

Edgar Filing: CBOE Holdings, Inc. - Form 10-Q

CBOE Holdings, Inc.  
Form 10-Q  
November 08, 2011  
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
Form 10-Q

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

For the quarterly period ended September 30, 2011

OR

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

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

Commission File No. 001-34774

CBOE HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Delaware

20-5446972

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

400 South LaSalle Street

60605

Chicago, Illinois

(Address of principal executive offices)

(Zip Code)

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

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

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date:

Class

Outstanding at September 30, 2011

Unrestricted Common Stock, par value \$0.01

89,920,627 shares



Table of Contents

CBOE HOLDINGS, INC.

INDEX

	Page
<u>PART I - FINANCIAL INFORMATION</u>	<u>6</u>
<u>Item 1. Condensed Consolidated Financial Statements (Unaudited)</u>	<u>6</u>
<u>Condensed Consolidated Statements of Income — Three and Nine Months Ended September 30, 2011 and 2010</u>	<u>7</u>
<u>Condensed Consolidated Balance Sheets — September 30, 2011 and December 31, 2010</u>	<u>8</u>
<u>Condensed Consolidated Statement of Stockholders' Equity — Nine Months Ended September 30, 2011</u>	<u>9</u>
<u>Condensed Consolidated Statements of Cash Flows — Nine Months Ended September 30, 2011 and 2010</u>	<u>10</u>
<u>Notes to Condensed Consolidated Financial Statements</u>	<u>11</u>
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>17</u>
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	<u>30</u>
<u>Item 4. Controls and Procedures</u>	<u>30</u>
<u>PART II - OTHER INFORMATION</u>	<u>31</u>
<u>Item 1. Legal Proceedings</u>	<u>31</u>
<u>Item 1A. Risk Factors</u>	<u>31</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>31</u>
<u>Item 3. Defaults Upon Senior Securities</u>	<u>31</u>
<u>Item 4. [Removed and Reserved]</u>	<u>31</u>
<u>Item 5. Other Information</u>	<u>31</u>
<u>Item 6. Exhibits</u>	<u>31</u>
<u>Signatures</u>	<u>32</u>
<u>Exhibits</u>	<u>33</u>

Table of Contents

CERTAIN DEFINED TERMS

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

“CBOE Holdings” or the “Company” refers to CBOE Holdings, Inc. and its subsidiaries after the completion of the restructuring transaction, which occurred on June 18, 2010. For periods prior to the restructuring transaction, the “Company” refers to CBOE and its subsidiaries.

“CBOE” or the “Exchange” refers to (1) prior to the completion of the restructuring transaction, Chicago Board Options Exchange, Incorporated, a Delaware non-stock corporation, and (2) after the completion of the restructuring transaction, Chicago Board Options Exchange, Incorporated, a Delaware stock corporation. CBOE became a wholly-owned subsidiary of CBOE Holdings on June 18, 2010.

“C2” refers to C2 Options Exchange, Incorporated, which became a wholly-owned subsidiary of CBOE Holdings on June 18, 2010.

“CFE” refers to CBOE Futures Exchange, LLC, which became a wholly-owned subsidiary of CBOE Holdings on June 18, 2010.

The “restructuring transaction” refers to the transaction on June 18, 2010 in which CBOE converted from a Delaware non-stock corporation owned by its Members to a Delaware stock corporation and a wholly-owned subsidiary of CBOE Holdings, a Delaware stock corporation.

• “Settlement Agreement” means the Stipulation of Settlement, as amended, approved by the Court of Chancery of the State of Delaware in the Delaware Action. The Delaware Action referred to the lawsuit, which was entitled CME Group Inc. et al. v. Chicago Board Options Exchange, Incorporated et al.

• “Member” or “Members” refers to, prior to the completion of the restructuring transaction, any person or organization (or any designee of any organization) that held a membership in CBOE.

• “Our exchanges” refers to CBOE, C2 and CFE and “our options exchanges” refers to CBOE and C2.

• “We,” “us” or “our” refers to (1) prior to the completion of the restructuring transaction, CBOE, and, as the context may require, CBOE Holdings, and (2) after the completion of the restructuring transaction, CBOE Holdings.

All references to “options” or “options contracts” in the text of this document refer to exchange-traded options and all references to “futures” refer to futures contracts or options on futures contracts.

Table of Contents

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involve a number of risks and uncertainties. You can identify these statements by forward-looking words such as “may,” “might,” “should,” “expect,” “plan,” “anticipate,” “believe,” “estimate,” “predict,” “potentially,” “continue,” and the negative of these terms and other comparable terminology. All statements that reflect our expectations, assumptions or projections about the future other than statements of historical fact are forward-looking statements, including statements in the “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” These forward-looking statements, which are subject to known and unknown risks, uncertainties and assumptions about us, may include projections of our future financial performance based on our growth strategies and anticipated trends in our business. These statements are only predictions based on our current expectations and projections about future events. There are important factors that could cause our actual results, level of activity, performance or achievements to differ materially from that expressed or implied by the forward-looking statements. In particular, you should consider the risks and uncertainties described under “Risk Factors” in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2010, Part II, Item 1A of this Quarterly Report on Form 10-Q and our other filings with the SEC.

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

Some factors that could cause actual results to differ include:

- legislative or regulatory changes affecting the options markets, including a possible cap of transaction fees;
- changes in law or government policy, including changes relating to enacted or proposed legislation, and the rules promulgated thereunder, relating to the economic crisis;
- increasing competition by foreign and domestic entities, including increased competition from new entrants into our markets and consolidation of existing entities;
- loss of our exclusive licenses to list certain index options;
- decreases in the amount of trading volumes on our exchanges;
- our ability to continue introducing competitive new products and services on a timely, cost-effective basis, including through our electronic trading capabilities, and our ability to maintain the competitiveness of our existing products and services;
- our ability to generate incremental operating revenue by making trading access available in exchange for a fee;
- changes in price levels and volatility in the derivatives markets and in the equity markets in general;
- economic, political and market conditions;
- our ability to adjust our fixed costs and expenses if our revenues decline;

our ability to maintain existing customers, develop strategic relationships and attract new customers;

our ability to operate our business without violating the intellectual property rights of others and the costs associated with protecting our intellectual property rights;

our ability to keep pace with rapid technological developments, including our ability to complete the development and implementation of the enhanced functionality required by our customers;

our ability to accommodate increases in trading volume and order transaction traffic without failure or degradation of performance of our systems;

4

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Table of Contents

our ability to maintain our growth effectively;

our ability to manage our reputation and brand name;

our ability to generate revenue from our market data, which may be reduced or eliminated by the growth of electronic trading or declines in subscriptions;

our ability to generate cash flow and revenue from the launch of C2;

our ability to successfully implement changes to our fee structure;

changes in our rate per contract due to shifts in the mix of the products traded, the trading venue and the mix of customers;

the ability of our compliance and risk management methods to effectively monitor and manage our risks;

our ability to maintain adequate liquidity to allow us to continue to invest in our business;

customer consolidation; and

changes to the tax treatment for options trading, including the possible imposition of a transaction tax on options transactions.

For a detailed discussion of these and other factors that might affect our performance, see Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2010, Part II, Item 1A of this Quarterly Report on Form 10-Q and our other filings with the SEC. We caution you not to place undue reliance on the forward-looking statements, which speak only as of the date of this filing.

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

On June 18, 2010, CBOE converted from a non-stock corporation owned by its members into a stock corporation that is a wholly-owned subsidiary of CBOE Holdings.

In the condensed consolidated statements of income of CBOE Holdings for the nine months ended September 30, 2010, net income per share allocated to common stockholders is calculated by dividing historical net income for the period by the weighted average number of common shares as if the restructuring transaction were consummated at the beginning of the period.

The unrestricted common stock of CBOE Holdings is listed on the NASDAQ Global Select Market under the symbol "CBOE."



Table of Contents

CBOE Holdings, Inc. and Subsidiaries  
Condensed Consolidated Statements of Income  
Three and Nine Months Ended September 30, 2011 and 2010

(in thousands, except per share amounts)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
	(unaudited)			
Operating Revenues:				
Transaction fees	\$109,840	\$72,885	\$286,018	\$250,378
Access fees	16,918	18,484	51,564	22,985
Exchange services and other fees	4,531	3,974	13,497	12,817
Market data fees	4,909	4,881	14,847	16,256
Regulatory fees	5,266	3,388	14,994	11,409
Other revenue	2,140	2,403	7,015	5,868
Total Operating Revenues	143,604	106,015	387,935	319,713
Operating Expenses:				
Employee costs	25,945	34,643	76,186	80,420
Depreciation and amortization	8,897	7,099	26,588	21,701
Data processing	4,337	4,304	13,671	14,541
Outside services	6,881	6,293	20,650	24,457
Royalty fees	13,956	9,226	35,475	31,643
Trading volume incentives	3,525	4,594	11,799	15,629
Travel and promotional expenses	2,416	2,702	6,470	7,897
Facilities costs	1,081	1,440	3,974	4,139
Other expenses	1,600	781	4,171	3,799
Total Operating Expenses	68,638	71,082	198,984	204,226
Operating Income	74,966	34,933	188,951	115,487
Other Income/(Expense):				
Investment income	15	158	119	393
Net loss from investment in affiliates	(190)	(168)	(650)	(542)
Interest and other borrowing costs	(226)	(225)	(673)	(671)
Total Other Income/(Expense)	(401)	(235)	(1,204)	(820)
Income Before Income Taxes	74,565	34,698	187,747	114,667
Income tax provision	33,238	14,244	80,148	46,648
Net Income	41,327	20,454	107,599	68,019
Net income allocated to participating securities	(730)	(434)	(2,294)	(615)
Net Income Allocated to Common Stockholders	\$40,597	\$20,020	\$105,305	\$67,404
Net Income Per Share Allocated to Common Stockholders(Note 4):				
Basic	\$0.45	\$0.20	\$1.17	\$0.71
Diluted	0.45	0.20	1.17	0.71
Weighted average shares used in computing income per share:				
Basic	90,334	102,103	90,195	95,065
Diluted	90,334	102,103	90,195	95,065

See notes to condensed consolidated financial statements



Table of Contents

CBOE Holdings, Inc. and Subsidiaries  
 Condensed Consolidated Balance Sheets  
 September 30, 2011 and December 31, 2010

(in thousands, except share amounts)	September 30, 2011 (unaudited)	December 31, 2010
Assets		
Current Assets:		
Cash and cash equivalents	\$ 147,220	\$ 53,789
Accounts receivable—net allowances of \$142 and \$108	46,013	37,746
Marketing fee receivable	6,999	7,815
Income taxes receivable	362	5,537
Other prepaid expenses	6,031	4,510
Other current assets	694	537
Total Current Assets	207,319	109,934
Investments in Affiliates	11,965	12,615
Land	4,914	4,914
Property and Equipment:		
Construction in progress	18	1,729
Building	60,917	60,917
Furniture and equipment	250,946	240,711
Less accumulated depreciation and amortization	(234,295)	(221,273)
Total Property and Equipment—Net	77,586	82,084
Other Assets:		
Software development work in progress	7,727	1,131
Data processing software and other assets (less accumulated amortization of \$117,959 and \$107,770)	35,132	43,434
Total Other Assets—Net	42,859	44,565
Total	\$ 344,643	\$ 254,112
Liabilities and Stockholders' Equity		
Current Liabilities:		
Accounts payable and accrued expenses	\$ 42,799	\$ 40,084
Marketing fee payable	7,540	8,349
Deferred revenue	11,236	280
Post-retirement medical benefits	26	103
Income taxes payable	3,545	—
Total Current Liabilities	65,146	48,816
Long-term Liabilities:		
Post-retirement medical benefits	1,856	1,782
Income taxes payable	8,553	3,165
Other long-term liabilities	3,806	3,993
Deferred income taxes	19,581	20,482
Total Long-term Liabilities	33,796	29,422
Commitments and Contingencies		
Total Liabilities	98,942	78,238
Stockholders' Equity:		
Preferred stock, \$0.01 par value: 20,000,000 shares authorized, no shares issued and outstanding at September 30, 2011 and December 31, 2010	—	—
	906	518

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Unrestricted common stock, \$0.01 par value: 325,000,000 shares authorized; 90,649,902 issued and 89,920,627 outstanding at September 30, 2011; 51,786,717 issued and outstanding at December 31, 2010			
Class A-2 common stock, \$0.01 par value: 45,366,690 shares authorized; none and 38,297,994 shares issued and outstanding at September 30, 2011 and December 31, 2010, respectively	—		383
Additional paid-in-capital	52,461		42,858
Retained earnings	211,210		133,087
Treasury stock at cost – 729,275 shares at September 30, 2011 and no shares at December 31, 2010	(17,962	)	—
Accumulated other comprehensive loss	(914	)	(972 )
Total Stockholders' Equity	245,701		175,874
Total	\$344,643		\$254,112
See notes to condensed consolidated financial statements			

Table of ContentsCBOE Holdings, Inc. and Subsidiaries  
Condensed Consolidated Statement of Stockholders' Equity  
(Unaudited)

(in thousands)	Preferred Stock	Unrestricted Common Stock	Class A-2 Common Stock	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
Balance—December 31, 2010	\$—	\$ 518	\$ 383	\$ 42,858	\$ 133,087	\$—	\$ (972 )	\$ 175,874
Automatic conversion of Class A-2 common stock into unrestricted common stock		383	(383 )					—
Cash dividends on common stock					(29,476 )			(29,476 )
Stock based compensation				9,608				9,608
Issuance of vested restricted stock granted to employees		5		(5 )				—
Purchase of unrestricted common stock						(17,962 )		(17,962 )
Net income					107,599			107,599
Post-retirement benefit obligation adjustment—net of tax expense of \$4							58	58
Comprehensive income								107,657
Balance—September 30, 2011	\$—	\$ 906	\$—	\$ 52,461	\$ 211,210	\$(17,962 )	\$ (914 )	\$ 245,701

See notes to condensed consolidated financial statements

Table of Contents

CBOE Holdings, Inc. and Subsidiaries  
Condensed Consolidated Statements of Cash Flows  
Nine Months Ended September 30, 2011 and 2010

(in thousands)	Nine Months Ended	
	September 30, 2011	September 30, 2010
	(unaudited)	
Cash Flows from Operating Activities:		
Net income	\$107,599	\$68,019
Adjustments to reconcile net income to net cash flows from operating activities:		
Depreciation and amortization	26,588	21,701
Other amortization	67	52
Provision for deferred income taxes	(911	) (3,012
Stock-based compensation	9,608	15,565
Loss on disposition of property	1,179	139
Loss on investment of affiliate	190	542
Impairment of investment in affiliate	460	—
Changes in assets and liabilities:		
Accounts receivable	(8,267	) (6,140
Marketing fee receivable	816	1,768
Income taxes receivable	5,175	(12,965
Prepaid expenses	(1,188	) 533
Other receivable	—	2,086
Other current assets	(157	) (119
Accounts payable and accrued expenses	4,248	(8,049
Marketing fee payable	(809	) (1,974
Deferred revenue and other long-term liabilities	10,769	11,514
Post-retirement benefit obligations	(3	) (7
Income taxes payable	8,933	839
Settlement with appellants	—	(3,000
Access fees subject to fee-based payment	—	(2,688
Net Cash Flows provided by Operating Activities	164,297	84,804
Cash Flows from Investing Activities:		
Capital and other assets expenditures	(23,485	) (15,049
Investment in Signal Trading Systems, LLC	—	(7,990
Other	57	—
Net Cash Flows used in Investing Activities	(23,428	) (23,039
Cash Flows from Financing Activities:		
Payments for debt issuance costs	—	(3
Payment of quarterly dividends	(29,476	) (10,432
Purchase of unrestricted stock from employees	(3,075	) —
Purchase of unrestricted common stock	(14,887	) —
Exercise right privilege payable	—	(300,000
Net proceeds from issuance of unrestricted common stock	—	301,238
Payment of special dividend		