Spirit Airlines, Inc.
Form 10-Q
October 30, 2013

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

Form 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2013

OR

o 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: 001-35186

SPIRIT AIRLINES, INC.
(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	38-1747023 (I.R.S. Employer Identification No.)
2800 Executive Way Miramar, Florida (Address of principal executive offices)	33025 (Zip Code)

(954) 447-7920
(Registrant’s telephone number, including area 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 ý No o

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

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 “small reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	ý	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	o

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

Indicate the number of shares outstanding of each of the registrant’s classes of common stock as of the close of business on October 18, 2013:

Class	Number of Shares
Common Stock, $0.0001 par value	72,647,167

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ITEM 1. UNAUDITED CONDENSED FINANCIAL STATEMENTS
Spirit Airlines, Inc.
Condensed Statements of Operations
(unaudited, in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Operating revenues:				
Passenger	$279,499	$202,181	$739,515	$594,071
Non-ticket	177,126	140,136	494,886	396,049
Total operating revenues	456,625	342,317	1,234,401	990,120
Operating expenses:				
Aircraft fuel	144,986	122,016	411,903	350,974
Salaries, wages and benefits	66,805	54,413	192,758	160,556
Aircraft rent	42,134	37,536	125,121	106,469
Landing fees and other rents	22,106	19,060	61,508	51,240
Distribution	17,916	14,620	50,874	43,559
Maintenance, materials and repairs	16,908	14,211	43,890	37,254
Depreciation and amortization	8,475	3,815	22,403	10,012
Other operating	38,884	35,253	110,799	95,862
Loss on disposal of assets	165	—	426	482
Special charges (credits)	442	(8,288)	488	(8,345)
Total operating expenses	358,821	292,636	1,020,170	848,063
Operating income	97,804	49,681	214,231	142,057
Other (income) expense:				
Interest expense	36	10	140	1,334
Capitalized interest	(36)	(10)	(140)	(1,334)
Interest income	(87)	(171)	(308)	(766)
Other expense	115	109	252	236
Total other (income) expense	28	(62)	(56)	(530)
Income before income taxes	97,776	49,743	214,287	142,587
Provision for income taxes	36,673	18,859	80,562	53,693
Net income	$61,103	$30,884	$133,725	$88,894
Basic earnings per share	$0.84	$0.43	$1.84	$1.23
Diluted earnings per share	$0.84	$0.43	$1.83	$1.22

The accompanying Notes are an integral part of these Condensed Financial Statements.

Spirit Airlines, Inc.
Condensed Balance Sheets
(unaudited, in thousands)

	September 30, 2013	December 31, 2012
Assets		
Current assets:		
Cash and cash equivalents	$540,195	$416,816
Accounts receivable, net	27,838	22,740
Deferred income taxes	14,512	12,591
Other current assets	79,299	95,210
Total current assets	661,844	547,357
Property and equipment:		
Flight equipment	5,148	2,648
Ground and other equipment	49,567	43,580
Less accumulated depreciation	(23,202)	(17,825)
	31,513	28,403
Deposits on flight equipment purchase contracts	132,483	96,692
Aircraft maintenance deposits	145,598	122,379
Deferred heavy maintenance	110,514	80,533
Other long-term assets	43,187	44,520
Total assets	$1,125,139	$919,884
Liabilities and shareholders’ equity		
Current liabilities:		
Accounts payable	$20,766	$24,166
Air traffic liability	180,735	131,414
Other current liabilities	129,770	121,314
Total current liabilities	331,271	276,894
Long-term deferred income taxes	43,932	33,216
Deferred credits and other long-term liabilities	26,167	27,239
Shareholders’ equity:		
Common stock	7	7
Additional paid-in-capital	513,142	504,527
Treasury stock	(2,257)	(1,151)
Retained earnings	212,877	79,152
Total shareholders’ equity	723,769	582,535
Total liabilities and shareholders’ equity	$1,125,139	$919,884

The accompanying Notes are an integral part of these Condensed Financial Statements.

Spirit Airlines, Inc.
Condensed Statements of Cash Flows
(unaudited, in thousands)

	Nine Months Ended September 30,	
	2013	2012
Net cash provided by operating activities	$173,631	$88,807
Investing activities:		
Proceeds from sale of property and equipment	—	14
Proceeds from sale of slots	—	9,060
Pre-delivery deposits for flight equipment, net of refunds	(41,328)	(6,817)
Purchase of property and equipment	(17,028)	(21,711)
Net cash used in investing activities	(58,356)	(19,454)
Financing activities:		
Proceeds from options exercised	675	410
Proceeds from sale and leaseback transactions	6,900	12,427
Payments to pre-IPO shareholders pursuant to tax receivable agreement	—	(26,905)
Excess tax benefits from share-based compensation	1,635	1,466
Repurchase of common stock	(1,106)	(936)
Net cash provided by (used in) financing activities	8,104	(13,538)
Net increase in cash and cash equivalents	123,379	55,815
Cash and cash equivalents at beginning of period	416,816	343,328
Cash and cash equivalents at end of period	$540,195	$399,143
Supplemental disclosures		
Cash payments for:		
Interest	$26	$297
Taxes	$60,942	$39,350

The accompanying Notes are an integral part of these Condensed Financial Statements.

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Notes to Condensed Financial Statements
(unaudited)
1. Basis of Presentation
The accompanying unaudited condensed financial statements include the accounts of Spirit Airlines, Inc. (the Company). These unaudited condensed financial statements reflect all normal recurring adjustments which management believes are necessary to present fairly the financial position, results of operations and cash flows of the Company for the respective periods presented. Certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission for Form 10-Q. These unaudited interim condensed financial statements should be read in conjunction with the audited financial statements of the Company and notes thereto included in the Annual Report on Form 10-K for the year ended December 31, 2012 filed with the Securities and Exchange Commission.
The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.
The interim results reflected in the unaudited condensed financial statements are not necessarily indicative of the results that may be expected for other interim periods or for the full year.
Certain prior period amounts have been reclassified to conform to the current year's presentation.
2. Recent Accounting Developments
In December 2011, the FASB issued amendments to Accounting Standards Update No. 2011-11, Balance Sheet (Topic 210); Disclosures about Offsetting Assets and Liabilities (ASU 2011-11). The amendments in this update are designed to enhance disclosures by requiring improved information about financial instruments and derivative instruments that are either (a) offset in accordance with certain right to set-off conditions prescribed by current accounting guidance or (b) subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset in accordance with current accounting guidance. On January 1, 2013, the Company adopted ASU 2011-11.
In January 2013, the FASB issued Accounting Standards Update No. 2013-01, Scope Clarification of Disclosures about Offsetting Assets and Liabilities (ASU 2013-01), to limit the scope of ASU 2011-11 and its new balance sheet offsetting disclosure requirements to derivatives (including bifurcated embedded derivatives), repurchase agreements and reverse repurchase agreements, and securities borrowing and lending transactions. On January 1, 2013, the Company adopted ASU 2013-01 in conjunction with ASU 2011-11.

3. Special Charges and Credits
Secondary Offering Costs
Special charges and credits for the nine months ended September 30, 2013 primarily include costs related to an underwritten public offering of 12,070,920 shares of common stock by certain stockholders affiliated with Indigo Partners LLC (Indigo) completed during the third quarter of 2013. The Company incurred a total of $0.4 million in costs related to this offering. The Company did not receive any proceeds from this offering.
On January 25, 2012, certain stockholders of the Company, including affiliates of Oaktree Capital Management and Indigo and certain members of the Company's executive team, sold an aggregate of 12,650,000 shares of common stock in an underwritten public offering. The Company incurred a total of $1.3 million in costs between 2011 and 2012 related to this offering, of which $0.5 million were incurred during the nine months ended September 30, 2012. These costs were offset by reimbursements from certain selling shareholders of $0.6 million in accordance with the Fourth Amendment to the Second Amended and Restated Investor Rights Agreement. The Company did not receive any proceeds from this offering.

Notes to Condensed Financial Statements—(Continued)

4. Earnings per Share

The following table sets forth the computation of basic and diluted earnings per common share:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
	(in thousands, except per share amounts)			
Numerator				
Net income	$ 61,103	$ 30,884	$ 133,725	$ 88,894
Denominator				
Weighted-average shares outstanding, basic	72,632	72,427	72,571	72,367
Effect of dilutive stock awards	371	231	363	214
Adjusted weighted-average shares outstanding, diluted	73,003	72,658	72,934	72,581
Net Income per Share				
Basic earnings per common share	$ 0.84	$ 0.43	$ 1.84	$ 1.23
Diluted earnings per common share	$ 0.84	$ 0.43	$ 1.83	$ 1.22
Potentially dilutive amounts excluded from calculations:				
Stock options and restricted stock units	1	—	1	—

5. Accrued Liabilities

Other current liabilities as of September 30, 2013 and December 31, 2012 consist of the following:

	September 30, 2013	December 31, 2012
	(in thousands)	
Federal excise and other passenger taxes and fees payable	$ 24,051	$ 23,401
Aircraft maintenance	23,784	22,319
Salaries and wages	22,357	21,057
Airport expenses	16,757	16,024
Fuel	12,994	11,219
Aircraft and facility rent	6,133	8,020
Tax receivable agreement	5,643	7,987
Other	18,051	11,287
Accrued liabilities	$ 129,770	$ 121,314

6. Financial Instruments and Risk Management

As part of the Company’s risk management program, the Company from time to time uses a variety of financial instruments to reduce its exposure to fluctuations in the price of jet fuel. The Company does not hold or issue derivative financial instruments for trading purposes.

The Company is exposed to credit losses in the event of nonperformance by counterparties to these financial instruments. The Company periodically reviews and seeks to mitigate exposure to the financial deterioration and nonperformance of any counterparty by monitoring the absolute exposure levels, each counterparty's credit ratings, and the historical performance of the counterparties relating to hedge transactions. The credit exposure related to these financial instruments is limited to the fair value of contracts in a net receivable position at the reporting date. The Company also maintains security agreements that require the Company to post collateral if the value of selected instruments falls below specified mark-to-market thresholds. As of September 30, 2013, the Company was not required to post collateral for these instruments.

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Notes to Condensed Financial Statements—(Continued)

The Company records financial derivative instruments at fair value, which includes an evaluation of each counterparty's credit risk. The Company's derivative contracts generally consist of United States Gulf Coast jet fuel swaps (jet fuel swaps) and United States Gulf Coast jet fuel options (jet fuel options). Jet fuel swaps are agreements to protect the refining price risk between the price of crude oil and the price of refined jet fuel. Jet fuel options are costless collar contracts to manage the risk of increasing fuel prices. Fair value of the instruments is determined using standard option valuation models.

The Company chose not to elect hedge accounting on any derivative instruments entered into during the three and nine months ended September 30, 2013 and 2012 and, as a result, changes in the fair value of these fuel hedge contracts are recorded each period in aircraft fuel expense.

The following table summarizes the components of aircraft fuel expense for the three and nine months ended September 30, 2013 and 2012:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
	(in thousands)			
Into-plane fuel cost	$ 143,978	$ 123,517	$ 402,066	$ 351,057
Settlement losses (gains)	6,663	(580)	6,348	(543)
Unrealized mark-to-market losses (gains)	(5,655)	(921)	3,489	460
Aircraft fuel	$ 144,986	$ 122,016	$ 411,903	$ 350,974

All realized gains and losses are reflected in the accompanying statements of cash flows in cash flow from operating activities.

During peak hurricane season (August through October), the Company enters into jet fuel swap agreements to protect the refining price risk between the price of crude oil and the price of refined jet fuel. As of September 30, 2013 and December 31, 2012, the Company had fuel hedges consisting of jet fuel swaps and jet fuel options, respectively, with crude oil and refined products as the underlying commodities. As of September 30, 2013, the Company had approximately 21% of its forecast fourth quarter 2013 fuel consumption protected from refining risk using jet fuel swaps. As of December 31, 2012, the Company had jet fuel option agreements in place to protect 7.8 million gallons, or approximately 5%, of its 2013 anticipated jet fuel consumption at a weighted-average ceiling and floor price of $3.09 and $2.84 per gallon, respectively.

7. Commitments and Contingencies

Aircraft-Related Commitments and Financing Arrangements

The Company’s contractual purchase commitments consist primarily of aircraft and engine acquisitions through manufacturers and aircraft leasing companies. On June 20, 2013, the Company entered into an amendment to the Airbus A320 Family Purchase Agreement, by and between the Company and Airbus S.A.S., dated May 5, 2004 (Airbus Amendment) for the order of an additional 20 Airbus A321 aircraft. These aircraft are in addition to the 95 aircraft not yet delivered under Spirit's existing order with Airbus and are scheduled for delivery between 2015 and 2017. On October 1, 2013, the Company entered into agreements with International Aero Engines AG (IAE) and Pratt & Whitney (collectively, the IAE & P&W Agreement) for the provision and servicing of engines to power its fleet of Airbus A320-family aircraft. The commitments reflected below are inclusive of the additional commitments resulting from the IAE & P&W Agreement. The Company's aircraft orders, including the conversion of 10 Airbus A320 orders to Airbus A321 orders and the conversion of 5 Airbus A321 orders to Airbus A321neo orders, consisted of 115 A320 family aircraft (40 of the existing A320 model, 45 A320neos, 25 of the existing A321 model, and 5 A321neos) with Airbus, 5 direct operating leases for A320neos with a third party, 6 spare engine orders for V2500 SelectOne™ engines with IAE and 9 spare engine orders for PurePower PW1100G-JM engines with Pratt & Whitney. Aircraft are scheduled for delivery from 2013 through 2021, and spare engines are scheduled for delivery from 2014 through 2023. Committed expenditures for these aircraft and related flight equipment, including estimated amounts for contractual price escalations and pre-delivery payments, will be approximately $136 million for the remainder of

2013, $412 million in 2014, $794 million in 2015, $640 million in 2016, $816 million in 2017, and $2,743 million in 2018 and beyond. We have secured financing commitments with third parties for our next ten aircraft deliveries from Airbus, which are scheduled for delivery between 2013 and 2014. We do not have financing commitments in place for the remaining 105 Airbus firm aircraft orders scheduled for delivery between 2015 and 2021.

During the first nine months of 2013, the Company took delivery of six aircraft, two of which were financed via direct operating leases and the remaining four under sale and leaseback transactions with third-party aircraft lessors. The four sale and

Notes to Condensed Financial Statements—(Continued)

leaseback transactions resulted in net deferred losses of $1.4 million. Deferred losses are included in other long-term assets on the accompanying balance sheet. Deferred losses are recognized as an increase to rent expense on a straight-line basis over the term of the respective operating leases. Deferred gains are included in deferred credits and other long-term liabilities on the accompanying balance sheet. Deferred gains are recognized as a decrease to rent expense on a straight-line basis over the term of the respective operating leases. The Company had agreements in place prior to the delivery of these aircraft which resulted in the settlement of the purchase obligation by the lessor and the refund of $21.5 million in pre-delivery deposits from Airbus during the nine months ended September 30, 2013. The refunded pre-delivery deposits have been disclosed in the accompanying statements of cash flows as investing activities within pre-delivery deposits for flight equipment, net of refunds. In addition, the Company entered into a sale and leaseback transaction with third-party lessors for the sale and leaseback of one V2500 SelectOne™ IAE engine. Cash outflows related to the purchase of the engine have been disclosed in the accompanying statements of cash flows as investing activities within purchases of property and equipment and the cash inflows from the sale of the engine as financing activities within proceeds received from sale and leaseback transactions. All of the leases from these sale and leaseback transactions are accounted for as operating leases. Under the terms of the lease agreements, the Company will continue to operate and maintain the aircraft. Payments under the lease agreements are fixed for the term of the lease. The lease agreements contain standard termination events, including termination upon a breach of the Company's obligations to make rental payments and upon any other material breach of the Company's obligations under the leases, and standard maintenance and return condition provisions. These return provisions are evaluated at inception of the lease and throughout the lease terms and are accounted for as additional rent expense when it is probable that such amounts will be paid to the lessor. Upon a termination of the lease due to a breach by the Company, the Company would be liable for standard contractual damages, possibly including damages suffered by the lessor in connection with remarketing the aircraft or while the aircraft is not leased to another party.

Future minimum lease payments under noncancelable operating leases as of September 30, 2013 and the periods in which payments are due were as follows:

	Operating Lease Obligations (in thousands)
Remainder of 2013	$47,411
2014	188,817
2015	188,492
2016	181,369
2017	157,756
2018 and thereafter	574,141
Total minimum lease payments	$1,337,986

During the second quarter, the Company extended the operating leases on 14 of its Airbus A319 aircraft, which were previously set to expire in 2017 through 2019. These extensions resulted in an additional $72.8 million of lease commitments from 2017 through 2022.

Some of the Company’s master lease agreements provide that the Company pays maintenance reserves to aircraft lessors to be held as collateral in advance of the Company’s required performance of major maintenance activities. Maintenance reserve payments are either fixed contractual amounts or utilization based. Fixed maintenance reserve payments for these aircraft and related flight equipment, including estimated amounts for contractual price escalations, are expected to be approximately $1.8 million for the remainder of 2013, $7.4 million in 2014, $7.6 million in 2015, $8.0 million in 2016, $7.4 million in 2017, and $24.2 million in 2018 and beyond. These lease agreements provide that maintenance reserves are reimbursable to the Company upon completion of the maintenance event in an amount equal to the lesser of (1) the amount of the maintenance reserve held by the lessor associated with the specific maintenance event or (2) the qualifying costs related to the specific maintenance event.

Notes to Condensed Financial Statements—(Continued)

Reservation System

The Company is contractually obligated to pay the following minimum guaranteed payments to the provider of its reservation system as of September 30, 2013: $0.9 million for the remainder of 2013, $3.9 million in 2014, $3.9 million in 2015, $3.9 million in 2016, $3.9 million in 2017, and $2.6 million in 2018 and thereafter.

Litigation

The Company is subject to commercial litigation claims and to administrative and regulatory proceedings and reviews that may be asserted or maintained from time to time. The Company believes the ultimate outcome of such lawsuits, proceedings and reviews will not, individually or in the aggregate, have a material adverse effect on its financial position, liquidity or results of operations.

Credit Card Processing Arrangements

The Company has agreements with organizations that process credit card transactions arising from the purchase of air travel, baggage charges, and other ancillary services by customers. As it is standard in the airline industry, the Company's contractual arrangements with credit card processors permit them, under certain circumstances, to retain a holdback or other collateral, which the Company records as restricted cash, when future air travel and other future services are purchased via credit card transactions. The required holdback is the percentage of the Company's overall credit card sales that its credit card processors hold to cover refunds to customers if the Company fails to fulfill its flight obligations. If the Company fails to satisfy certain liquidity and other financial covenants, the processing agreements provide the processors the right to require the Company to maintain cash collateral up to approximately 100% of the Company's air traffic liability, resulting in a commensurate reduction of unrestricted cash. As of September 30, 2013 and December 31, 2012, the Company continued to be in compliance with its credit card processing agreements, and the processors were holding back $0 of remittances.

The maximum potential exposure to cash holdbacks by the Company's credit card processors, based upon advance ticket sales and $9 Fare Club memberships as of September 30, 2013 and December 31, 2012, was $203.8 million and $144.8 million, respectively.

Employees

Approximately 59% of the Company’s employees are covered under collective bargaining agreements. The table below sets forth our employee groups and status of the collective bargaining agreements as of September 30, 2013.

Employee Groups	Representative	Amendable Date	Percentage of Workforce
Pilots	Air Line Pilots Association, International (ALPA)	August 2015	24%
Flight Attendants	Association of Flight Attendants (AFA-CWA)	August 2007	34%
Dispatchers	Transport Workers Union (TWU)	August 2018	1%

During the third quarter of 2013, the Company reached a five-year agreement with the TWU. The Company is currently in negotiations with the AFA-CWA to reach a new collective bargaining agreement.

The Company is self-insured for health care claims, up to a stop loss amount, for eligible participating employees and qualified dependent medical claims, subject to deductibles and limitations. The Company’s liabilities for claims incurred but not reported are determined based on an estimate of the ultimate aggregate liability for claims incurred. The estimate is calculated from actual claim rates and adjusted periodically as necessary. The Company has accrued $2.1 million and $1.9 million for health care claims as of September 30, 2013 and December 31, 2012, respectively.

8. Fair Value Measurements

Under ASC 820, Fair Value Measurements and Disclosures, disclosures are required about how fair value is determined for assets and liabilities, and a hierarchy for which these assets and liabilities must be grouped is established, based on significant levels of inputs, as follows:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Notes to Condensed Financial Statements—(Continued)

Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.
Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The Company utilizes several valuation techniques in order to assess the fair value of the Company's financial assets and liabilities. The Company's derivative contracts generally consist of jet fuel swaps and jet fuel options. These instruments are valued using energy and commodity market data, which is derived by combining raw inputs with quantitative models and processes to generate forward curves and volatilities.
The Company utilizes the market approach to measure fair value for its financial assets and liabilities. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

Assets and liabilities measured at gross fair value on a recurring basis are summarized below:

	Fair Value Measurements as of September 30, 2013			
	Total	Level 1	Level 2	Level 3
	(in millions)			
Cash and cash equivalents	$540.2	$540.2	$—	$—
Jet fuel swaps	1.7	—	1.7	—
Total assets	$541.9	$540.2	$1.7	$—
Jet fuel swaps	$4.9	$—	$4.9	$—
Total liabilities	$4.9	$—	$4.9	$—

	Fair Value Measurements as of December 31, 2012			
	Total	Level 1	Level 2	Level 3
	(in millions)			
Cash and cash equivalents	$416.8	$416.8	$—	$—
Jet fuel options	0.3	—	—	0.3
Total assets	$417.1	$416.8		