets:</b>   |                               |                              |
| Cash and cash equivalents  | \$ 172,709                    | \$ 271,014                   |
| Cash of consolidated sponsored investment products   | 1,055                         | 531                          |
| Cash pledged or on deposit of consolidated sponsored investment products   | 12,492                        |                              |
| Investments  | 63,659                        | 37,258                       |
| Investments of consolidated sponsored investment products  | 241,107                       | 139,054                      |
| Accounts receivable, net   | 53,045                        | 50,166                       |
| Furniture, equipment, and leasehold improvements, net  | 7,291                         | 7,219                        |
| Intangible assets, net   | 42,710                        | 44,633                       |
| Goodwill   | 5,260                         | 5,260                        |
| Deferred taxes, net  | 59,668                        | 64,500                       |
| Other assets   | 28,249                        | 15,724                       |
| Other assets of consolidated sponsored investment products   | 8,756                         | 9,595                        |
| Total assets   | \$ 696,001                    | \$ 644,954                   |
| <b>Liabilities and Equity</b>  |                               |                              |
| <b>Liabilities:</b>  |                               |                              |
| Accrued compensation and benefits  | \$ 42,924                     | \$ 53,140                    |
| Accounts payable and accrued liabilities   | 33,389                        | 29,912                       |
| Dividends payable  | 4,229                         |                              |
| Other liabilities  | 8,926                         | 18,413                       |
| Liabilities of consolidated sponsored investment products  | 23,838                        | 8,435                        |
| Total liabilities  | 113,306                       | 109,900                      |
| <b>Commitments and Contingencies (Note 11)</b>   |                               |                              |
| Redeemable noncontrolling interests  | 22,265                        | 42,186                       |
| <b>Equity:</b>   |                               |                              |
| <b>Equity attributable to stockholders:</b>  |                               |                              |
| Common stock, \$0.01 par value, 1,000,000,000 shares authorized; 9,546,252 shares issued and 9,059,378 shares outstanding at September 30, 2014 and 9,455,521 shares issued and 9,105,521 shares outstanding at December 31, | 95                            | 95                           |

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|   |            |            |
|---|------------|------------|
| 2013  |            |            |
| Additional paid-in capital  | 1,150,716  | 1,135,644  |
| Accumulated deficit   | (526,400)  | (605,221)  |
| Accumulated other comprehensive loss  | (140)      | (150)      |
| Treasury stock, at cost, 486,874 shares at September 30, 2014 and 350,000 shares at December 31, 2013 | (63,695)   | (37,438)   |
| Total equity attributable to stockholders   | 560,576    | 492,930    |
| Noncontrolling interests  | (146)      | (62)       |
| Total equity  | 560,430    | 492,868    |
| Total liabilities and equity  | \$ 696,001 | \$ 644,954 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

**Table of Contents****Virtus Investment Partners, Inc.****Condensed Consolidated Statements of Operations****(Unaudited)**

|   | <b>Three Months Ended</b> |                | <b>Nine Months Ended</b> |                |
|---|---------------------------|----------------|--------------------------|----------------|
|   | <b>September 30,</b>      |                | <b>September 30,</b>     |                |
|   | <b>2014</b>               | <b>2013</b>    | <b>2014</b>              | <b>2013</b>    |
| <i>(\$ in thousands, except per share data)</i>   |                           |                |                          |                |
| <b>Revenues</b>   |                           |                |                          |                |
| Investment management fees  | \$ 78,960                 | \$ 67,119      | \$ 225,289               | \$ 189,371     |
| Distribution and service fees   | 23,671                    | 20,322         | 70,049                   | 57,007         |
| Administration and transfer agent fees  | 14,804                    | 12,492         | 41,819                   | 35,248         |
| Other income and fees   | 406                       | 476            | 1,304                    | 1,091          |
| <b>Total revenues</b>   | <b>117,841</b>            | <b>100,409</b> | <b>338,461</b>           | <b>282,717</b> |
| <b>Operating Expenses</b>   |                           |                |                          |                |
| Employment expenses   | 35,246                    | 33,022         | 105,756                  | 98,311         |
| Distribution and administration expenses  | 29,180                    | 25,253         | 96,139                   | 71,133         |
| Other operating expenses  | 11,288                    | 8,538          | 34,952                   | 27,778         |
| Other operating expenses of consolidated sponsored investment products                                | 1,246                     | 231            | 2,374                    | 547            |
| Restructuring and severance   | 294                       |                | 294                      | 203            |
| Depreciation and other amortization   | 713                       | 610            | 2,040                    | 1,782          |
| Amortization expense  | 947                       | 1,125          | 2,851                    | 3,351          |
| <b>Total operating expenses</b>   | <b>78,914</b>             | <b>68,779</b>  | <b>244,406</b>           | <b>203,105</b> |
| <b>Operating Income</b>   | <b>38,927</b>             | <b>31,630</b>  | <b>94,055</b>            | <b>79,612</b>  |
| <b>Other Income (Expense)</b>   |                           |                |                          |                |
| Realized and unrealized (loss) gain on investments, net   | (1,039)                   | 1,285          | 1,712                    | 1,887          |
| Realized and unrealized (loss) gain on investments of consolidated sponsored investment products, net | (5,330)                   | 324            | 1,150                    | (2,460)        |
| Other income, net   | 233                       | 111            | 573                      | 82             |
| <b>Total other (expense) income, net</b>  | <b>(6,136)</b>            | <b>1,720</b>   | <b>3,435</b>             | <b>(491)</b>   |
| <b>Interest Income (Expense)</b>  |                           |                |                          |                |
| Interest expense  | (149)                     | (207)          | (412)                    | (634)          |
| Interest and dividend income  | 326                       | 126            | 1,053                    | 426            |
| Interest and dividend income of investments of consolidated sponsored investment products             | 2,222                     | 600            | 4,734                    | 1,692          |

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|   |                  |                  |                  |                  |
|---|------------------|------------------|------------------|------------------|
| Total interest income, net  | 2,399            | 519              | 5,375            | 1,484            |
| <b>Income Before Income Taxes</b>                                 | <b>35,190</b>    | <b>33,869</b>    | <b>102,865</b>   | <b>80,605</b>    |
| Income tax (benefit) expense                                      | (1,805)          | 12,567           | 24,311           | 30,335           |
| <b>Net Income</b>   | <b>36,995</b>    | <b>21,302</b>    | <b>78,554</b>    | <b>50,270</b>    |
| Noncontrolling interests  | 345              | (213)            | 267              | 164              |
| <b>Net Income Attributable to Common Stockholders</b>             | <b>\$ 37,340</b> | <b>\$ 21,089</b> | <b>\$ 78,821</b> | <b>\$ 50,434</b> |
| <b>Earnings per share Basic</b>                                   | <b>\$ 4.10</b>   | <b>\$ 2.64</b>   | <b>\$ 8.65</b>   | <b>\$ 6.40</b>   |
| <b>Earnings per share Diluted</b>                                 | <b>\$ 4.02</b>   | <b>\$ 2.56</b>   | <b>\$ 8.46</b>   | <b>\$ 6.21</b>   |
| <b>Cash dividends declared per share</b>                          | <b>\$ 0.45</b>   | <b>\$</b>        | <b>\$ 0.90</b>   | <b>\$</b>        |
| <b>Weighted Average Shares Outstanding Basic (in thousands)</b>   | <b>9,096</b>     | <b>7,995</b>     | <b>9,115</b>     | <b>7,879</b>     |
| <b>Weighted Average Shares Outstanding Diluted (in thousands)</b> | <b>9,279</b>     | <b>8,227</b>     | <b>9,322</b>     | <b>8,125</b>     |

The accompanying notes are an integral part of these condensed consolidated financial statements.

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## Virtus Investment Partners, Inc.

## Condensed Consolidated Statements of Comprehensive Income

(Unaudited)

|  | Three Months Ended<br>September 30,<br>2014 |           | Nine Months Ended<br>September 30,<br>2014 |           |
|--|---|-----------|--|-----------|
|  | 2013  | 2014      | 2013                                       | 2014      |
| <i>(\$ in thousands)</i>   |   |           |  |           |
| Net Income   | \$ 36,995                                   | \$ 21,302 | \$ 78,554                                  | \$ 50,270 |
| <b>Other comprehensive income (loss), net of tax:</b>  |   |           |  |           |
| Foreign currency translation adjustment, net of tax of \$56 and \$(23) for the three months ended September 30, 2014 and 2013, respectively and \$49 and \$(12) for the nine months ended September 30, 2014 and 2013, respectively                | (93)  | 37        | (80)                                       | 19        |
| Unrealized (loss) gain on available-for-sale securities, net of tax of \$60 and \$29 for the three months ended September 30, 2014 and 2013, respectively and \$(55) and \$207 for the nine months ended September 30, 2014 and 2013, respectively | (95)  | (48)      | 90   | 91        |
| Other comprehensive (loss) income  | (188)                                       | (11)      | 10   | 110       |
| Comprehensive income   | 36,807                                      | 21,291    | 78,564                                     | 50,380    |
| Comprehensive loss (income) attributable to noncontrolling interests   | 345   | (213)     | 267  | 164       |
| Comprehensive income attributable to common stockholders   | \$ 37,152                                   | \$ 21,078 | \$ 78,831                                  | \$ 50,544 |

The accompanying notes are an integral part of these condensed consolidated financial statements.



**Table of Contents****Virtus Investment Partners, Inc.****Condensed Consolidated Statements of Cash Flows****(Unaudited)****Nine Months Ended****September 30,  
2014            2013***(\$ in thousands)***Cash Flows from Operating Activities:**

|   |           |           |
|---|-----------|-----------|
| Net income  | \$ 78,554 | \$ 50,270 |
| Adjustments to reconcile net income to net cash (used in) provided by operating activities:         |           |           |
| Depreciation expense, intangible asset and other amortization                                       | 5,055     | 5,291     |
| Stock-based compensation  | 7,021     | 5,983     |
| Excess tax benefits from stock-based compensation   | (25,089)  |           |
| Amortization of deferred commissions  | 14,032    | 10,032    |
| Payments of deferred commissions  | (11,761)  | (13,993)  |
| Equity in earnings of equity method investments   | (295)     | (94)      |
| Realized and unrealized gains on trading securities   | (1,712)   | (1,887)   |
| Realized and unrealized (gains) losses on investments of consolidated sponsored investment products | (1,247)   | 2,460     |
| Sales (purchases) of trading securities, net  | 24,996    | (1,163)   |
| Purchase of investments by consolidated sponsored investment products, net                          | (190,123) | (53,531)  |
| Sale of securities sold short by consolidated sponsored investment products, net                    | 10,461    |           |
| Deferred income taxes   | 4,826     | 29,001    |
| Changes in operating assets and liabilities:  |           |           |
| Cash pledged or on deposit of consolidated sponsored investment products                            | (12,492)  |           |
| Accounts receivable, net and other assets   | (17,776)  | (10,083)  |
| Other assets of consolidated sponsored investment products  | (481)     | (40,944)  |
| Accrued compensation and benefits, accounts payable, accrued liabilities and other liabilities      | 8,424     | 3,786     |
| Liabilities of consolidated sponsored investment products   | 5,319     | 40,951    |
| Net cash (used in) provided by operating activities   | (102,288) | 26,079    |

**Cash Flows from Investing Activities:**

|  |         |         |
|--|---------|---------|
| Capital expenditures   | (1,814) | (1,654) |
| Asset acquisitions   | (5,000) | (3,364) |
| Change in cash and cash equivalents of consolidated sponsored investment products due to deconsolidation | (366)   | (666)   |
| Purchase of available-for-sale securities  | (260)   | (145)   |
| Net cash used in investing activities  | (7,440) | (5,829) |

**Cash Flows from Financing Activities:**

|  |                   |                   |
|--|-------------------|-------------------|
| Contingent consideration paid for acquired investment management contracts   |                   | (420)             |
| Proceeds from issuance of debt by consolidated sponsored investment products | 1,200             |                   |
| Dividends paid   | (4,104)           |                   |
| Repurchase of common shares  | (26,257)          | (19,704)          |
| Proceeds from exercise of stock options                                      | 660               | 478               |
| Taxes paid related to net share settlement of restricted stock units         | (9,512)           | (7,493)           |
| Proceeds from issuance of common stock, net of issuance costs                |                   | 191,800           |
| Payment on debt and deferred financing costs                                 |                   | (15,026)          |
| Excess tax benefits from stock-based compensation                            | 25,089            |                   |
| Contributions of noncontrolling interests, net                               | 24,871            | 11,396            |
| Net cash provided by financing activities                                    | 11,947            | 161,031           |
| Net (decrease) increase in cash and cash equivalents                         | (97,781)          | 181,281           |
| Cash and cash equivalents, beginning of period                               | 271,545           | 63,446            |
| <b>Cash and Cash Equivalents, end of period</b>                              | <b>\$ 173,764</b> | <b>\$ 244,727</b> |

## Non-Cash Financing Activities:

|   |             |          |
|---|-------------|----------|
| (Decrease) increase to noncontrolling interest due to (deconsolidation) consolidation of sponsored investment products, net | \$ (44,613) | \$ 4,414 |
| Dividend payable  | \$ 4,229    | \$       |

The accompanying notes are an integral part of these condensed consolidated financial statements.

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## Virtus Investment Partners, Inc.

## Condensed Consolidated Statements of Changes in Equity

(Unaudited)

|  | Common Stock | Additional<br>Paid-in<br>Capital | Accumulated<br>Deficit | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) | Treasury Stock<br>Shares | Treasury Stock<br>Amount | Total<br>Attributed<br>To<br>Stockholder | Non-<br>controlling<br>Interests | Total<br>Equity | Redeem<br>Non-<br>controll<br>Interests |           |
|--|--------------|----------------------------------|------------------------|---|--------------------------|--------------------------|--|----------------------------------|-----------------|---|-----------|
| (in<br>thousands)  | Shares       | Par Value                        |                        |   |                          |                          |  |                                  |                 |   |           |
| Balance at<br>September 30,<br>2012  | 7,826,674    | \$ 81                            | \$ 942,825             | \$ (680,411)  | \$ (287)                 | 245,000                  | \$ (17,734)                              | \$ 244,474                       | \$ (3)          | \$ 244,471                              | \$ 3,111  |
| Net income (loss)  |              |                                  |                        | 50,434  |                          |                          |  | 50,434                           | (46)            | 50,388                                  | (1)       |
| Unrealized<br>gain on securities<br>available-for-sale   |              |                                  |                        |   | 91                       |                          |  | 91                               |                 | 91                                      |           |
| Translation<br>adjustment  |              |                                  |                        |   | 19                       |                          |  | 19                               |                 | 19                                      |           |
| Change in<br>percentage of<br>ownership of<br>controlling<br>interests, net<br>of change of<br>common stock, |              |                                  |                        |   |                          |                          |  |                                  |                 |   | 15,800    |
| Issuance of<br>common stock,   | 1,298,386    | 13                               | 191,568                |   |                          |                          |  | 191,581                          |                 | 191,581                                 |           |
| Repurchase of<br>common shares   | (105,000)    |                                  |                        |   | 105,000                  | (19,704)                 | (19,704)                                 |                                  |                 | (19,704)                                |           |
| Issuance of<br>common stock<br>related to<br>employee stock<br>purchase<br>transactions                      | 80,738       | 1                                | 982                    |   |                          |                          |  | 983                              |                 | 983                                     |           |
| Expenses paid on<br>stock-based<br>compensation  |              |                                  | (7,493)                |   |                          |                          |  | (7,493)                          |                 | (7,493)                                 |           |
| Expenses paid on<br>stock-based<br>compensation  |              |                                  | 5,468                  |   |                          |                          |  | 5,468                            |                 | 5,468                                   |           |
| Balance at<br>September 30,<br>2013  | 9,100,798    | \$ 95                            | \$ 1,133,350           | \$ (629,977)  | \$ (177)                 | 350,000                  | \$ (37,438)                              | \$ 465,853                       | \$ (49)         | \$ 465,804                              | \$ 18,800 |
|  | 9,105,521    | \$ 95                            | \$ 1,135,644           | \$ (605,221)  | \$ (150)                 | 350,000                  | \$ (37,438)                              | \$ 492,930                       | \$ (62)         | \$ 492,868                              | \$ 42,100 |

| <b>ances at</b>  |           |         |              |             |         |         |            |            |         |            |         |
|------------------|-----------|---------|--------------|-------------|---------|---------|------------|------------|---------|------------|---------|
| <b>ember 31,</b> |           |         |              |             |         |         |            |            |         |            |         |
| <b>3</b>         |           |         |              |             |         |         |            |            |         |            |         |
| Income (loss)    |           |         |              |             |         |         |            |            |         |            |         |
|                  |           |         |              |             |         |         |            |            |         |            |         |
| unrealized       |           |         |              |             |         |         |            |            |         |            |         |
| on securities    |           |         |              |             |         |         |            |            |         |            |         |
| able-for-sale    |           |         |              |             |         |         |            |            |         |            |         |
| ign currency     |           |         |              |             |         |         |            |            |         |            |         |
| lation           |           |         |              |             |         |         |            |            |         |            |         |
| stment           |           |         |              |             |         |         |            |            |         |            |         |
| ivity of         |           |         |              |             |         |         |            |            |         |            |         |
| controlling      |           |         |              |             |         |         |            |            |         |            |         |
| ests, net        |           |         |              |             |         |         |            |            |         |            | (19,7   |
| n dividends      |           |         |              |             |         |         |            |            |         |            |         |
| ared             |           |         |              |             |         |         |            |            |         |            |         |
|                  |           |         |              |             |         |         |            |            |         |            |         |
| urchase of       |           |         |              |             |         |         |            |            |         |            |         |
| mon shares       | (136,874) |         |              |             |         |         |            |            |         |            |         |
| ance of          |           |         |              |             |         |         |            |            |         |            |         |
| mon stock        |           |         |              |             |         |         |            |            |         |            |         |
| ed to            |           |         |              |             |         |         |            |            |         |            |         |
| loyee stock      |           |         |              |             |         |         |            |            |         |            |         |
| sactions         | 90,731    | 1,224   |              |             |         |         |            |            |         |            |         |
| es paid on       |           |         |              |             |         |         |            |            |         |            |         |
| k-based          |           |         |              |             |         |         |            |            |         |            |         |
| ensation         |           | (9,512) |              |             |         |         |            |            |         |            |         |
| k-based          |           |         |              |             |         |         |            |            |         |            |         |
| ensation         |           | 6,604   |              |             |         |         |            |            |         |            |         |
| ess tax          |           |         |              |             |         |         |            |            |         |            |         |
| efits from       |           |         |              |             |         |         |            |            |         |            |         |
| k-based          |           |         |              |             |         |         |            |            |         |            |         |
| ensation         |           | 25,089  |              |             |         |         |            |            |         |            |         |
| <b>ances at</b>  |           |         |              |             |         |         |            |            |         |            |         |
| <b>ember 30,</b> |           |         |              |             |         |         |            |            |         |            |         |
| <b>4</b>         |           |         |              |             |         |         |            |            |         |            |         |
|                  | 9,059,378 | \$ 95   | \$ 1,150,716 | \$(526,400) | \$(140) | 486,874 | \$(63,695) | \$ 560,576 | \$(146) | \$ 560,430 | \$ 22,2 |

The accompanying notes are an integral part of these condensed consolidated financial statements.

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**Virtus Investment Partners, Inc.**

**Notes to Condensed Consolidated Financial Statements**

**(Unaudited)**

**1. Organization and Business**

Virtus Investment Partners, Inc. (the Company, we, us, our or Virtus ), a Delaware corporation, operates in the investment management industry through its wholly-owned subsidiaries.

The Company provides investment management and related services to individuals and institutions throughout the United States of America. The Company's retail investment management services are provided to individuals through products consisting of open-end mutual funds, closed-end funds, variable insurance funds and separately managed accounts. Separately managed accounts are offered through intermediary programs that are sponsored and distributed by unaffiliated broker-dealers and individual direct managed account investment services that are provided by the Company. Institutional investment management services are provided primarily to corporations, multi-employer retirement funds, employee retirement systems, foundations and endowments.

**2. Basis of Presentation and Significant Accounting Policies**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ) for interim financial information. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, these financial statements contain all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of the Company's financial condition and results of operations. Operating results for the nine months ended September 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014.

The condensed consolidated financial statements include the accounts of the Company, its subsidiaries and sponsored investment products in which it has a controlling financial interest. Intercompany accounts and transactions have been eliminated. The Company is generally considered to have a controlling financial interest when it owns a majority of the voting interest in an entity or otherwise has the power to govern the financial and operating policies of the subsidiary. See Note 12 for additional information related to the consolidation of sponsored investment products. The Company also evaluates any variable interest entities ( VIEs ) in which the Company has a variable interest for consolidation. A VIE is an entity in which either (a) the equity investment at risk is not sufficient to permit the entity to finance its own activities without additional financial support, or (b) where as a group, the holders of equity investment at risk do not possess: (i) the power to direct the activities that most significantly impact the entity's performance; (ii) the obligation to absorb expected losses or the right to receive expected residual returns of the entity; or (iii) proportionate voting and economic interests and where substantially all of the entity's activities either involve or are conducted on behalf of the equity holders. If an entity has any of these characteristics, it is considered a VIE and required to be consolidated by its primary beneficiary. The primary beneficiary is the entity that has both the power to direct the activities that most significantly impact the VIE's economic performance and has the obligation to absorb losses of, or the right to receive benefits from, the VIE that could potentially be significant to the VIE.

These unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K, as amended, for the year ended December 31, 2013 (collectively the 2013 Annual Report on Form 10-K ) filed with the

Securities and Exchange Commission. The Company's significant accounting policies, which have been consistently applied, are summarized in the 2013 Annual Report on Form 10-K, as amended.

Effective December 31, 2013, the Company changed the presentation of its Consolidated Balance Sheets from a classified basis, which distinguishes between current and long-term assets and liabilities, to an unclassified basis, which has no such distinction. There were no changes to the Condensed Consolidated Balance Sheets that impacted the Condensed Consolidated Statements of Operations. Amounts in the prior year's Condensed Consolidated Statements of Cash Flows have been recast to conform to the current year's presentation.

**Table of Contents****3. Intangible Assets, Net**

Intangible assets, net are summarized as follows:

|  | September 30,<br>2014 | December 31,<br>2013 |
|--|-----------------------|----------------------|
| <i>(\$ in thousands)</i>                     |                       |                      |
| <b>Definite-lived intangible assets:</b>     |                       |                      |
| Investment contracts                         | \$ 158,747            | \$ 157,882           |
| Accumulated amortization                     | (148,453)             | (145,665)            |
| <b>Definite-lived intangible assets, net</b> | 10,294                | 12,217               |
| Indefinite-lived intangible assets           | 32,416                | 32,416               |
| <b>Total intangible assets, net</b>          | \$ 42,710             | \$ 44,633            |

Activity in intangible assets, net is as follows:

|                               | Nine Months Ended<br>September 30, |           |
|-------------------------------|------------------------------------|-----------|
|                               | 2014                               | 2013      |
| <i>(\$ in thousands)</i>      |                                    |           |
| <b>Intangible assets, net</b> |                                    |           |
| Balance, beginning of period  | \$ 44,633                          | \$ 48,711 |
| Purchases                     | 1,075                              | 356       |
| Amortization                  | (2,998)                            | (3,160)   |
| <b>Balance, end of period</b> | \$ 42,710                          | \$ 45,907 |

**4. Investments**

Investments consist primarily of investments in our sponsored mutual funds. The Company's investments, excluding the assets of consolidated sponsored investment products discussed in Note 12, at September 30, 2014 and December 31, 2013 are as follows:

|                                     | September 30,<br>2014 | December 31,<br>2013 |
|-------------------------------------|-----------------------|----------------------|
| <i>(\$ in thousands)</i>            |                       |                      |
| Marketable securities               | \$ 50,845             | \$ 28,968            |
| Equity method investments           | 7,235                 | 4,070                |
| Nonqualified retirement plan assets | 4,654                 | 4,220                |
| Other investments                   | 925                   |                      |

|                          |    |        |    |        |
|--------------------------|----|--------|----|--------|
| <b>Total investments</b> | \$ | 63,659 | \$ | 37,258 |
|--------------------------|----|--------|----|--------|

*Marketable Securities*

The Company's marketable securities consist of both trading and available-for-sale securities. The composition of the Company's marketable securities is summarized as follows:



**Table of Contents****September 30, 2014**

|                                    | <b>Cost</b>      | <b>Unrealized<br/>Loss</b> | <b>Unrealized<br/>Gain</b> | <b>Fair<br/>Value</b> |
|------------------------------------|------------------|----------------------------|----------------------------|-----------------------|
| <i>(\$ in thousands)</i>           |                  |                            |                            |                       |
| <b>Trading:</b>                    |                  |                            |                            |                       |
| Sponsored funds                    | \$ 37,426        | \$ (633)                   | \$ 2,036                   | \$ 38,829             |
| Equity securities                  | 8,255            |                            | 672                        | 8,927                 |
| <b>Available-for-sale:</b>         |                  |                            |                            |                       |
| Sponsored funds                    | 3,074            | (136)                      | 151                        | 3,089                 |
| <b>Total marketable securities</b> | <b>\$ 48,755</b> | <b>\$ (769)</b>            | <b>\$ 2,859</b>            | <b>\$ 50,845</b>      |

**December 31, 2013**

|                                    | <b>Cost</b>      | <b>Unrealized<br/>Loss</b> | <b>Unrealized<br/>Gain</b> | <b>Fair<br/>Value</b> |
|------------------------------------|------------------|----------------------------|----------------------------|-----------------------|
| <i>(\$ in thousands)</i>           |                  |                            |                            |                       |
| <b>Trading:</b>                    |                  |                            |                            |                       |
| Sponsored funds                    | \$ 16,079        | \$ (704)                   | \$ 2,529                   | \$ 17,904             |
| Equity securities                  | 7,043            |                            | 1,336                      | 8,379                 |
| <b>Available-for-sale:</b>         |                  |                            |                            |                       |
| Sponsored funds                    | 2,815            | (145)                      | 15                         | 2,685                 |
| <b>Total marketable securities</b> | <b>\$ 25,937</b> | <b>\$ (849)</b>            | <b>\$ 3,880</b>            | <b>\$ 28,968</b>      |

For the three months ended September 30, 2014 and 2013, the Company recognized realized gains of \$1.7 million and \$0.2 million, respectively, and \$6.2 million and \$0.5 million for the nine months ended September 30, 2014 and 2013, respectively, on trading securities.

**5. Fair Value Measurements**

The Company's assets and liabilities measured at fair value, excluding the assets and liabilities of consolidated sponsored investment products discussed in Note 12, on a recurring basis as of September 30, 2014 and December 31, 2013 by fair value hierarchy level were as follows:

**September 30, 2014**

|                          | <b>Level 1</b> | <b>Level 2</b> | <b>Level 3</b> | <b>Total</b> |
|--------------------------|----------------|----------------|----------------|--------------|
| <i>(\$ in thousands)</i> |                |                |                |              |
| <b>Assets</b>            |                |                |                |              |
| Cash equivalents         | \$ 171,934     | \$             | \$             | \$ 171,934   |

|  |            |    |    |            |
|--|------------|----|----|------------|
| <b>Marketable securities trading:</b>            |            |    |    |            |
| Sponsored funds                                  | 38,829     |    |    | 38,829     |
| Equity securities                                | 8,927      |    |    | 8,927      |
| <b>Marketable securities available for sale:</b> |            |    |    |            |
| Sponsored funds                                  | 3,089      |    |    | 3,089      |
| <b>Other investments:</b>                        |            |    |    |            |
| Nonqualified retirement plan assets              | 4,654      |    |    | 4,654      |
| <b>Total assets measured at fair value</b>       | \$ 227,433 | \$ | \$ | \$ 227,433 |

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December 31, 2013

|  | Level 1           | Level 2   | Level 3   | Total             |
|--|-------------------|-----------|-----------|-------------------|
| <i>(\$ in thousands)</i>                         |                   |           |           |                   |
| <b>Assets</b>                                    |                   |           |           |                   |
| Cash equivalents                                 | \$ 270,262        | \$        | \$        | \$ 270,262        |
| <b>Marketable securities trading:</b>            |                   |           |           |                   |
| Sponsored funds                                  | 17,904            |           |           | 17,904            |
| Equity securities                                | 8,379             |           |           | 8,379             |
| <b>Marketable securities available for sale:</b> |                   |           |           |                   |
| Sponsored funds                                  | 2,685             |           |           | 2,685             |
| <b>Other investments:</b>                        |                   |           |           |                   |
| Nonqualified retirement plan assets              | 4,220             |           |           | 4,220             |
| <b>Total assets measured at fair value</b>       | <b>\$ 303,450</b> | <b>\$</b> | <b>\$</b> | <b>\$ 303,450</b> |

The following is a discussion of the valuation methodologies used for the Company's assets measured at fair value.

*Sponsored funds* represent investments in open-end mutual funds, variable insurance funds and closed-end funds for which the Company acts as the investment manager. The fair value of open-end mutual funds and variable insurance funds is determined based on their published net asset values and are categorized as Level 1. The fair value of closed-end funds is determined based on the official closing price of the exchange they are traded on and are categorized as Level 1.

*Equity securities* include securities traded on active markets and are valued at the official closing price (typically last sale or bid) on the exchange on which the securities are primarily traded and are categorized as Level 1.

*Nonqualified retirement plan assets* represent mutual funds within a nonqualified retirement plan whose fair value is determined based on their published net asset value and are categorized as Level 1.

Cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities equal or approximate fair value based on the short-term nature of these instruments. Marketable securities are reflected in the condensed consolidated financial statements at fair value based upon publicly quoted market prices.

Transfers into and out of levels are reflected when significant inputs, including market inputs or performance attributes, used for the fair value measurement become observable or unobservable or when the Company determines it has the ability, or no longer has the ability, to redeem, in the near term, certain investments that the Company values using a net asset value, or if the book value of certain equity method investments no longer represents fair value. There were no transfers between Level 1 and Level 2 during the nine months ended September 30, 2014 and 2013.

**6. Treasury Stock and Dividends**

During the nine months ended September 30, 2014 and 2013, the Company repurchased 136,874 and 105,000 common shares, respectively, at a weighted average price of \$191.79 and \$187.61 per share, respectively, plus transaction costs for a total cost of approximately \$26.3 million and \$19.7 million, respectively. The Company has repurchased a total of 486,874 shares of common stock at a weighted average price of \$130.78 per share plus

transaction costs for a total cost of \$63.7 million under its share repurchase program. At September 30, 2014, there were 213,126 shares of common stock available to repurchase under the Company's current authorization through the share repurchase program.

In August 2014, the Company paid a cash dividend on the Company's common stock in the amount of \$0.45 per share totaling \$4.1 million. On August 13, 2014, the Board of Directors approved a cash dividend on the Company's common stock in the amount of \$0.45 per share to stockholders of record as of October 31, 2014, estimated at \$4.1 million, to be paid on November 14, 2014.

**Table of Contents****7. Accumulated Other Comprehensive Income**

The changes in accumulated other comprehensive income, by component, for the nine months ended September 30, 2014 and 2013 were as follows:

|  | <b>Unrealized Gains<br/>and<br/>(Losses)<br/>on Securities<br/>Available-for-<br/>Sale</b> | <b>Foreign Currency<br/>Translation<br/>Adjustments</b> |
|--|--|---|
| <i>(\$ in thousands)</i>   |  |   |
| <b>Balance December 31, 2013</b>                                 | \$ (231)   | \$ 81   |
| Unrealized net gains on investments, net of tax of (\$55)        | 90   |   |
| Foreign currency translation adjustments, net of tax of \$49     |  | (80)  |
| Amounts reclassified from accumulated other comprehensive income |  |   |
| <b>Net current-period other comprehensive income</b>             | 90   | (80)  |
| <b>Balance September 30, 2014</b>                                | \$ (141)   | \$ 1  |
| <br>   |  |   |
|  | <b>Unrealized Gains<br/>and (Losses)<br/>on Securities<br/>Available-for-<br/>Sale</b>     | <b>Foreign Currency<br/>Translation<br/>Adjustments</b> |
| <i>(\$ in thousands)</i>   |  |   |
| <b>Balance December 31, 2012</b>                                 | \$ (287)   | \$  |
| Unrealized net gains on investments, net of tax of \$207         | 91   |   |
| Foreign currency translation, net of tax of (\$12)               |  | 19  |
| Amounts reclassified from accumulated other comprehensive income |  |   |
| <b>Net current-period other comprehensive income</b>             | 91   | 19  |
| <b>Balance September 30, 2013</b>                                | \$ (196)   | \$ 19   |

## **8. Stock-based Compensation**

The Company has an Omnibus Incentive and Equity Plan (the Plan ) under which officers, employees and directors may be granted equity-based awards, including restricted stock units ( RSUs ), stock options and unrestricted shares of common stock. At September 30, 2014, 427,045 shares of common stock remain available for issuance of the 1,800,000 shares that were reserved for issuance under the Plan. Each RSU entitles the holder to one share of common stock when the restriction expires. RSUs generally have a term of one to three years and may be time-vested or performance-contingent. Stock options generally cliff vest after three years and have a contractual life of ten years. Stock options are granted with an exercise price equal to the fair market value of the shares at the date of grant. The fair value of each RSU is estimated using the intrinsic value method, which is based on the fair market value price on the date of grant unless it contains a performance metric that is considered a market condition. RSUs that contain a market condition are valued using a simulation valuation model. Shares that are issued upon exercise of stock options and vesting of RSUs are newly issued shares from the Plan and are not issued from treasury stock.

**Table of Contents*****Restricted Stock Units***

RSU activity for the nine months ended September 30, 2014 is summarized as follows:

|  | <b>Number<br/>of Shares</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|--|-----------------------------|---|
| Outstanding at December 31, 2013         | 233,763                     | \$ 87.97  |
| Granted                                  | 76,387                      | \$ 184.31   |
| Forfeited                                | (10,966)                    | \$ 132.15   |
| Settled                                  | (117,914)                   | \$ 60.91  |
| <b>Outstanding at September 30, 2014</b> | <b>181,270</b>              | <b>\$ 143.50</b>  |

For the nine months ended September 30, 2014 and 2013, a total of 50,952 and 38,128 RSUs, respectively, were withheld by the Company as a result of net share settlements to satisfy employee tax withholding obligations. During the nine months ended September 30, 2014 and 2013, the Company paid \$9.5 million and \$7.5 million, respectively, in employee tax withholding obligations related to employee share transactions during each period. These net share settlements had the effect of share repurchases by the Company as they reduced the number of shares that would have been otherwise issued as a result of the vesting or exercise.

***Stock Options***

Stock option activity for the nine months ended September 30, 2014 is summarized as follows:

|  | <b>Number<br/>of Shares</b> | <b>Weighted<br/>Average<br/>Exercise Price</b> |
|--|-----------------------------|--|
| Outstanding at December 31, 2013         | 190,160                     | \$ 20.11                                       |
| Granted                                  |                             | \$   |
| Exercised                                | (22,912)                    | \$ 29.42                                       |
| Forfeited                                |                             | \$   |
| <b>Outstanding at September 30, 2014</b> | <b>167,248</b>              | <b>\$ 18.83</b>                                |

The Company recognized total stock compensation expense of \$2.5 million and \$2.0 million, respectively, and \$7.0 million and \$6.0 million, respectively, for the three and nine months ended September 30, 2014 and 2013. As of September 30, 2014 and 2013, unamortized stock-based compensation expense for unvested RSUs was \$15.1 million and \$11.2 million, with a weighted-average remaining amortization period of 1.4 years and 1.2 years, respectively. There was no unamortized stock-based compensation expense related to stock options as of September 30, 2014 as all outstanding options were fully vested and unamortized stock-based compensation expense related to stock options was \$0.1 million with a weighted-average remaining amortization period of 0.5 years at September 30, 2013.

## **9. Earnings per Share**

Basic earnings per share ( EPS ) excludes dilution for potential common stock issuances and is computed by dividing net income available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. For the calculation of diluted EPS, the basic weighted-average number of shares is increased by the dilutive effect of RSUs and common stock options using the treasury stock method.



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The computation of basic and diluted EPS is as follows:

|  | Three Months Ended September 30, |                  | Nine Months Ended September 30, |               |
|--|----------------------------------|------------------|---------------------------------|---------------|
|  | 2014                             | 2013             | 2014                            | 2013          |
| <i>(\$ in thousands, except per share amounts)</i>                       |                                  |                  |                                 |               |
| Net Income   | \$ 36,995                        | \$ 21,302        | \$ 78,554                       | \$ 50,270     |
| Noncontrolling interests   | 345                              | (213)            | 267                             | 164           |
| <b>Net Income Attributable to Common Stockholders</b>                    | <b>\$ 37,340</b>                 | <b>\$ 21,089</b> | <b>\$ 78,821</b>                | <b>50,434</b> |
| <b>Shares (in thousands):</b>  |                                  |                  |                                 |               |
| Basic: Weighted-average number of shares outstanding                     | 9,096                            | 7,995            | 9,115                           | 7,879         |
| Plus: Incremental shares from assumed conversion of dilutive instruments | 183                              | 232              | 207                             | 246           |
| <b>Diluted: Weighted-average number of shares outstanding</b>            | <b>9,279</b>                     | <b>8,227</b>     | <b>9,322</b>                    | <b>8,125</b>  |
| Earnings per share - basic   | \$ 4.10                          | \$ 2.64          | \$ 8.65                         | \$ 6.40       |
| Earnings per share - diluted   | \$ 4.02                          | \$ 2.56          | \$ 8.46                         | \$ 6.21       |
| Cash dividends declared per share  | \$ 0.45                          | \$               | \$ 0.90                         | \$            |

For the three and nine months ended September 30, 2014, there were no instruments excluded from the above computations of weighted-average shares for diluted EPS. For both the three and nine months ended September 30, 2013, there were 3,115 instruments excluded from the above computations of weighted-average shares for diluted EPS because their effect would be anti-dilutive.

**10. Income Taxes**

In calculating the provision for income taxes, the Company uses an estimate of the annual effective tax rate based upon the facts and circumstances at each interim period. On a quarterly basis, the estimated annual effective tax rate is adjusted, as appropriate, based upon changes in facts and circumstances, if any, as compared to those forecasted at the beginning of the fiscal year and each interim period thereafter.

The provision for income taxes reflects U.S. federal, state and local taxes at an estimated effective tax rate of (5.1)% and 37.1% and 23.6% and 37.6% for the three and nine months ended September 30, 2014 and 2013, respectively. The Company's effective tax rate for the three and nine months ended September 30, 2014 was impacted by a net tax benefit of approximately \$15.5 million due to the settlement of audits of its 2011 federal corporate income tax return. The net benefit is comprised of the recognition of tax benefits from uncertain tax positions of approximately \$31.0 million and a reduction in the deferred tax assets of approximately \$15.5 million which are related to a loss resulting from the past dissolution of a subsidiary.

During the quarter ended September 30, 2014, the Company recognized tax benefits of \$25.1 million related to cumulative windfall deductions on certain stock-based incentive plans. Under Accounting Standard Codification

( ASC ) 718, *Compensation-Stock Compensation*, these tax benefits are utilized for financial statement purposes when they serve to reduce income taxes payable. Under the Company's accounting policy, net operating losses and benefits from other sources are recognized before these windfall benefit carryforwards. The tax benefit related to these windfall deductions was recorded as an increase to Stockholders' Equity.

**Table of Contents****11. Commitments and Contingencies*****Legal Matters***

The Company is regularly involved in litigation and arbitration as well as examinations and investigations by various regulatory bodies, including the SEC, involving its compliance with, among other things, securities laws, client investment guidelines, laws governing the activities of broker-dealers and other laws and regulations affecting its products and other activities. Legal and regulatory matters of this nature may involve the Company's activities as an employer, issuer of securities, investor, investment adviser, broker-dealer or taxpayer. The Company cannot predict the ultimate outcome of such legal claims or matters or in certain instances provide reasonable ranges of potential losses. As of the date of this report, the Company believes that the outcomes of its legal or regulatory matters are not likely, either individually or in the aggregate, to have a material adverse effect on its consolidated financial condition. However, in the event of unexpected subsequent developments and given the inherent unpredictability of these legal and regulatory matters, the Company can provide no assurance that its assessment of any claim, dispute, regulatory examination or investigation or other legal matter will reflect the ultimate outcome and an adverse outcome in certain matters could, from time to time, have a material adverse effect on the Company's results of operations or cash flows in particular quarterly or annual periods.

**12. Consolidated Sponsored Investment Products*****Sponsored Investment Products***

In the normal course of its business, the Company sponsors various types of investment products. The Company consolidates an investment product when it owns a majority of the voting interest in the entity or it is the primary beneficiary of an investment product that is a VIE. The consolidation and deconsolidation of these investment products has no impact on net income attributable to stockholders. The Company's risk with respect to these investments is limited to its investment in these products. The Company has no right to the benefits from, and does not bear the risks associated with, these investment products, beyond the Company's investments in, and fees generated from these products. If the Company were to liquidate, these investments would not be available to the general creditors of the Company. The Company does not consider cash and investments held by consolidated sponsored investment products to be assets of the Company other than its direct investment in these products.

As of September 30, 2014 and December 31, 2013, the Company consolidated twelve and eight sponsored investment products, respectively. During the nine months ended September 30, 2014, the Company consolidated five additional sponsored investment products and deconsolidated one sponsored investment product because it no longer had a majority voting interest.

The following table presents the balances of the consolidated sponsored investment products that were reflected in the Condensed Consolidated Balance Sheets as of September 30, 2014 and December 31, 2013:

|                          | As of                 |                      |
|--------------------------|-----------------------|----------------------|
|                          | September 30,<br>2014 | December 31,<br>2013 |
| <i>(\$ in thousands)</i> |                       |                      |
| Total cash               | \$ 13,547             | \$ 531               |
| Total investments        | 241,107               | 139,054              |

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|                                     |          |          |
|-------------------------------------|----------|----------|
| All other assets                    | 8,756    | 9,595    |
| Total liabilities                   | (23,838) | (8,435)  |
| Redeemable noncontrolling interests | (22,265) | (42,186) |

|  |            |           |
|--|------------|-----------|
| <b>The Company's net interests in consolidated sponsored investment products</b> | \$ 217,307 | \$ 98,559 |
|--|------------|-----------|

**Table of Contents****Consolidation**

The following tables reflect the impact of the consolidated sponsored investment products in the Condensed Consolidated Balance Sheets as of September, 30, 2014 and December 31, 2013, respectively:

**As of September 30, 2014**

|  | <b>Balance Before<br/>Consolidation of<br/>Investment Products</b> | <b>Consolidated<br/>Sponsored<br/>Investment<br/>Products</b> | <b>Eliminations<br/>and<br/>Adjustments (a)</b> | <b>Balances as<br/>Reported in<br/>Condensed<br/>Consolidated<br/>Balance Sheet</b> |
|--|--|---|---|---|
| <i>(\$ in thousands)</i>                           |  |   |   |   |
| Total cash   | \$ 172,709   | \$ 13,547   | \$  | \$ 186,256  |
| Total investments                                  | 280,953  | 241,107   | (217,294)                                       | 304,766   |
| All other assets                                   | 196,236  | 8,756   | (13)  | 204,979   |
| <b>Total assets</b>                                | <b>\$ 649,898</b>  | <b>\$ 263,410</b>   | <b>\$ (217,307)</b>                             | <b>\$ 696,001</b>   |
| Total liabilities                                  | \$ 89,468  | \$ 23,851   | \$ (13)   | \$ 113,306  |
| Redeemable noncontrolling interests                |  |   | 22,265  | 22,265  |
| Equity attributable to stockholders of the Company | 560,576  | 239,559   | (239,559)                                       | 560,576   |
| Non-redeemable noncontrolling interests            | (146)  |   |   | (146)   |
| <b>Total liabilities and equity</b>                | <b>\$ 649,898</b>  | <b>\$ 263,410</b>   | <b>\$ (217,307)</b>                             | <b>\$ 696,001</b>   |

- (a) Adjustments include the elimination of intercompany transactions between the Company and its consolidated sponsored investment products, primarily the elimination of the investments and equity and recording of any noncontrolling interest.

**As of December 31, 2013**

|                          | <b>Balance Before<br/>Consolidation of<br/>Investment Products</b> | <b>Consolidated<br/>Sponsored<br/>Investment<br/>Products</b> | <b>Eliminations<br/>and<br/>Adjustments (a)</b> | <b>Balances<br/>as<br/>Reported in<br/>Condensed<br/>Consolidated<br/>Balance Sheet</b> |
|--------------------------|--|---|---|---|
| <i>(\$ in thousands)</i> |  |   |   |   |
| Total cash               | \$ 271,014   | \$ 531  | \$  | \$ 271,545  |

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|  |                   |                   |                    |                   |
|--|-------------------|-------------------|--------------------|-------------------|
| Total investments                                  | 135,692           | 139,054           | (98,434)           | 176,312           |
| All other assets                                   | 187,627           | 9,595             | (125)              | 197,097           |
| <b>Total assets</b>                                | <b>\$ 594,333</b> | <b>\$ 149,180</b> | <b>\$ (98,559)</b> | <b>\$ 644,954</b> |
| Total liabilities                                  | \$ 101,465        | \$ 8,560          | \$ (125)           | \$ 109,900        |
| Redeemable noncontrolling interests                |                   |                   | 42,186             | 42,186            |
| Equity attributable to stockholders of the Company | 492,930           | 140,620           | (140,620)          | 492,930           |
| Non-redeemable noncontrolling interests            | (62)              |                   |                    | (62)              |
| <b>Total liabilities and equity</b>                | <b>\$ 594,333</b> | <b>\$ 149,180</b> | <b>\$ (98,559)</b> | <b>\$ 644,954</b> |

- (a) Adjustments include the elimination of intercompany transactions between the Company and its consolidated sponsored investment products, primarily the elimination of the investments and equity and recording of any noncontrolling interest.

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The following table reflects the impact of the consolidated sponsored investment products in the Condensed Consolidated Statement of Operations for the three and nine months ended September 30, 2014 and 2013, respectively:

**For the Three Months Ended September 30, 2014**

|  | <b>Balance Before<br/>Consolidation<br/>of<br/>Investment Products</b> | <b>Consolidated<br/>Sponsored<br/>Investment<br/>Products</b> | <b>Eliminations<br/>and<br/>Adjustments (a)</b> | <b>Balances<br/>as<br/>Reported<br/>in<br/>Condensed<br/>Consolidated<br/>Statement<br/>of<br/>Operations</b> |
|--|--|---|---|---|
| <i>(\$ in thousands)</i>   |  |   |   |   |
| <b>Total operating revenues</b>                                  | \$ 117,808   | \$  | \$ 33   | \$ 117,841  |
| <b>Total operating expenses</b>                                  | 77,668   | 1,213   | 33  | 78,914  |
| <b>Operating income (loss)</b>                                   | 40,140   | (1,213)   |   | 38,927  |
| <b>Total other non-operating<br/>(loss) income</b>               | (4,649)  | (3,109)   | 4,021   | (3,737)   |
| <b>Income (loss) before income<br/>tax expense</b>               | 35,491   | (4,322)   | 4,021   | 35,190  |
| Income tax benefit   | (1,805)  |   |   | (1,805)   |
| <b>Net income (loss)</b>   | 37,296   | (4,322)   | 4,021   | 36,995  |
| Noncontrolling interests   | 44   |   | 301   | 345   |
| <b>Net income (loss) attributable<br/>to common stockholders</b> | \$ 37,340  | \$ (4,322)  | \$ 4,322  | \$ 37,340   |

- (a) Adjustments include the elimination of intercompany transactions between the Company and its consolidated sponsored investment products, primarily the elimination of the investments and equity and recording of any noncontrolling interest.

**For the Three Months Ended September 30, 2013**

| <b>Balance Before<br/>Consolidation of<br/>Investment</b> | <b>Consolidated<br/>Investment<br/>Products</b> | <b>Eliminations<br/>and</b> | <b>Balances<br/>as<br/>Reported</b> |
|---|---|-----------------------------|-------------------------------------|
|---|---|-----------------------------|-------------------------------------|

|  | Products |         | Adjustments (a) |       | in<br>Condensed<br>Consolidated<br>Statement<br>of<br>Operations |
|--|----------|---------|-----------------|-------|--|
| <i>(\$ in thousands)</i>                                     |          |         |                 |       |  |
| <b>Total operating revenues</b>                              | \$       | 100,319 | \$              | 90    | \$ 100,409   |
| <b>Total operating expenses</b>                              |          | 68,547  |                 | 142   | 68,779   |
| <b>Operating income (loss)</b>                               |          | 31,772  |                 | (142) | 31,630   |
| <b>Total other non-operating income (expense)</b>            |          | 1,870   |                 | 923   | (554)  |
| <b>Income (loss) before income tax expense</b>               |          | 33,642  |                 | 781   | (554)  |
| Income tax expense   |          | 12,567  |                 |       | 12,567   |
| <b>Net income (loss)</b>                                     |          | 21,075  |                 | 781   | (554)  |
| Noncontrolling interests                                     |          | 14      |                 |       | (227)  |
| <b>Net income (loss) attributable to common stockholders</b> | \$       | 21,089  | \$              | 781   | \$ (781)   |
|  |          |         |                 |       | \$ 21,089  |

- (a) Adjustments include the elimination of intercompany transactions between the Company and its consolidated sponsored investment products, primarily the elimination of the investments and equity and recording of any noncontrolling interest.



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For the Nine Months Ended September 30, 2014

|  | Balance Before<br>Consolidation<br>of<br>Investment Products | Consolidated<br>Sponsored<br>Investment<br>Products | Eliminations<br>and<br>Adjustments (a) | Balances<br>as<br>Reported<br>in<br>Condensed<br>Consolidated<br>Statement<br>of<br>Operations |
|--|--|---|--|--|
| <i>(\$ in thousands)</i>   |  |   |  |  |
| <b>Total operating revenues</b>                                  | \$ 338,534   | \$  | \$ (73)                                | \$ 338,461   |
| <b>Total operating expenses</b>                                  | 242,032  | 2,447   | (73)                                   | 244,406  |
| <b>Operating income (loss)</b>                                   | 96,502   | (2,447)   |  | 94,055   |
| <b>Total other non-operating<br/>income (expense)</b>            | 6,545  | 5,883   | (3,618)                                | 8,810  |
| <b>Income (loss) before income tax<br/>expense</b>               | 103,047  | 3,436   | (3,618)                                | 102,865  |
| Income tax expense   | 24,311   |   |  | 24,311   |
| <b>Net income (loss)</b>   | 78,736   | 3,436   | (3,618)                                | 78,554   |
| Noncontrolling interests   | 85   |   | 182                                    | 267  |
| <b>Net income (loss) attributable to<br/>common stockholders</b> | \$ 78,821  | \$ 3,436  | \$ (3,436)                             | \$ 78,821  |

- (a) Adjustments include the elimination of intercompany transactions between the Company and its consolidated sponsored investment products, primarily the elimination of the investments and equity and recording of any noncontrolling interest.

For the Nine Months Ended September 30, 2013

|  | Balance Before<br>Consolidation of<br>Investment<br>Products | Consolidated<br>Investment<br>Products | Eliminations<br>and<br>Adjustments (a) | Balances<br>as<br>Reported<br>in<br>Condensed<br>Consolidated<br>Statement |
|--|--|--|--|--|
|--|--|--|--|--|

|  | <b>of</b>         |            |          |            |
|--|-------------------|------------|----------|------------|
|  | <b>Operations</b> |            |          |            |
| <i>(\$ in thousands)</i>                                     |                   |            |          |            |
| <b>Total operating revenues</b>                              | \$ 282,575        | \$         | \$ 142   | \$ 282,717 |
| <b>Total operating expenses</b>                              | 202,557           | 406        | 142      | 203,105    |
| <b>Operating income (loss)</b>                               | 80,018            | (406)      |          | 79,612     |
| <b>Total other non-operating income (expense)</b>            | 705               | (768)      | 1,056    | 993        |
| <b>Income (loss) before income tax expense</b>               | 80,723            | (1,174)    | 1,056    | 80,605     |
| Income tax expense   | 30,335            |            |          | 30,335     |
| <b>Net income (loss)</b>                                     | 50,388            | (1,174)    | 1,056    | 50,270     |
| Noncontrolling interests                                     | 46                |            | 118      | 164        |
| <b>Net income (loss) attributable to common stockholders</b> | \$ 50,434         | \$ (1,174) | \$ 1,174 | \$ 50,434  |

- (a) Adjustments include the elimination of intercompany transactions between the Company and its consolidated sponsored investment products, primarily the elimination of the investments and equity and recording of any noncontrolling interest.

**Table of Contents*****Fair Value Measurements of Consolidated Sponsored Investment Products***

The assets and liabilities of the consolidated sponsored investment products measured at fair value on a recurring basis as of September 30, 2014 and December 31, 2013 by fair value hierarchy level were as follows:

**September 30, 2014**

|   | Level 1          | Level 2           | Level 3       | Total             |
|---|------------------|-------------------|---------------|-------------------|
| <i>(\$ in thousands)</i>                        |                  |                   |               |                   |
| <i>Assets</i>                                   |                  |                   |               |                   |
| Debt securities                                 | \$               | \$ 146,245        | \$ 447        | \$ 146,692        |
| Equity securities                               | 94,219           | 196               |               | 94,415            |
| Derivatives                                     | 140              | 148               |               | 288               |
| <b>Total Assets Measured at Fair Value</b>      | <b>\$ 94,359</b> | <b>\$ 146,589</b> | <b>\$ 447</b> | <b>\$ 241,395</b> |
| <i>Liabilities</i>                              |                  |                   |               |                   |
| Short sales                                     | \$ 10,249        | \$ 485            | \$            | \$ 10,734         |
| <b>Total Liabilities Measured at Fair Value</b> | <b>\$ 10,249</b> | <b>\$ 485</b>     | <b>\$</b>     | <b>\$ 10,734</b>  |

**December 31, 2013**

|  | Level 1          | Level 2          | Level 3   | Total             |
|--|------------------|------------------|-----------|-------------------|
| <i>(\$ in thousands)</i>                   |                  |                  |           |                   |
| <i>Assets</i>                              |                  |                  |           |                   |
| Debt securities                            | \$               | \$ 47,114        | \$        | \$ 47,114         |
| Equity securities                          | 91,940           |                  |           | 91,940            |
| <b>Total Assets Measured at Fair Value</b> | <b>\$ 91,940</b> | <b>\$ 47,114</b> | <b>\$</b> | <b>\$ 139,054</b> |

The following is a discussion of the valuation methodologies used for the assets and liabilities of the Company's consolidated sponsored investment products measured at fair value.

*Investments of consolidated sponsored investment products* represent the underlying debt and equity securities held in sponsored products which are consolidated by the Company. Equity securities are valued at the official closing price on the exchange on which the securities are traded and are categorized within Level 1. Level 2 investments include certain equity securities for which closing prices are not readily available or are deemed to not reflect readily available market prices and are valued using an independent pricing service as well as most debt securities, which are valued based on quotations received from independent pricing services or from dealers who make markets in such securities. Pricing services do not provide pricing for all securities, and therefore indicative bids from dealers are utilized, which are based on pricing models used by market makers in the security and are also included within Level 2. Level 3 investments include debt securities that are not widely traded, are illiquid and are priced by dealers based on pricing models used by market makers in the security.

The following table is a reconciliation of assets of consolidated sponsored investment products for Level 3 investments for which significant unobservable inputs were used to determine fair value.

|                                      | <b>Level 3<br/>Debt<br/>securities (a)</b> |
|--------------------------------------|--|
| Balance at December 31, 2013         | \$   |
| Purchases                            | 450  |
| Sales                                |  |
| Paydowns                             | (2)  |
| Change in unrealized gain/loss       | (1)  |
| <b>Balance at September 30, 2014</b> | <b>\$ 447</b>                              |

(a) None of the securities in the above table are internally fair valued at September 30, 2014.

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There were no transfers between Level 1, Level 2 and Level 3 during the nine months ended September 30, 2014. Securities held by the consolidated sponsored investment products, with an end-of-period value of \$5.2 million, were transferred from Level 2 to Level 1 during the nine months ended September 30, 2013 due to the availability of unadjusted quoted market prices in active markets.

***Derivatives***

Beginning in the second quarter of 2014, the Company consolidated investment products which include derivative instruments as part of their investment strategies. These derivatives may include futures contracts, options contracts and forward contracts. The fair value of such derivatives at September 30, 2014 was immaterial. The change in fair value of such derivatives, which is recorded in realized and unrealized gain (loss) on investments of consolidated sponsored investment products, net, was immaterial for the three and nine months ended September 30, 2014. In connection with entering into these derivative contracts, these funds may be required to pledge to the broker an amount of cash equal to the initial margin requirements that varies based on the type of derivative. The cash pledged or on deposit is recorded in the Condensed Consolidated Balance Sheet of the Company as Cash pledged or on deposit of consolidated sponsored investment products.

***Short Sales***

Some of the Company's consolidated sponsored investment products may engage in short sales, which are transactions in which a fund sells a security that it does not own (or that it owns but does not intend to deliver) in anticipation that the price of the security will decline. Short sales are recorded in the Condensed Consolidated Balance Sheet within Other liabilities of consolidated sponsored investment products.

**13. New Accounting Standards**

In August 2014, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) No. 2014-13, *Measuring the Financial Assets and Financial Liabilities of a Consolidated Collateralized Financing Entity* ( CFE ). This new guidance requires reporting entities to use the more observable of the fair value of the financial assets or the financial liabilities to measure the financial assets and the financial liabilities of a CFE when a CFE is initially consolidated. It permits entities to make an accounting policy election to apply this same measurement approach after initial consolidation or to apply other GAAP to account for the consolidated CFE's financial assets and financial liabilities. It also prohibits all entities from electing to use the fair value option in ASC 825, *Financial Instruments*, to measure either the financial assets or financial liabilities of a consolidated CFE that is within the scope of this issue. This guidance is effective for fiscal years beginning after December 15, 2015, and interim periods therein. Early adoption is permitted using a modified retrospective transition approach as described in the pronouncement. The Company does not expect this standard to have a material effect on its financial statements.

In May 2014, the FASB issued ASU No. 2014-09 *Revenue from Contracts with Customers* ( ASU 2014-09 ). ASU 2014-09 provides a comprehensive new revenue recognition model requiring a company to recognize revenue to depict the transfer of goods or services to a customer at an amount reflecting the consideration it expects to receive in exchange for those goods or services. Companies may use either a full retrospective or a modified retrospective approach. ASU 2014-09 is effective for the first interim period within annual reporting periods beginning after December 15, 2016. Early adoption is prohibited. The Company is currently evaluating the impact ASU 2014-09 is expected to have on its consolidated financial statements.

In July 2013, the FASB issued ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* ( ASU 2013-11 ). ASU

2013-11 provides guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss or a tax credit carryforward exists. ASU 2013-11 became effective for the Company on January 1, 2014. The Company adopted this standard as of January 1, 2014. The adoption of this standard did not have a material impact on the Company's financial results.

In June 2013, the FASB issued ASU No. 2013-08, *Investment Companies: Amendments to the Scope, Measurement and Disclosure Requirements*. The new standard clarifies the characteristics of an investment company and provides comprehensive guidance for assessing whether an entity is an investment company. The amendments apply to an entity's interim and annual reporting periods in fiscal years that begin after December 15, 2013. The Company adopted this standard as of January 1, 2014. The adoption of this standard did not have a material impact on the Company's financial results.

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

***Cautionary Statement Regarding Forward Looking Statements***

This Quarterly Report on Form 10-Q contains statements that are, or may be considered to be, forward-looking statements within the meaning of The Private Securities Litigation Reform Act of 1995, as amended, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements that are not historical facts, including statements about our beliefs or expectations, are forward-looking statements. These statements may be identified by such forward-looking terminology as expect, estimate, intend, believe, may, will, should, could, continue, project, opportunity, predict, would, potential, likely, target, forecast or similar statements or variations of such terms.

Our forward-looking statements are based on a series of expectations, assumptions and projections about our Company and the markets in which we operate, are not guarantees of future results or performance and involve substantial risks and uncertainty, including assumptions and projections concerning our assets under management, net cash inflows and outflows, operating cash flows and future credit facilities, for all future periods. All of our forward-looking statements contained in this Quarterly Report are as of the date of this Quarterly Report only.

We can give no assurance that such expectations or forward-looking statements will prove to be correct. Actual results may differ materially. We do not undertake or plan to update or revise any such forward-looking statements to reflect actual results, changes in plans, assumptions, estimates or projections, or other circumstances occurring after the date of this Quarterly Report, even if such results, changes or circumstances make it clear that any forward-looking information will not be realized. If there are any future public statements or disclosures by us which modify or impact any of the forward-looking statements contained in or accompanying this Quarterly Report, such statements or disclosures will be deemed to modify or supersede such statements in this Quarterly Report.

Our business and our forward-looking statements involve substantial known and unknown risks and uncertainties, including those discussed under Risk Factors, and Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2013, as amended, and in this Quarterly Report on Form 10-Q, as well as the following risks and uncertainties: (a) any reduction in our assets under management; (b) damage to our reputation; (c) our inability to attract and retain key personnel; (d) the competition we face in our business; (e) adverse regulatory and legal developments; (f) limitations on our deferred tax assets; (g) changes in key distribution or unaffiliated sub advisory relationships; (h) interruptions in service or failure to provide service by third-party service providers; (i) impairment of our goodwill or intangible assets; (j) lack of availability of required and necessary capital on satisfactory terms; (k) liabilities and losses not covered by our insurance policies; and (l) certain other risks and uncertainties described in our 2013 Annual Report on Form 10-K, as amended, or in any of our filings with the Securities and Exchange Commission (SEC). Any occurrence of, or any material adverse change in, one or more risk factors or risks and uncertainties referred to in this Quarterly Report or included in our 2013 Annual Report on Form 10-K, as amended, or our other periodic reports filed with the SEC could materially and adversely affect our operations, financial results, cash flows, prospects and liquidity.

Certain other factors which may impact our continuing operations, prospects, financial results and liquidity or which may cause actual results to differ from such forward-looking statements are discussed or included in the Company's periodic reports filed with the SEC and are available on our website at [www.virtus.com](http://www.virtus.com) under Investor Relations. You are urged to carefully consider all such factors.

***Overview***

We are a provider of investment management and related services to individuals and institutions. We use a multi-manager, multi-style approach, offering investment strategies from affiliated managers and unaffiliated subadvisers, each having its own distinct investment style, autonomous investment process and individual brand. By offering a broad array of products, we believe we can appeal to a greater number of investors, which allows us to have offerings across market cycles through changes in investor preferences. Our earnings are primarily driven by asset-based fees charged for services relating to these various products including investment management, fund administration, distribution and shareholder services.

We offer investment strategies for individual and institutional investors in different product structures and through multiple distribution channels. Our investment strategies are available in a diverse range of styles and disciplines, managed by a collection of boutique investment managers, both affiliated and unaffiliated. We have offerings in various asset classes (domestic and international equity, fixed income and alternative), in all market capitalizations (large, mid and small), in different styles (growth, blend and value) and with various investment approaches (fundamental, quantitative and thematic). Our retail products include open-end mutual funds, closed-end funds, variable insurance funds and separately managed accounts. We also offer certain of our investment strategies to institutional clients.



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We distribute our open-end mutual funds through financial intermediaries. We have broad access in the retail market, with distribution partners that include national and regional broker-dealers, independent broker-dealers and independent financial advisory firms. In many of these firms, we have a number of products that are on firms preferred recommended lists and on fee-based advisory programs. Our sales efforts are supported by regional sales professionals, a national account relationship group and separate teams for the retirement and insurance markets.

Our separately managed accounts are distributed through financial intermediaries and directly by teams at our affiliated managers. Our institutional distribution strategy is an affiliate-centric and coordinated model. Through relationships with consultants, our affiliates target key market segments, including foundations and endowments, corporate and public and private pension plans.

## ***Financial Highlights***

Total revenues were \$117.8 million in the third quarter of 2014, an increase of \$17.4 million, or 17.4% from \$100.4 million in the third quarter of 2013. Total revenues increased in the third quarter of 2014 compared to the same period in the prior year as a result of higher average assets under management and an increase in average fees earned.

Long-term open-end mutual fund sales in the third quarter of 2014 remained relatively balanced among asset strategies, with 26.8% of sales in domestic equity funds, 30.0% in fixed income strategies, 33.1% of sales in international equity funds, and 10.1% in alternative strategies.

Net income attributable to common stockholders in the third quarter of 2014 increased 77.1% to \$37.3 million, from \$21.1 million, in third quarter of 2013, which includes a net tax benefit, related to the resolution of uncertain tax positions, of \$15.5 million in the third quarter of 2014. Earnings per diluted common share increased 57.0% to \$4.02 in the third quarter of 2014 from \$2.56 in the third quarter of 2013.

## ***Assets Under Management***

At September 30, 2014, we managed \$60.9 billion in total assets, representing an increase of \$5.9 billion, or 10.7%, from the \$55.0 billion managed at September 30, 2013 and an increase of \$3.2 billion, or 5.4%, from December 31, 2013. Long-term assets under management, which exclude cash management products, were \$59.5 billion at September 30, 2014, an increase of \$6.1 billion, or 11.6%, from \$53.4 billion at September 30, 2013 and an increase of \$3.3 billion, or 6.0%, from December 31, 2013. Average assets under management, which generally correspond to our fee-earning asset levels, were \$59.3 billion for the nine months ended September 30, 2014, an increase of \$7.5 billion, or 14.6%, from \$51.8 billion for the nine months ended September 30, 2013.

On October 20, 2014, three of our money market funds were liquidated that had a combined \$1.2 billion of assets under management as of September 30, 2014. This liquidation is expected to have no impact on our operating results.

## ***Operating Results***

In the third quarter of 2014, total revenues increased 17.4% to \$117.8 million from \$100.4 million in the third quarter of 2013. This increase was primarily the result of an increase in average assets under management. Operating income increased by 23.1% from \$31.6 million in the third quarter of 2013 to \$38.9 million in the third quarter of 2014, due to

higher levels of average assets under management.

**Table of Contents****Assets Under Management by Product**

The following table summarizes our assets under management by product:

|  | <b>As of September 30,</b> |                    | <b>Change</b>        |              |
|--|----------------------------|--------------------|----------------------|--------------|
|  | <b>2014</b>                | <b>2013</b>        | <b>2014 vs. 2013</b> | <b>%</b>     |
| <i>(\$ in millions)</i>  |                            |                    |                      |              |
| <b>Retail Assets</b>   |                            |                    |                      |              |
| <i>Mutual fund assets</i>  |                            |                    |                      |              |
| Long-term open-end mutual funds                                  | \$ 39,838.8                | \$ 34,173.0        | \$ 5,665.8           | 16.6%        |
| Closed-end funds   | 7,568.1                    | 6,379.4            | 1,188.7              | 18.6%        |
| Money market open-end funds                                      | 1,231.9                    | 1,610.2            | (378.3)              | (23.5)%      |
| Total mutual fund assets   | 48,638.8                   | 42,162.6           | 6,476.2              | 15.4%        |
| Variable insurance funds   | 1,237.5                    | 1,286.8            | (49.3)               | (3.8)%       |
| Separately managed accounts (1)                                  | 6,653.0                    | 6,950.7            | (297.7)              | (4.3)%       |
| <b>Total retail assets</b>                                       | <b>56,529.3</b>            | <b>50,400.1</b>    | <b>6,129.2</b>       | <b>12.2%</b> |
| Total institutional assets (1)                                   | 4,348.3                    | 4,606.9            | (258.6)              | (5.6)%       |
| <b>Total Assets Under Management</b>                             | <b>\$ 60,877.6</b>         | <b>\$ 55,007.0</b> | <b>\$ 5,870.6</b>    | <b>10.7%</b> |
| <b>Average Assets Under Management for the Nine Months Ended</b> | <b>\$ 59,329.0</b>         | <b>\$ 51,780.8</b> | <b>\$ 7,548.2</b>    | <b>14.6%</b> |

(1) Includes assets under management related to option strategies

**Table of Contents****Asset Flows by Product**

The following table summarizes our asset flows by product:

| (\$ in millions)                       | Three Months Ended September 30, |                    | Nine Months Ended September 30, |                    |
|--|----------------------------------|--------------------|---------------------------------|--------------------|
|  | 2014                             | 2013               | 2014                            | 2013               |
| <b>Mutual Funds Long-Term Open-End</b> |                                  |                    |                                 |                    |
| Beginning balance                      | \$ 39,819.1                      | \$ 32,351.2        | \$ 36,367.7                     | \$ 25,827.1        |
| Inflows                                | 3,034.5                          | 4,256.0            | 9,824.3                         | 15,036.5           |
| Outflows                               | (2,382.9)                        | (3,125.3)          | (8,169.8)                       | (7,742.3)          |
| Net flows                              | 651.6                            | 1,130.7            | 1,654.5                         | 7,294.2            |
| Market performance                     | (697.9)                          | 635.2              | 1,604.7                         | 847.6              |
| Other (1)                              | 66.0                             | 55.9               | 211.9                           | 204.1              |
| <b>Ending balance</b>                  | <b>\$ 39,838.8</b>               | <b>\$ 34,173.0</b> | <b>\$ 39,838.8</b>              | <b>\$ 34,173.0</b> |
| <b>Mutual Funds Closed-End</b>         |                                  |                    |                                 |                    |
| Beginning balance                      | \$ 7,530.6                       | \$ 6,422.3         | \$ 6,499.6                      | \$ 6,231.6         |
| Inflows                                | 30.5                             |                    | 493.8                           |                    |
| Outflows                               |                                  |                    |                                 |                    |
| Net flows                              | 30.5                             |                    | 493.8                           |                    |
| Market performance                     | (98.4)                           | 118.7              | 676.1                           | 507.3              |
| Other (1)                              | 105.4                            | (161.6)            | (101.4)                         | (359.5)            |
| <b>Ending balance</b>                  | <b>\$ 7,568.1</b>                | <b>\$ 6,379.4</b>  | <b>\$ 7,568.1</b>               | <b>\$ 6,379.4</b>  |
| <b>Mutual Funds Money Market</b>       |                                  |                    |                                 |                    |
| Beginning balance                      | \$ 1,311.7                       | \$ 1,707.7         | \$ 1,556.6                      | \$ 1,994.1         |
| Other (1)                              | (79.8)                           | (97.5)             | (324.7)                         | (383.9)            |
| <b>Ending balance</b>                  | <b>\$ 1,231.9</b>                | <b>\$ 1,610.2</b>  | <b>\$ 1,231.9</b>               | <b>\$ 1,610.2</b>  |
| <b>Variable Insurance Funds</b>        |                                  |                    |                                 |                    |
| Beginning balance                      | \$ 1,305.5                       | \$ 1,250.8         | \$ 1,311.8                      | \$ 1,295.7         |
| Inflows                                | 20.7                             | 13.1               | 53.2                            | 35.2               |
| Outflows                               | (59.3)                           | (59.4)             | (168.1)                         | (186.1)            |
| Net flows                              | (38.6)                           | (46.3)             | (114.9)                         | (150.9)            |
| Market performance                     | (29.4)                           | 82.3               | 40.6                            | 141.5              |
| Other (1)                              |                                  |                    |                                 | 0.5                |
| <b>Ending balance</b>                  | <b>\$ 1,237.5</b>                | <b>\$ 1,286.8</b>  | <b>\$ 1,237.5</b>               | <b>\$ 1,286.8</b>  |
| <b>Separately Managed Accounts (2)</b> |                                  |                    |                                 |                    |

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|  |                    |                    |                    |                    |
|--|--------------------|--------------------|--------------------|--------------------|
| Beginning balance                        | \$ 6,862.4         | \$ 6,521.7         | \$ 7,433.1         | \$ 5,829.0         |
| Inflows                                  | 319.2              | 312.7              | 1,069.9            | 1,004.3            |
| Outflows                                 | (343.3)            | (283.4)            | (1,832.3)          | (812.7)            |
| Net flows                                | (24.1)             | 29.3               | (762.4)            | 191.6              |
| Market performance                       | (180.5)            | 399.7              | (42.1)             | 961.1              |
| Other (1)                                | (4.8)              |                    | 24.4               | (31.0)             |
| <b>Ending balance</b>                    | <b>\$ 6,653.0</b>  | <b>\$ 6,950.7</b>  | <b>\$ 6,653.0</b>  | <b>\$ 6,950.7</b>  |
| <b><u>Institutional Accounts (2)</u></b> |                    |                    |                    |                    |
| Beginning balance                        | \$ 4,565.0         | \$ 4,399.3         | \$ 4,570.8         | \$ 4,359.5         |
| Inflows                                  | 109.4              | 287.3              | 340.6              | 630.9              |
| Outflows                                 | (236.5)            | (155.0)            | (610.9)            | (481.6)            |
| Net flows                                | (127.1)            | 132.3              | (270.3)            | 149.3              |
| Market performance                       | (45.6)             | 96.4               | 172.4              | 192.4              |
| Other (1)                                | (44.0)             | (21.1)             | (124.6)            | (94.3)             |
| <b>Ending balance</b>                    | <b>\$ 4,348.3</b>  | <b>\$ 4,606.9</b>  | <b>\$ 4,348.3</b>  | <b>\$ 4,606.9</b>  |
| <b><u>Total</u></b>                      |                    |                    |                    |                    |
| Beginning balance                        | \$ 61,394.3        | \$ 52,653.0        | \$ 57,739.6        | \$ 45,537.0        |
| Inflows                                  | 3,514.3            | 4,869.1            | 11,781.8           | 16,706.9           |
| Outflows                                 | (3,022.0)          | (3,623.1)          | (10,781.1)         | (9,222.7)          |
| Net flows                                | 492.3              | 1,246.0            | 1,000.7            | 7,484.2            |
| Market performance                       | (1,051.8)          | 1,332.3            | 2,451.7            | 2,649.9            |
| Other (1)                                | 42.8               | (224.3)            | (314.4)            | (664.1)            |
| <b>Ending balance</b>                    | <b>\$ 60,877.6</b> | <b>\$ 55,007.0</b> | <b>\$ 60,877.6</b> | <b>\$ 55,007.0</b> |

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(1) Represents open-end and closed-end mutual fund distributions, net flows of cash management strategies, net flows and market performance on structured products and net flows from non-sales related activities such as asset acquisitions/(dispositions), marketable securities investments/(withdrawals) and the impact on assets from the use of leverage.

(2) Includes assets under management related to option strategies.

The following table summarizes our assets under management by asset class:

|                         | As of September 30, |                    | Change            |              | % of Total    |               |
|-------------------------|---------------------|--------------------|-------------------|--------------|---------------|---------------|
|                         | 2014                | 2013               | 2014 vs.<br>2013  | %            | 2014          | 2013          |
| <i>(\$ in millions)</i> |                     |                    |                   |              |               |               |
| <b>Asset Class</b>      |                     |                    |                   |              |               |               |
| Equity                  | \$ 35,573.6         | \$ 31,595.9        | \$ 3,977.7        | 12.6%        | 58.4%         | 57.4%         |
| Fixed income            | 16,671.0            | 15,855.2           | 815.8             | 5.1%         | 27.4%         | 28.8%         |
| Alternatives (1)        | 6,769.5             | 4,538.3            | 2,231.2           | 49.2%        | 11.1%         | 8.3%          |
| Other (2)               | 1,863.5             | 3,017.6            | (1,154.1)         | (38.2%)      | 3.1%          | 5.5%          |
| <b>Total</b>            | <b>\$ 60,877.6</b>  | <b>\$ 55,007.0</b> | <b>\$ 5,870.6</b> | <b>10.7%</b> | <b>100.0%</b> | <b>100.0%</b> |

(1) Consists of non-traditional investment strategies such as long/short equity, real estate, master-limited partnerships and other.

(2) Consists of cash management and option strategies. Options strategies were \$522.8 million and \$1,369.1 million at September 30, 2014 and 2013, respectively.

**Average Assets Under Management and Average Basis Points**

The following table summarizes the average assets under management and the average management fee basis points:

|  | Three Months Ended September 30,   |           |                                 |                    |
|--|------------------------------------|-----------|---------------------------------|--------------------|
|  | Average Fees Earned                |           | Average Assets Under Management |                    |
|  | <i>(expressed in basis points)</i> |           | <i>(\$ in millions)</i>         |                    |
|  | 2014                               | 2013      | 2014                            | 2013               |
| <b>Products</b>                        |                                    |           |                                 |                    |
| Mutual Funds Long-Term Open-End (1)(2) | 51                                 | 51        | \$ 40,353.9                     | \$ 33,604.3        |
| Mutual Funds Closed-End                | 67                                 | 63        | 7,571.4                         | 6,442.9            |
| Mutual Funds Money Market Open-End (1) |                                    | 1         | 1,310.1                         | 1,672.5            |
| Variable Insurance Funds (1)           | 52                                 | 57        | 1,285.7                         | 1,280.4            |
| Separately Managed Accounts (3)        | 51                                 | 48        | 6,793.5                         | 6,495.8            |
| Institutional Accounts (3)             | 35                                 | 34        | 4,483.6                         | 4,484.3            |
| <b>All Products</b>                    | <b>51</b>                          | <b>49</b> | <b>\$ 61,798.2</b>              | <b>\$ 53,980.2</b> |

**Nine Months Ended September 30,**  
**Average Fees Earned** **Average Assets Under Management**  
*(expressed in basis points)* *(\$ in millions)*

|  | <b>2014</b> | <b>2013</b> |           | <b>2014</b>     | <b>2013</b>        |
|--|-------------|-------------|-----------|-----------------|--------------------|
| <b>Products</b>                        |             |             |           |                 |                    |
| Mutual Funds Long-Term Open-End (1)(2) | 52          | 51          | \$        | 38,358.5        | \$ 31,480.6        |
| Mutual Funds Closed-End                | 65          | 61          |           | 6,966.6         | 6,486.7            |
| Mutual Funds Money Market Open-End (1) |             | 2           |           | 1,354.7         | 1,737.2            |
| Variable Insurance Funds (1)           | 52          | 57          |           | 1,285.1         | 1,299.7            |
| Separately Managed Accounts (3)        | 52          | 49          |           | 6,825.5         | 6,299.0            |
| Institutional Accounts (3)             | 36          | 33          |           | 4,538.6         | 4,477.6            |
| <b>All Products</b>                    | <b>51</b>   | <b>49</b>   | <b>\$</b> | <b>59,329.0</b> | <b>\$ 51,780.8</b> |

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- (1) Average fees earned are net of non-affiliated subadvisory fees.  
(2) Excludes the impact of consolidated sponsored investment products.  
(3) Includes assets under management related to option strategies.

Long-term and money market open-end mutual fund and variable insurance fund fees are calculated based on average daily net assets. Closed-end fund fees are calculated based on either average weekly or daily net assets. Average fees earned will vary based on several factors, including the asset mix and reimbursements to funds. Separately managed account fees are calculated based on the end of the preceding or current quarter's asset values or on an average of month-end balances. Institutional account fees are calculated based on an average of month-end balances or current quarter's asset values.

The average fee rate earned for the three and nine months ended September 30, 2014 increased as compared to the same period in the prior year as equity and alternative products, which generally have higher fees, represented a higher percentage of our assets under management due to positive flows and market appreciation over the past four quarters. The average fee rate earned on closed-end funds increased for the three and nine months ended September 30, 2014 as compared to the same periods in 2013 due to the full quarter effect of the new Duff & Phelps Select Energy MLP Fund Inc. (NYSE: DSE) on the average fee rate earned. The average fee rate earned on separately managed accounts increased for the nine month period ended September 30, 2014 as compared to same period in 2013 primarily due to the redemption of low fee earning accounts.

**Results of Operations****Summary Financial Data**

|                                 | Three Months Ended September 30, |                |                  |              | Nine Months Ended September 30, |                |                  |              |
|---------------------------------|----------------------------------|----------------|------------------|--------------|---------------------------------|----------------|------------------|--------------|
|                                 | 2014                             | 2013           | 2014 vs.<br>2013 | %            | 2014                            | 2013           | 2014 vs.<br>2013 | %            |
| <i>(\$ in thousands)</i>        |                                  |                |                  |              |                                 |                |                  |              |
| <b>Results of Operations</b>    |                                  |                |                  |              |                                 |                |                  |              |
| Investment management fees      | \$ 78,960                        | \$ 67,119      | \$ 11,841        | 17.6%        | \$ 225,289                      | \$ 189,371     | \$ 35,918        | 19.0%        |
| Other revenue                   | 38,881                           | 33,290         | 5,591            | 16.8%        | 113,172                         | 93,346         | 19,826           | 21.2%        |
| <b>Total revenues</b>           | <b>117,841</b>                   | <b>100,409</b> | <b>17,432</b>    | <b>17.4%</b> | <b>338,461</b>                  | <b>282,717</b> | <b>55,744</b>    | <b>19.7%</b> |
| Operating expenses              | 77,967                           | 67,654         | 10,313           | 15.2%        | 241,555                         | 199,754        | 41,801           | 20.9%        |
| Amortization expense            | 947                              | 1,125          | (178)            | (15.8)%      | 2,851                           | 3,351          | (500)            | (14.9)%      |
| <b>Total operating expenses</b> | <b>78,914</b>                    | <b>68,779</b>  | <b>10,135</b>    | <b>14.7%</b> | <b>244,406</b>                  | <b>203,105</b> | <b>41,301</b>    | <b>20.3%</b> |
| <b>Operating income</b>         | <b>38,927</b>                    | <b>31,630</b>  | <b>7,297</b>     | <b>23.1%</b> | <b>94,055</b>                   | <b>79,612</b>  | <b>14,443</b>    | <b>18.1%</b> |
|                                 | (6,136)                          | 1,720          | (7,856)          | (456.7)%     | 3,435                           | (491)          | 3,926            | (799.6)%     |



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|   |                  |                  |                  |              |                  |                  |                  |              |
|---|------------------|------------------|------------------|--------------|------------------|------------------|------------------|--------------|
| Other (expense) income, net                           |                  |                  |                  |              |                  |                  |                  |              |
| Interest income, net                                  | 2,399            | 519              | 1,880            | 362.2%       | 5,375            | 1,484            | 3,891            | 262.2%       |
| <b>Income before income taxes</b>                     | <b>35,190</b>    | <b>33,869</b>    | <b>1,321</b>     | <b>3.9%</b>  | <b>102,865</b>   | <b>80,605</b>    | <b>22,260</b>    | <b>27.6%</b> |
| Income tax (benefit) expense                          | (1,805)          | 12,567           | (14,372)         | (114.4)%     | 24,311           | 30,335           | (6,024)          | (19.9)%      |
| <b>Net income</b>                                     | <b>36,995</b>    | <b>21,302</b>    | <b>15,693</b>    | <b>73.7%</b> | <b>78,554</b>    | <b>50,270</b>    | <b>28,284</b>    | <b>56.3%</b> |
| Noncontrolling interests                              | 345              | (213)            | 558              | 262.0%       | 267              | 164              | 103              | 62.8%        |
| <b>Net income attributable to common stockholders</b> | <b>\$ 37,340</b> | <b>\$ 21,089</b> | <b>\$ 16,251</b> | <b>77.1%</b> | <b>\$ 78,821</b> | <b>\$ 50,434</b> | <b>\$ 28,387</b> | <b>56.3%</b> |

**Table of Contents****Revenues**

Revenues by source are as follows:

|   | Three Months Ended September 30, |                   |                  |                | Nine Months Ended September 30, |                   |                  |              |
|---|----------------------------------|-------------------|------------------|----------------|---------------------------------|-------------------|------------------|--------------|
|   | 2014                             | 2013              | 2014 vs.<br>2013 | %              | 2014                            | 2013              | 2014 vs.<br>2013 | %            |
| <i>(\$ in thousands)</i>                      |                                  |                   |                  |                |                                 |                   |                  |              |
| <b>Investment management fees</b>             |                                  |                   |                  |                |                                 |                   |                  |              |
| Mutual funds                                  | \$ 64,571                        | \$ 53,527         | \$ 11,044        | 20.6%          | \$ 181,709                      | \$ 149,775        | \$ 31,934        | 21.3%        |
| Separately managed accounts                   | 8,776                            | 7,909             | 867              | 11.0%          | 26,517                          | 23,063            | 3,454            | 15.0%        |
| Institutional accounts                        | 3,938                            | 3,830             | 108              | 2.8%           | 12,076                          | 11,042            | 1,034            | 9.4%         |
| Variable products                             | 1,675                            | 1,853             | (178)            | (9.6)%         | 4,987                           | 5,491             | (504)            | (9.2)%       |
| <b>Total investment management fees</b>       | <b>78,960</b>                    | <b>67,119</b>     | <b>11,841</b>    | <b>17.6%</b>   | <b>225,289</b>                  | <b>189,371</b>    | <b>35,918</b>    | <b>19.0%</b> |
| <b>Distribution and service fees</b>          | <b>23,671</b>                    | <b>20,322</b>     | <b>3,349</b>     | <b>16.5%</b>   | <b>70,049</b>                   | <b>57,007</b>     | <b>13,042</b>    | <b>22.9%</b> |
| <b>Administration and transfer agent fees</b> | <b>14,804</b>                    | <b>12,492</b>     | <b>2,312</b>     | <b>18.5%</b>   | <b>41,819</b>                   | <b>35,248</b>     | <b>6,571</b>     | <b>18.6%</b> |
| <b>Other income and fees</b>                  | <b>406</b>                       | <b>476</b>        | <b>(70)</b>      | <b>(14.7)%</b> | <b>1,304</b>                    | <b>1,091</b>      | <b>213</b>       | <b>19.5%</b> |
| <b>Total revenues</b>                         | <b>\$ 117,841</b>                | <b>\$ 100,409</b> | <b>\$ 17,432</b> | <b>17.4%</b>   | <b>\$ 338,461</b>               | <b>\$ 282,717</b> | <b>\$ 55,744</b> | <b>19.7%</b> |

**Investment Management Fees**

Investment management fees are earned based on a percentage of assets under management and are paid pursuant to the terms of the respective investment management contracts, which generally require monthly or quarterly payments. Investment management fees increased by \$11.8 million, or 17.6%, for the three months ended September 30, 2014 compared to the same period in the prior year due to a 14.5% increase in average assets under management and an increase of 4.1% in the average fee rate earned. The increase in average assets under management for the three months ended September 30, 2014, as compared to the three months ended September 30, 2013, was due primarily to the cumulative four quarter impact of \$1.6 billion in net flows and \$4.7 billion of market appreciation. Revenues increased at a higher rate than assets under management due to the increase in the average fee rate earned. Equity and alternative assets, which generally earn a higher average fee rate, represented 69.5% of total assets under management at September 30, 2014 compared to 65.7% at September 30, 2013.

Investment management fees increased by \$35.9 million, or 19.0%, for the nine months ended September 30, 2014 compared to the same period in the prior year due to a 14.6% increase in average assets under management and an increase of approximately 4.1% in the average fee rate earned. The increase in average assets under management for the nine months ended September 30, 2014 was due primarily to the cumulative four quarter impact of \$1.6 billion in net flows and \$4.7 billion of market appreciation on total assets under management. Revenues increased at a higher rate than assets under management due to the increase in the average fee rate earned.

***Distribution and Service Fees***

Distribution and service fees, which are asset-based fees earned from open-end mutual funds and variable insurance funds for distribution services, increased by \$3.3 million or 16.5% and \$13.0 million or 22.9%, respectively, for the three and nine months ended September 30, 2014, respectively, compared to the same periods in the prior year due to higher average long-term open-end assets under management. The increase in fees also resulted in a corresponding increase in distribution and administrative expenses, primarily driven by increased payments to third-party distribution partners for providing services to investors in our sponsored funds, including marketing support services.

***Administration and Transfer Agent Fees***

Administration and transfer agent fees represent fees earned for fund administration and shareholder services from our open-end mutual funds, variable insurance funds and certain of our closed-end funds. Fund administration and transfer agent fees increased \$2.3 million or 18.5% and \$6.6 million or 18.6%, respectively, for the three and nine months ended September 30, 2014, respectively, compared to the same periods in the prior year due to higher average long-term open-end assets under management.

**Table of Contents****Other Income and Fees**

Other income and fees primarily represent contingent sales charges earned from redemptions of certain shares sold without a front-end sales charge and fees earned for the distribution of unaffiliated products. Other income and fees decreased \$0.1 million or 14.7% and increased \$0.2 million or 19.5%, respectively, for the three and nine months ended September 30, 2014 compared to the same periods in the prior year.

**Operating Expenses**

Operating expenses by category were as follows:

|   | Three Months Ended September 30, |                  |                  |              | Nine Months Ended September 30, |                   |                  |              |
|---|----------------------------------|------------------|------------------|--------------|---------------------------------|-------------------|------------------|--------------|
|   | 2014                             | 2013             | 2014 vs.<br>2013 | %            | 2014                            | 2013              | 2014 vs.<br>2013 | %            |
| <i>(\$ in thousands)</i>                    |                                  |                  |                  |              |                                 |                   |                  |              |
| <b>Operating expenses</b>                   |                                  |                  |                  |              |                                 |                   |                  |              |
| Employment expenses                         | \$ 35,246                        | \$ 33,022        | \$ 2,224         | 6.7%         | \$ 105,756                      | \$ 98,311         | \$ 7,445         | 7.6%         |
| Distribution and administrative expenses    | 29,180                           | 25,253           | 3,927            | 15.6%        | 96,139                          | 71,133            | 25,006           | 35.2%        |
| Other operating expenses                    | 12,534                           | 8,769            | 3,765            | 42.9%        | 37,326                          | 28,325            | 9,001            | 31.8%        |
| Restructuring and severance                 | 294                              |                  | 294              | N/A          | 294                             | 203               | 91               | 44.8%        |
| Depreciation and other amortization expense | 713                              | 610              | 103              | 16.9%        | 2,040                           | 1,782             | 258              | 14.5%        |
| Amortization expense                        | 947                              | 1,125            | (178)            | (15.8)%      | 2,851                           | 3,351             | (500)            | (14.9)%      |
| <b>Total operating expenses</b>             | <b>\$ 78,914</b>                 | <b>\$ 68,779</b> | <b>\$ 10,135</b> | <b>14.7%</b> | <b>\$ 244,406</b>               | <b>\$ 203,105</b> | <b>\$ 41,301</b> | <b>20.3%</b> |

**Employment Expenses**

Employment expenses primarily consist of fixed and variable compensation and related employee benefit costs. Employment expenses for the three months ended September 30, 2014 were \$35.2 million, which represented an increase of \$2.2 million, or 6.7%, compared to the same period in the prior year. The increase was primarily due to personnel additions related to the growth of the business, increases in profit-based variable incentive compensation, payroll taxes and other benefits resulting from higher profits.

Employment expenses for the nine months ended September 30, 2014 were \$105.8 million, an increase of \$7.4 million, or 7.6%, compared to the same period in the prior year. The increase was primarily due to personnel additions related to the growth of the business, increases in profit-based variable incentive compensation and payroll taxes resulting from higher profits.

**Distribution and Administrative Expenses**

Distribution and administrative expenses primarily consist of payments to third-party distribution partners for providing services to investors in our sponsored funds. These payments are primarily based on percentages of assets under management. These expenses also include the amortization of deferred sales commissions related to up-front commissions on shares sold without a front-end sales charge to shareholders. The deferred sales commissions are amortized on a straight line basis over the periods in which commissions are generally recovered from distribution fee revenues and contingent sales charges received from shareholders of the funds upon redemption of their shares. Distribution and administrative expenses increased by \$3.9 million, or 15.6%, in the three months ended September 30, 2014, and \$25.0 million or 35.2% during the nine months ended September 30, 2014, compared to the same periods in the prior year. The increase during the three month period was primarily due to an increase in assets under management. The increase in the nine-month period was primarily attributable to closed-end fund structuring costs of \$9.6 million incurred in connection with the launch of the new DSE closed-end fund during the second quarter of 2014 as well as higher overall assets under management.

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***Other Operating Expenses***

Other operating expenses primarily consist of investment research and technology costs, professional fees, travel and distribution related costs, rent and occupancy expenses and other miscellaneous costs. Other operating expenses for the three months ended September 30, 2014 increased \$3.8 million, or 42.9%, to \$12.5 million as compared to \$8.8 million for the same period in the prior year primarily due to increases in expenses related to higher professional fees and costs related to the transition of middle-and-back office systems to a third party service provider.

Other operating expenses for the nine months ended September 30, 2014 increased \$9.0 million, or 31.8%, to \$37.3 million as compared to \$28.3 million for the same period in the prior year primarily due to increases in investment research costs, expenses related to organizational, start-up and distribution costs associated with the launch of new funds, higher professional fees and costs related to the transition of middle-and-back office systems to a third party service provider.

***Restructuring and Severance***

We incurred \$0.3 million of restructuring and severance costs in both the three and nine months ended September 30, 2014 resulting from staff eliminations.

***Depreciation and Other Amortization Expense***

Depreciation and other amortization expense primarily consists of the straight-line depreciation of furniture, equipment, and leasehold improvements over their estimated useful lives. Depreciation and other amortization expense was \$0.7 million and \$2.0 million during the three and nine month periods ended September 30, 2014, respectively, consistent with depreciation expense during the same periods in the prior year.

***Amortization Expense***

Amortization expense primarily consists of the straight-line amortization of definite-lived intangible assets over their estimated useful lives. Amortization expense was \$0.9 million and \$2.9 million during the three and nine month periods ended September 30, 2014, respectively, representing a decrease of \$0.2 and \$0.5 million, respectively, compared to the same periods in the prior year. The decrease was primarily due to certain definite-lived intangible assets becoming fully amortized during the prior corresponding periods.

***Other (Expense) Income, net***

Other (expense) income, net consists primarily of realized and unrealized gains and losses recorded on trading securities and investments of consolidated sponsored investment products. Other (expense) income, net decreased \$7.9 million to \$6.1 million for the three month period ended September 30, 2014 from income of \$1.7 million for the three month period ended September 30, 2013 due to realized and unrealized losses on investments by us and our consolidated sponsored investment products during the period. Other (expense) income, net increased \$3.9 million to income of \$3.4 million for the nine month period ended September 30, 2014 compared to an expense of \$0.5 million for the same period in the prior year due to overall gains on investments by us and our consolidated sponsored investment products during the nine months ended September 30, 2014.

***Interest Income, net***

Interest income, net consists of interest and dividend income earned on cash equivalents, investments and the investments of our consolidated sponsored investment products. Interest income, net increased \$1.9 million and \$3.9 million for the three and nine month periods ended September 30, 2014, respectively, compared to the same periods in the prior year. The increase in interest income, net was primarily due to higher interest and dividend income earned on our investments and the investments of our consolidated sponsored investment products, which increased by \$26.4 million and \$102.1 million for the nine months ended September 30, 2014, respectively, from December 31, 2013.

***Income Tax (Benefit) Expense***

The provision for income taxes reflects U.S. federal, state and local taxes at an estimated effective tax rate of (5.1)% and 37.1% and 23.6% and 37.6% for the three and nine months ended September 30, 2014 and 2013, respectively. Our effective tax rate for the three and nine months ended September 30, 2014 was impacted by a net tax benefit of approximately \$15.5 million due to the settlement of the audit of the Company's 2011 federal corporate income tax return. The net benefit was comprised of the recognition of the benefits from uncertain tax positions of approximately \$31.0 million and a reduction of the deferred tax assets of approximately \$15.5 million, which was related to a loss resulting from the past dissolution of a subsidiary.

**Table of Contents****Liquidity and Capital Resources***Certain Financial Data*

The following table summarizes certain key financial data relating to our liquidity and capital resources:

|  | <b>September 30,<br/>2014</b> | <b>December 31,<br/>2013</b> | <b>Change<br/>2014 vs. 2013 %</b> |         |
|--|-------------------------------|------------------------------|-----------------------------------|---------|
| <i>(\$ in thousands)</i>                                     |                               |                              |                                   |         |
| <b>Balance Sheet Data</b>                                    |                               |                              |                                   |         |
| Cash and cash equivalents                                    | \$ 172,709                    | \$ 271,014                   | \$ (98,305)                       | (36.3)% |
| Investments  | 63,659                        | 37,258                       | 26,401                            | 70.9%   |
| Deferred taxes, net  | 59,668                        | 64,500                       | (4,832)                           | (7.5)%  |
| Dividends payable  | 4,229                         |                              | 4,229                             | 100.0%  |
| Total equity   | 560,430                       | 492,868                      | 67,562                            | 13.7%   |
| Net assets of consolidated sponsored investment products (1) | 217,294                       | 98,433                       | 118,861                           | 120.8%  |

- (1) Net assets of consolidated sponsored investment products are comprised of \$263.4 million and \$149.2 million of total assets, \$23.8 million and \$8.6 million of total liabilities and \$22.3 million and \$42.2 million of redeemable noncontrolling interest at September 30, 2014 and December 31, 2013, respectively.

|                               | <b>Nine Months Ended September, 30</b> |             | <b>Change</b>        |          |
|-------------------------------|--|-------------|----------------------|----------|
|                               | <b>2014</b>                            | <b>2013</b> | <b>2014 vs. 2013</b> | <b>%</b> |
| <i>(in thousands)</i>         |  |             |                      |          |
| <b>Cash Flow Data:</b>        |  |             |                      |          |
| <i>Provided by (used in):</i> |  |             |                      |          |
| Operating Activities          | \$ (102,288)                           | \$ 26,079   | \$ (128,367)         | (492.2)% |
| Investing Activities          | (7,440)                                | (5,829)     | (1,611)              | 27.6%    |
| Financing Activities          | 11,947                                 | 161,031     | (149,084)            | (92.6)%  |

**Short-Term Capital Requirements**

Our short-term capital requirements, which we consider to be those capital requirements due within one year, include payment of annual incentive compensation, dividends to stockholders, income tax payments and other operating expenses, primarily consisting of investment research and technology costs, professional fees, distribution and occupancy costs. Incentive compensation, which is generally the Company's largest annual operating cash payment, is paid in the first quarter of the year. In the first quarter of 2014 and 2013, we paid approximately \$45.0 million and \$33.0 million, respectively, in incentive compensation earned during the years ended December 31, 2013 and 2012, respectively. In August 2014, we paid a cash dividend on our common stock in the amount of \$0.45 per share totaling \$4.1 million. On August 13, 2014, our Board of Directors approved a cash dividend on our common stock in the amount of \$0.45 per share to stockholders of record as of October 31, 2014, estimated at \$4.1 million, to be paid on November 14, 2014. Short-term capital requirements may also be affected by employee tax withholding payments related to net share settlement of equity awards. The Company paid \$9.5 million and \$7.5 million in employee tax withholding obligations related to net share settlements in the nine months ended September 30, 2014 and 2013,



respectively. These net share settlements had the effect of share repurchases by the Company as they reduced the number of shares that otherwise would have been issued as a result of the vesting or exercise. The amount we pay in future periods will vary based on our stock price, the number of equity awards net settled during the period and whether we and our employees elect to satisfy withholding taxes through net share settlement.

### *Uses and Sources of Capital*

We expect that our main uses of cash will be to (i) invest in our organic growth, including our distribution efforts and closed-end fund launches; (ii) seed new investment strategies and mutual funds to introduce new products or to enhance distribution access; (iii) return of capital to stockholders through acquisition of shares of our common stock, payment of dividends or other means; (iv) fund ongoing and potential investments in our infrastructure to achieve greater economies of scale and a more efficient overall cost structure; and (v) invest in inorganic growth opportunities as they arise.

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**Table of Contents*****Capital and Reserve Requirements***

VP Distributors, LLC ( VPD ), a wholly-owned subsidiary of the Company, is a broker-dealer registered with the SEC and is therefore subject to certain rules regarding minimum net capital, as defined by those rules. VPD is required to maintain a ratio of aggregate indebtedness to net capital, as defined, which may not exceed 15 to 1 and must also maintain a minimum amount of net capital. Failure to meet these requirements could result in adverse consequences to us including additional reporting requirements, a lower required ratio of aggregate indebtedness to net capital or interruption of our business. At September 30, 2014 and December 31, 2013, the ratio of aggregate indebtedness to net capital of our broker-dealer was below the maximum allowed, and its net capital was significantly greater than the required minimum.

***Balance Sheet***

Cash and cash equivalents consist of cash in banks and money market fund investments. Cash and cash equivalents typically increase in the second, third and fourth quarters of the year as we record, but do not pay, variable incentive compensation. Annual incentive compensation is paid in the first quarter of the year. Investments consist primarily of investments in our affiliated mutual funds. Consolidated sponsored investment products primarily represent investment products we sponsor and where we own a majority of the voting interest in the entity. As of September 30, 2014, we consolidated a total of 12 sponsored investment products. At both September 30, 2014 and December 31, 2013, we had no debt outstanding.

***Operating Cash Flow***

Net cash used in operating activities of \$102.3 million for the nine months ended September 30, 2014 decreased by \$128.4 million from net cash provided by operating activities of \$26.1 million in the same period in the prior year due primarily to increases in net purchases of investments of consolidated sponsored investment products, including trading securities and increases in tax payments and structuring fees, partially offset by cash generated from increased operating profitability.

***Investing Cash Flow***

Net cash used in investing activities consists primarily of capital expenditures and other investing activities related to our business operations. Net cash used in investing activities of \$7.4 million for the nine months ended September 30, 2014 increased by \$1.6 million from net cash used in investing activities of \$5.8 million for the same period in the prior year due to an asset acquisition in the current year.

***Financing Cash Flow***

Cash flows used in financing activities consist primarily of repurchases of our common stock and payments to settle tax withholding obligations for the net share settlement of employee share transactions, payments of dividends and contributions to noncontrolling interests related to our consolidated sponsored investment products. Net cash provided by financing activities decreased \$149.1 million to \$11.9 million for the nine months ended September 30, 2014 compared to \$161.0 million for the same period in the prior year. The primary reason for the decrease was due to proceeds of \$191.8 million from the issuance of 1.3 million shares of our common stock in the prior year with no such issuance in the current year period partially offset by the repayment of the entire \$15.0 million of debt. During the first nine months of 2014, we received \$25.1 million in excess tax benefits from stock-based compensation with no amount in the prior year. Contributions from noncontrolling interests, net increased \$13.5 million to \$24.9 million during the first nine months of 2014 compared to \$11.4 million in the prior year due to our increased investments in consolidated

sponsored investment products.

***Debt***

Our Credit Facility, as amended and restated, has a five-year term expiring in September 2017 and provides borrowing capacity of up to \$75.0 million with a \$7.5 million sub-limit for the issuance of standby letters of credit. In addition, the Credit Facility provides for a \$50.0 million increase provision conditioned on approval by the lending group. The Credit Facility is secured by substantially all of our assets. At September 30, 2014 and December 31, 2013, no amount was outstanding under the Credit Facility. As of September 30, 2014, we had the capacity to draw on the entire \$75.0 million available under the Credit Facility. The Credit Facility contains financial covenants with respect to leverage and interest coverage and requires us to pay an annual commitment fee on any unused portion. We were in compliance with all debt covenants as of September 30, 2014.

***Contractual Obligations***

Our contractual obligations are summarized in our 2013 Annual Report on Form 10-K, as amended. As of September 30, 2014, there have been no material changes outside of the ordinary course in our contractual obligations since December 31, 2013.

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**Table of Contents*****Critical Accounting Policies and Estimates***

Our financial statements and the accompanying notes are prepared in accordance with Generally Accepted Accounting Principles, which requires the use of estimates. Actual results will vary from these estimates. A discussion of our critical accounting policies and estimates is included in Management's Discussion and Analysis of Financial Condition and Results of Operations in our 2013 Annual Report on Form 10-K, as amended. A complete description of our significant accounting policies is included in our 2013 Annual Report on Form 10-K, as amended. There were no changes in our critical accounting policies in the nine months ended September 30, 2014.

***Recently Issued Accounting Pronouncements***

In August 2014, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) No. 2014-13, *Measuring the Financial Assets and Financial Liabilities of a Consolidated Collateralized Financing Entity* ( CFE ). This new guidance requires reporting entities to use the more observable of the fair value of the financial assets or the financial liabilities to measure the financial assets and the financial liabilities of a CFE when a CFE is initially consolidated. It permits entities to make an accounting policy election to apply this same measurement approach after initial consolidation or to apply other GAAP to account for the consolidated CFE's financial assets and financial liabilities. It also prohibits all entities from electing to use the fair value option in ASC 825, *Financial Instruments*, to measure either the financial assets or financial liabilities of a consolidated CFE that is within the scope of this issue. This guidance is effective for fiscal years beginning after December 15, 2015, and interim periods therein. Early adoption is permitted using a modified retrospective transition approach as described in the pronouncement. We do not expect this standard to have a material effect on our financial statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers* ( ASU 2014-09 ). ASU 2014-09 provides a comprehensive new revenue recognition model requiring a company to recognize revenue to depict the transfer of goods or services to a customer at an amount reflecting the consideration it expects to receive in exchange for those goods or services. Companies may use either a full retrospective or a modified retrospective approach. ASU 2014-09 is effective for the first interim period within annual reporting periods beginning after December 15, 2016. Early adoption is prohibited. We are currently evaluating the impact ASU 2014-09 is expected to have on our consolidated financial statements.

In July 2013, the FASB issued ASU No. 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* ( ASU 2013-11 ). ASU 2013-11 provides guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. ASU 2013-11 is effective for us on January 1, 2014. We adopted this standard as of January 1, 2014. The adoption of this standard did not have a material impact on our financial results.

In June, 2013, the FASB issued ASU No. 2013-08, *Investment Companies: Amendments to the Scope, Measurement and Disclosure Requirements*. The new standard clarifies the characteristics of an investment company and provides comprehensive guidance for assessing whether an entity is an investment company. The amendments apply to an entity's interim and annual reporting periods in fiscal years that begin after December 15, 2013. We adopted this standard as of January 1, 2014. The adoption of this standard did not have a material impact on our financial results.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk*****Market Risk***

Substantially all of our revenues are derived from investment management, distribution and service, and administration and transfer agent fees, which are based on the market value of assets under management. Accordingly, a decline in the prices of securities would cause our revenues and income to decline due to a decrease in the value of the assets under management. In addition, a decline in security prices could cause our clients to withdraw their investments in favor of other investments offering higher returns or lower risk, which would cause our revenues and income to decline.

We are also subject to market risk due to a decline in the market value of our investments, consisting primarily of marketable securities. At September 30, 2014, the fair value of marketable securities, excluding redeemable noncontrolling interests, was \$268.1 million. Assuming a 10.0% increase or decrease in the fair value of marketable securities at September 30, 2014, our net income attributable to common stockholders would change by \$16.4 million, and our total comprehensive income would change by \$16.5 million, in each case for the nine months ended September 30, 2014.

### ***Interest Rate Risk***

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. At September 30, 2014, we were exposed to interest rate risk as a result of holding investments in fixed-income sponsored funds of \$103.3 million. Assuming a 1.0% increase or decrease in interest rates, the fair value of our fixed income investments would change by \$3.6 million for the nine months ended September 30, 2014.

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At September 30, 2014, we had no amounts outstanding under our Credit Facility. Amounts outstanding under the Credit Facility bear interest at an annual rate equal to, at our option, either LIBOR for interest periods of one, two, three or six months or an alternate base rate (as defined in the Credit Facility agreement), plus, in each case, an applicable margin, that ranges from 0.75% to 2.50%.

## **Item 4. Controls and Procedures**

### **Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures designed to ensure that information required to be disclosed in reports filed under the Securities Exchange Act of 1934, as amended (the Exchange Act), is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

Our management, with the participation of our Chief Executive Officer and our Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on their evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, because a material weakness in the Company's internal control over financial reporting existed at December 31, 2013 and had not been remediated by the end of the period covered by this Quarterly Report on Form 10-Q, the Company's disclosure controls and procedures were not effective as of the end of the period covered by this Quarterly Report on Form 10-Q. This material weakness in the Company's internal control over financial reporting and the Company's remediation efforts are described below.

#### *Material Weakness in Internal Control Over Financial Reporting*

The Company's management, including our Chief Executive Officer and Chief Financial Officer have identified a material weakness in the Company's internal control over financial reporting. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. The Company failed to design controls upon the adoption of ASC 810-10, as amended by ASU 2009-17, to assess whether it has the potential to receive collateral management fees that could be significant and failed to design appropriate controls over the requirement to continuously reassess its variable interest entities at appropriate levels of precision. As a result, the Company's analysis of whether it has the potential to receive collateral management fees that could be significant was not at the appropriate levels of precision to determine whether to consolidate certain variable interest entities. This material weakness could result in a failure to consolidate certain variable interest entities that could result in a material misstatement to the annual or interim consolidated financial statements that would not be prevented or detected.

Based on this assessment and the material weakness described above, management concluded that the Company's internal control over financial reporting was not effective as of December 31, 2013 and had not been remediated by the end of the period covered by this Quarterly Report on Form 10-Q. However, the Company has concluded that the existence of this material weakness did not result in a material misstatement of the Company's previously issued financial statements or the Company's financial statements included in this Quarterly Report on Form 10-Q.

#### *Remediation Measures*

To address the material weakness described above, during the period covered by this Quarterly Report on Form 10-Q, the Company designed and implemented new and enhanced controls to ensure that the primary beneficiary assessment for variable interest entities is assessed at the appropriate level of precision and that in-house accounting personnel have training to ensure they have the relevant expertise related to the consolidation of variable interest entities.

We believe the actions described above will be sufficient to remediate the identified material weakness and strengthen our internal control over financial reporting. However, the new and enhanced controls have not operated for a sufficient amount of time to conclude that the material weakness has been remediated. We will continue to monitor the effectiveness of these controls and will make any further changes management determines appropriate.

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**Changes in Internal Control over Financial Reporting**

As disclosed above under Remediation Measures, there were changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II OTHER INFORMATION**

**Item 1. Legal Proceedings**

The Company is regularly involved in litigation and arbitration as well as examinations, inquiries, and investigations by various regulatory bodies, including the SEC, involving its compliance with, among other things, securities laws, client investment guidelines, laws governing the activities of broker-dealers and other laws and regulations affecting its products and other activities. Legal and regulatory matters of this nature may involve the Company's activities as an employer, issuer of securities, investor, investment adviser, broker-dealer or taxpayer. The Company cannot predict the ultimate outcome of such legal claims or matters or in certain instances provide reasonable ranges of potential losses. As of the date of this report, the Company believes that the outcomes of its legal or regulatory matters are not likely, either individually or in the aggregate, to have a material adverse effect on its consolidated financial condition. However, in the event of unexpected subsequent developments and given the inherent unpredictability of these legal and regulatory matters, the Company can provide no assurance that its assessment of any claim, dispute, regulatory examination or investigation or other legal matter will reflect the ultimate outcome and an adverse outcome in certain matters could, from time to time, have a material adverse effect on the Company's results of operations or cash flows in particular quarterly or annual periods.

**Item 1A. Risk Factors**

There have been no material changes to our risk factors previously reported in our 2013 Annual Report on Form 10-K, as amended.



**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

In the fourth quarter of 2010, we implemented a share repurchase program authorizing the repurchase of 350,000 shares of our common stock, which was renewed in the second quarter of 2013 permitting the repurchase of an additional 350,000 shares of our common stock prior to May 21, 2016. Under the terms of the program, we may repurchase shares of our common stock from time to time at our discretion through open market repurchases and/or privately negotiated transactions, depending on price and prevailing market and business conditions. The program is intended to generally offset dilution caused by shares issued under equity-based plans. The program may be suspended or terminated at any time.

The following table sets forth information regarding our share repurchases in each month during the quarter ended September 30, 2014:

| Period                 | Total number of shares repurchased | Average price paid per share (1) | Maximum number of shares that  |  |
|------------------------|------------------------------------|----------------------------------|--|--|
|                        |                                    |                                  | Total number of shares repurchased as part of publicly announced plans or programs (2) | may yet be repurchased under the plans or programs (2) |
| July 1 - 31, 2014      |                                    | \$                               |  | 283,087  |
| August 1 - 31, 2014    | 30,000                             | \$ 208.53                        | 30,000   | 253,087  |
| September 1 - 30, 2014 | 39,961                             | \$ 187.64                        | 39,961   | 213,126  |

(1) Average price per share is calculated on a settlement basis and excludes commissions.

(2) The share repurchases above were completed pursuant to an expanded program announced in May 2013.

There were no unregistered sales of equity securities during the period covered by this Quarterly Report. Shares of our common stock purchased by participants in our Employee Stock Purchase Plan were delivered to participant accounts via open market purchases at fair value by the third-party administrator under the plan. We do not reserve shares for this plan or discount the purchase price of the shares.

For the nine months ended September 30, 2014, we paid \$9.5 million in employee tax withholding obligations related to employee share transactions.

**Item 6. Exhibits**

| Exhibit Number | Description   |
|----------------|---|
| 31.1           | Certification of the Registrant's Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.2           | Certification of the Registrant's Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |

- 32.1 Certification of the Registrant's Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 The following information formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets (Unaudited) as of September 30, 2014 and December 31, 2013, (ii) Condensed Consolidated Statements of Operations (Unaudited) for the three and nine months ended September 30, 2014 and 2013, (iii) Condensed Consolidated Statements of Comprehensive Income (Unaudited) for the three and nine months ended September 30, 2014 and 2013, (iv) Condensed Consolidated Statements of Cash Flows (Unaudited) for the nine months ended September 30, 2014 and 2013, (v) Condensed Consolidated Statements of Changes in Stockholders Equity (Unaudited) for the nine months ended September 30, 2014 and 2013 and (vi) Notes to Condensed Consolidated Financial Statements (Unaudited).

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**SIGNATURES**

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

Dated: November 6, 2014

**VIRTUS INVESTMENT PARTNERS, INC.**  
(Registrant)

By: /s/ Michael A. Angerthal  
**Michael A. Angerthal**  
**Executive Vice President and Chief**  
**Financial Officer (Principal Financial**  
**Officer and Principal Accounting**  
**Officer)**