

Morningstar, Inc.
Form 10-Q
October 30, 2014

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED 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: 000-51280

MORNINGSTAR, INC.

(Exact Name of Registrant as Specified in its Charter)

Illinois

(State or Other Jurisdiction of
Incorporation or Organization)

36-3297908

(I.R.S. Employer
Identification Number)

22 West Washington Street

Chicago, Illinois

(Address of Principal Executive Offices)

(312) 696-6000

(Registrant's Telephone Number, Including Area Code)

60602

(Zip Code)

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.

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 Exchange Act).
Yes No

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As of October 24, 2014 there were 44,581,820 shares of the Company's common stock, no par value, outstanding.

Table of Contents

MORNINGSTAR, INC. AND SUBSIDIARIES
INDEX

<u>PART 1</u>	<u>FINANCIAL INFORMATION</u>	<u>3</u>
<u>Item 1.</u>	<u>Financial Statements</u>	<u>3</u>
	Unaudited Condensed Consolidated Statements of Income for the three and nine months ended September 30, 2014 and 2013	<u>4</u>
	Unaudited Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended September 30, 2014 and 2013	<u>5</u>
	Unaudited Condensed Consolidated Balance Sheets as of September 30, 2014 and December 31, 2013	<u>6</u>
	Unaudited Condensed Consolidated Statement of Equity for the nine months ended September 30, 2014	<u>7</u>
	Unaudited Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2014 and 2013	<u>8</u>
	<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	<u>9</u>
<u>Item 2.</u>	<u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>28</u>
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	<u>42</u>
<u>Item 4.</u>	<u>Controls and Procedures</u>	<u>42</u>
<u>PART 2</u>	<u>OTHER INFORMATION</u>	<u>44</u>
<u>Item 1.</u>	<u>Legal Proceedings</u>	<u>44</u>
<u>Item 1A.</u>	<u>Risk Factors</u>	<u>44</u>
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>44</u>
<u>Item 6.</u>	<u>Exhibits</u>	<u>44</u>
<u>SIGNATURE</u>		<u>45</u>
<u>EXHIBIT INDEX</u>		<u>46</u>

Table of Contents

PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements

3

Table of Contents

Morningstar, Inc. and Subsidiaries

Unaudited Condensed Consolidated Statements of Income

(in thousands except per share amounts)	Three months ended September		Nine months ended September	
	30 2014	2013	30 2014	2013
Revenue	\$ 193,106	\$ 173,482	\$ 563,656	\$ 517,766
Operating expense (1):				
Cost of revenue	80,142	72,422	237,243	198,499
Sales and marketing	26,761	22,774	83,138	78,789
General and administrative	26,384	22,416	82,926	77,863
Depreciation and amortization	14,558	11,257	40,336	33,858
Litigation settlement (2)	—	—	61,000	—
Total operating expense	147,845	128,869	504,643	389,009
Operating income	45,261	44,613	59,013	128,757
Non-operating income (expense):				
Interest income, net	515	630	1,734	2,035
Gain (loss) on sale of investments, reclassified from other comprehensive income	158	(42)	505	1,106
Holding gain (loss) upon acquisition of additional ownership of equity and cost method investments	—	(78)	5,168	3,635
Other income (expense), net	(971)	261)	(942)	(1,949)
Non-operating income (expense), net	(298)	771)	6,465	4,827
Income before income taxes and equity in net income of unconsolidated entities	44,963	45,384	65,478	133,584
Equity in net income of unconsolidated entities	337	315	1,433	1,172
Income tax expense	15,149	14,265	20,188	42,647
Consolidated net income	30,151	31,434	46,723	92,109
Net loss attributable to the noncontrolling interest	29	29	64	93
Net income attributable to Morningstar, Inc.	\$ 30,180	\$ 31,463	\$ 46,787	\$ 92,202
Net income per share attributable to Morningstar, Inc.:				
Basic	\$ 0.67	\$ 0.68	\$ 1.04	\$ 1.99
Diluted	\$ 0.67	\$ 0.68	\$ 1.04	\$ 1.98
Dividends per common share:				
Dividends declared per common share	\$ 0.17	\$ —	\$ 0.51	\$ 0.25
Dividends paid per common share	\$ 0.17	\$ 0.13	\$ 0.51	\$ 0.25

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Weighted average shares outstanding:

Basic	44,734	46,080	44,763	46,293
Diluted	44,889	46,519	44,990	46,635

	Three months ended September 30		Nine months ended September 30	
	2014	2013	2014	2013
(1) Includes stock-based compensation expense of:				
Cost of revenue	\$2,177	\$1,471	\$5,829	\$4,863
Sales and marketing	607	456	1,634	1,490
General and administrative	2,167	1,489	5,790	4,800
Total stock-based compensation expense	\$4,951	\$3,416	\$13,253	\$11,153

(2) See Note 12, Contingencies, for additional information.

See notes to unaudited condensed consolidated financial statements.

Table of Contents

Morningstar, Inc. and Subsidiaries

Unaudited Condensed Consolidated Statements of Comprehensive Income

(in thousands)	Three months ended September		Nine months ended September	
	30 2014	2013	30 2014	2013
Consolidated net income	\$30,151	\$31,434	\$46,723	\$92,109
Other comprehensive income (loss):				
Foreign currency translation adjustment	(18,809	) 11,247	(13,476	) (4,952
Unrealized gains (losses) on securities, net of tax:				
Unrealized holding gains (losses) arising during period	(244	) 774	152	1,774
Reclassification of (gains) losses included in net income	(100	) 28	(318	) (706
Other comprehensive income (loss)	(19,153	) 12,049	(13,642	) (3,884
Comprehensive income	10,998	43,483	33,081	88,225
Comprehensive loss attributable to noncontrolling interest	83	40	98	246
Comprehensive income attributable to Morningstar, Inc.	\$11,081	\$43,523	\$33,179	\$88,471

See notes to unaudited condensed consolidated financial statements.

Table of Contents

Morningstar, Inc. and Subsidiaries

Unaudited Condensed Consolidated Balance Sheets

	As of September 30 2014	As of December 31 2013
(in thousands except share amounts)		
Assets		
Current assets:		
Cash and cash equivalents	\$ 189,318	\$ 168,160
Investments	38,490	130,407
Accounts receivable, less allowance of \$1,323 and \$1,089, respectively	124,966	114,131
Deferred tax asset, net	7,524	3,892
Income tax receivable, net	4,427	3,942
Other current assets	23,619	26,361
Total current assets	388,344	446,893
Property, equipment, and capitalized software, less accumulated depreciation and amortization of \$126,449 and \$106,166, respectively	112,584	104,986
Investments in unconsolidated entities	30,428	38,714
Goodwill	378,969	326,450
Intangible assets, net	103,443	103,909
Other assets	6,407	9,716
Total assets	\$ 1,020,175	\$ 1,030,668
Liabilities and equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 38,495	\$ 42,131
Accrued compensation	67,692	71,403
Deferred revenue	150,051	149,225
Short-term debt	30,017	—
Other current liabilities	4,632	6,786
Total current liabilities	290,887	269,545
Accrued compensation	6,905	8,193
Deferred tax liability, net	17,565	23,755
Deferred rent	23,460	23,938
Other long-term liabilities	10,839	13,947
Total liabilities	349,656	339,378
Equity:		
Morningstar, Inc. shareholders' equity:		
Common stock, no par value, 200,000,000 shares authorized, of which 44,661,350 and 44,967,423 shares were outstanding as of September 30, 2014 and December 31, 2013, respectively	5	5
Treasury stock at cost, 7,809,277 shares as of September 30, 2014 and 7,202,896 shares as of December 31, 2013	(493,642)	(449,054)
Additional paid-in capital	553,172	539,507
Retained earnings	618,484	594,626
Accumulated other comprehensive income (loss):		
Currency translation adjustment	(8,833)) 4,609
Unrealized gain on available-for-sale investments	398	564

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Total accumulated other comprehensive income (loss)	(8,435) 5,173
Total Morningstar, Inc. shareholders' equity	669,584	690,257
Noncontrolling interests	935	1,033
Total equity	670,519	691,290
Total liabilities and equity	\$1,020,175	\$1,030,668

See notes to unaudited condensed consolidated financial statements.

6

Table of Contents

Morningstar, Inc. and Subsidiaries
 Unaudited Condensed Consolidated Statement of Equity
 For the nine months ended September 30, 2014

(in thousands, except share amounts)	Morningstar, Inc. Shareholders' Equity					Accumulated Other Comprehensive Income (Loss)	Non- Controlling Interests	Total Equity
	Common Stock Shares Outstanding	Par Value	Treasury Stock	Additional Paid-in Capital	Retained Earnings			
Balance as of December 31, 2013	44,967,423	\$5	\$(449,054)	\$539,507	\$594,626	\$5,173	\$1,033	\$691,290
Net income (loss)		—	—	—	46,787		(64)	46,723
Other comprehensive income (loss):								
Unrealized gain on available-for-sale investments, net of income tax of \$82		—	—	—	—	152	—	152
Reclassification of adjustments for gains included in net income, net of income tax of \$187		—	—	—	—	(318)	—	(318)
Foreign currency translation adjustment, net		—	—	—	—	(13,442)	(34)	(13,476)
Other comprehensive loss, net		—	—	—	—			