

CHURCHILL DOWNS INC
Form 10-K
February 25, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K

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

For the fiscal year ended December 31, 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 001-33998

(Exact name of registrant as specified in its charter)

Kentucky 61-0156015
(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

600 North Hurstbourne Parkway, Suite 400 (502) 636-4400
Louisville, Kentucky 40222
(Address of principal executive offices) (zip code) (Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:
Common Stock, No Par Value The NASDAQ Stock Market LLC
(Title of each class registered) (Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act:
None
(Title of class)

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes 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 Exchange Act during the preceding 12 months 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) 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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 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

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 February 20, 2015, 17,632,693 shares of the Registrant's Common Stock were outstanding. As of June 30, 2014 (based upon the closing sale price for such date on the NASDAQ Global Market), the aggregate market value of the shares held by non-affiliates of the Registrant was \$1,177,242,546.

Portions of the Registrant's Proxy Statement for its Annual Meeting of Shareholders to be held on April 23, 2015 are incorporated by reference herein in response to Items 10, 11, 12, 13 and 14 of Part III of Form 10-K. This Form 10-K filing includes 120 pages, which includes an exhibit index on pages 117-120.

CHURCHILL DOWNS INCORPORATED
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For the Year Ended December 31, 2014

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PART I

ITEM 1. BUSINESS

A. Introduction

Churchill Downs Incorporated (the "Company") is a diversified provider of pari-mutuel horseracing, online account wagering on horseracing and casino gaming. We are also one of the world's largest producers and distributors of online and mobile casual games. Our principal executive offices are located at 600 North Hurstbourne Parkway, Suite 400, Louisville, Kentucky, 40222.

We manage our operations through five operating segments as follows:

1. Racing, which includes:

• Churchill Downs Racetrack ("Churchill Downs") in Louisville, Kentucky, an internationally known thoroughbred racing operation and home of the Kentucky Derby since 1875;

• Arlington International Race Course ("Arlington"), a thoroughbred racing operation in Arlington Heights along with ten off-track betting facilities ("OTBs") in Illinois;

• Fair Grounds Race Course ("Fair Grounds"), a thoroughbred and quarterhorse racing operation in New Orleans along with twelve OTBs in Louisiana; and

• Calder Race Course ("Calder"), a thoroughbred racing facility in Miami Gardens, Florida, where as of July 1, 2014, we ceased pari-mutuel operations, except for limited operations conducted by a third party.

2. Casinos, which includes:

• Oxford Casino ("Oxford") in Oxford, Maine, which we acquired on July 17, 2013. Oxford operates approximately 860 slot machines, 26 table games and various dining facilities;

• Riverwalk Casino Hotel ("Riverwalk") in Vicksburg, Mississippi, which we acquired on October 23, 2012. Riverwalk operates approximately 690 slot machines, 15 table games, a five story, 80-room attached hotel, multi-functional event center and dining facilities;

• Harlow's Casino Resort & Spa ("Harlow's") in Greenville, Mississippi, which operates approximately 750 slot machines, 13 table games, a five-story, 105-room attached hotel, multi-functional event center, pool, spa and dining facilities;

• Calder Casino, a slot facility in Florida adjacent to Calder, which operates approximately 1,130 slot machines and included a poker room branded "Studz Poker Club" which ceased operations on June 30, 2014;

• Fair Grounds Slots, a slot facility in Louisiana adjacent to Fair Grounds, which operates approximately 620 slot machines;

• Video Services, LLC ("VSI"), the owner and operator of approximately 710 video poker machines in southeast Louisiana which are located within ten of our OTBs; and

• Our equity investment in Miami Valley Gaming, LLC ("MVG"), a 50% joint venture harness racetrack and video lottery terminal facility in Lebanon, Ohio, which opened on December 12, 2013. MVG has approximately 1,580 video lottery terminals, a racing simulcast center and a harness racetrack.

3. TwinSpires, which includes:

• TwinSpires, an Advance Deposit Wagering ("ADW") business that is licensed as a multi-jurisdictional simulcasting and interactive wagering hub in the state of Oregon;

• Fair Grounds Account Wagering ("FAW"), an ADW business that is licensed in the state of Louisiana;

• Velocity, a business that is licensed in the British Dependency Isle of Man focusing on high wagering-volume international customers;

• Bloodstock Research Information Services ("BRIS"), a data service provider for the equine industry;

• Our equity investment in HRTV, LLC ("HRTV"), a horseracing television channel, which was divested on January 2, 2015; and

• Luckity, an ADW business that offered real-money online bingo with outcomes based on and determined by pari-mutuel wagers on live horseraces which ceased operations during the fourth quarter of 2014.

4. Big Fish Games, Inc. ("Big Fish Games") which:

Is headquartered in Seattle, Washington with locations in Oakland, California and Luxembourg, which we acquired on December 16, 2014. Big Fish Games is a producer of premium paid, casual free-to-play and casino-style games for PCs and mobile devices.

5. Other Investments, which includes:

• United Tote Company and United Tote Canada (collectively "United Tote"), which manufactures and operates pari-mutuel wagering systems for racetracks, OTBs and other pari-mutuel wagering businesses;

• Capital View Casino & Resort, a 50% joint venture with Saratoga Harness Racing, Inc. ("SHRI") formed to bid on the development and management of a destination casino and resort in the Capital Region of New York;

• Bluff Media ("Bluff"), a multimedia poker content brand and publishing company, which we acquired on February 10, 2012; and

• Our other minor investments.

B. Acquisition, Development & Disposal Activity

Big Fish Games

On December 16, 2014, the Company completed the acquisition of Big Fish Games for upfront consideration of \$485 million plus a working capital adjustment with an earnout payment of up to \$350 million. Big Fish Games, headquartered in Seattle, Washington, with offices in Oakland, California and Luxembourg, employs approximately 580 employees and develops casual games for PCs and mobile devices worldwide. Big Fish Games operates in three business lines: premium paid, casino and casual free-to-play. The Company acquired Big Fish Games to leverage its casino and casual game experience, as well as its assembled workforce, and to position itself as a leader in the mobile and online games industry. The Company financed the upfront consideration for the acquisition with borrowings under its Amended and Restated Credit Agreement (the "Senior Secured Credit Facility") and a \$200 million Term Loan Facility ("Term Loan") added to its existing Senior Secured Credit Facility.

Saratoga Harness Racing, Inc. Joint Ventures

On May 13, 2014, the Company entered into a 50% joint venture with Saratoga Harness Racing, Inc. ("SHRI") to bid on the development, construction and operation of the Capital View Casino & Resort located in the Capital Region near Albany, New York. On June 30, 2014, the joint venture filed an application with the New York State Facility Location Board to obtain a license to build and operate a facility with approximately 1,500 slot machines, 56 table games, a 100-room hotel and multiple entertainment and dining options. On December 17, 2014, the New York State Facility Location Board recommended that the Capital Region license be granted to another bidder.

During the year ended December 31, 2014, the Company incurred \$1.0 million in equity losses in its other investments segment associated with the license application process and funded \$3.3 million to the joint venture. Due to the result of the bidding process, we recorded an impairment loss of \$1.6 million to reduce the value of the Company's investment in the joint venture to its estimated fair market value of \$1.1 million.

On October 28, 2014, the Company signed a definitive purchase agreement to acquire a 25% ownership interest in Saratoga Casino Holdings, LLC ("SCH"), a newly formed entity which owns Saratoga Casino and Raceway in Saratoga Springs, NY; SHRI's controlling interest in Saratoga Casino Black Hawk in Black Hawk, Colorado; SHRI's 50% interest in a joint venture with Delaware North Companies to manage the Gideon Putnam Hotel and Resort in Saratoga Springs, New York; its interest in the proposed Capital View Casino & Resort in East Greenbush, New York; and SHRI's interest in a joint venture with Rush Street Gaming to build the proposed Hudson Valley Casino and Resort in Newburgh, New York.

In addition, the Company signed a five-year management agreement pursuant to which it will manage Saratoga Casino and Raceway and Saratoga Casino Black Hawk. Both the funding of the equity investment and the commencement of the management agreement are subject to regulatory approval and licensing requirements in New York and Colorado.

Oxford

On July 17, 2013, the Company completed its acquisition of Oxford in Oxford, Maine for cash consideration of approximately \$168.6 million. The transaction included the acquisition of a 25,000-square-foot casino with various dining facilities on approximately 130 acres of land. The acquisition continued the Company's diversification and

growth strategies to invest in assets with rates of returns attractive to the Company's shareholders. The Company financed the acquisition with borrowings under its Senior Secured Credit Facility. During December 2013, Oxford continued an expansion of its facilities, adding an additional 46 slot machines and four table games. An additional twelve slot machines were added to the facilities during 2014.

Miami Valley Gaming Joint Venture

During March 2012, the Company entered into a 50% joint venture with Delaware North Companies Gaming & Entertainment Inc. (“DNC”) to develop a new harness racetrack and video lottery terminal (“VLT”) casino facility in Lebanon, Ohio.

Through the joint venture agreement, the Company and DNC formed a new company, MVG, to manage both the Company’s and DNC’s interests in the development and operation of the racetrack and VLT casino facility. During the years ended December 31, 2014, 2013 and 2012, the Company funded \$14.6 million, \$70.5 million and \$19.9 million in capital contributions to the joint venture, respectively. On December 21, 2012, MVG completed the purchase of the harness racing licenses and certain assets held by Lebanon Trotting Club Inc. and Miami Valley Trotting Inc. for total consideration of \$60.0 million, of which \$10.0 million was funded at closing with the remainder funded through a \$50.0 million note payable with a six-year term effective upon the commencement of casino operations. In addition, there is a potential contingent consideration payment of \$10.0 million based on the financial performance of the facility during the seven-year period after casino operations commence.

On December 12, 2013, the new facility opened on a 120-acre site. The facility includes a 5/8-mile harness racing track and a 186,000-square-foot gaming facility with approximately 1,580 VLTs. MVG has invested approximately \$204.6 million in the new facility, which includes a \$50.0 million license fee.

Luckity ADW Operations

On November 4, 2014, we ceased operations of Luckity, our ADW business which offered real-money online bingo with outcomes based on and determined by pari-mutuel wagers on live horseraces. We determined that Luckity did not achieve the expected financial returns and was unlikely to significantly improve its results. During the fourth quarter of 2014, we recorded an impairment charge of \$3.2 million for fixed assets specifically associated with Luckity. We do not expect to incur any additional, material expenditures in connection with ceasing operations.

Calder Racecourse

On July 1, 2014, we finalized an agreement with The Stronach Group (“TSG”) under which TSG operates, at TSG’s expense, live racing and maintains certain facilities used for racing and training at Calder. The agreement, which expires on December 31, 2020, includes a lease to TSG of Calder’s racetrack and certain other racing and training facilities, including a portion of the barns on Calder’s backside consisting of approximately 430 stalls. TSG will operate live horse racing at Calder under Calder’s racing permits in compliance with all applicable laws and licensing requirements. TSG operates and maintains the racing and training facilities at Calder on a year-round basis. Furthermore, TSG is responsible for substantially all of the direct and indirect costs associated with these activities and receive the associated revenues. We continue to own and operate the Calder Casino.

As part of the agreement with TSG, effective July 1, 2014, we amended Calder’s agreement with the Florida Horsemen’s Benevolent and Protective Association, Inc. (“FHBPA”) which reduced the rate of non-stakes purse supplements payable by the Calder Casino from 12 percent to 10 percent of slot machine revenue. Finally, we modified our HRTV operating and ownership agreement with TSG which resulted in the divestiture of the Company’s interest in HRTV on January 2, 2015.

Bluff

Bluff, which we acquired in February 2012, operates a poker periodical, BLUFF Magazine and BluffMagazine.com; ThePokerDB, a comprehensive online database and resource that tracks and ranks the performance of poker players and tournaments; and various other news and content forums. During January 2015, we ceased the distribution of BLUFF Magazine in paper form and now distribute Bluff only electronically.

C. Racing

We conduct live horseracing at Churchill Downs, Fair Grounds and Arlington. The following is a summary of our significant live racing events, a description of our properties and our annual racing calendar.

The Kentucky Derby and the Kentucky Oaks, both held at Churchill Downs, continue to be our premier racing events offering minimum purses of \$2.0 million and \$1.0 million, respectively. The Kentucky Derby is the first race of the annual series of races for 3-year old thoroughbreds known as the Triple Crown. Our other significant stakes races include the Arlington Million at Arlington and the Louisiana Derby at Fair Grounds, each of which offers purses of

approximately \$0.8 million.

Churchill Downs

The Churchill Downs racetrack site and improvements (the “Churchill facility”) are located in Louisville, Kentucky. Churchill Downs has conducted thoroughbred racing continuously since 1875 and is internationally known as the home of the Kentucky Derby. The Churchill facility consists of approximately 147 acres of land with a one-mile dirt track, a seven-eighths (7/8) mile turf track, a grandstand, luxury suites and a stabling area. The Churchill facility accommodates approximately 57,400 persons in our clubhouse, grandstand, Jockey Club Suites, Finish Line Suites, Grandstand Terrace, Rooftop Garden and Mansion. The Churchill facility also has a saddling paddock, accommodations for groups and special events, parking areas for the public, our

racetrack office facilities, and includes permanent lighting in order to accommodate night races. The stable area has barns sufficient to accommodate approximately 1,400 horses, a 114-room dormitory and other facilities for backstretch personnel. The Churchill facility also includes a simulcast wagering facility, "The Parlay", designed to accommodate 600 persons, which is Churchill Downs' simulcast wagering facility during the months outside of its live racing meets and houses the track's media operations in the weeks leading up to the Kentucky Derby, and a hospitality venue, "The Mansion". The Mansion, located on the sixth floor of the Clubhouse, is used primarily during the Kentucky Derby and Kentucky Oaks. The Mansion has accommodations for 296 guests and offers seating in its Dining Room, Living Room, Library, Parlor and Veranda. The Churchill facility opened the Grandstand Terrace and Rooftop Garden during the second quarter of 2014. This new area offers nearly 2,400 new seats and updated restrooms, wagering windows and food and beverage offerings. In the second quarter of 2014, the Churchill facility also completed the installation of a 15,224 square foot, state of the art high-definition video board, which provides an enhanced viewing experience for patrons. During the second quarter of 2015, the Churchill facility plans to open its new winner's circle suites and a courtyard. The winner's circle suites will include 20 private, open-air suites reserved specifically for Kentucky Derby and Oaks horsemen. The courtyard will be a spacious lawn area in front of the winner's circle suites.

To supplement the facilities at Churchill Downs, we provided additional stabling facilities sufficient to accommodate 500 horses and a three-quarter (3/4) mile dirt track at a facility known as Trackside Louisville. Trackside Louisville previously operated as a simulcast wagering facility until 2013, when it ceased operations. The simulcast wagering portion of the facility, a 100,000 square-foot property on approximately 88 acres of land, was razed during January 2015.

As part of financing improvements to the Churchill facility, during 2002, we transferred title of the Churchill facility to the City of Louisville, Kentucky and leased back the facility. Subject to the terms of the lease, we can re-acquire the facility at any time for \$1.00.

Calder

The Calder racetrack and improvements (the "Calder facility") are located in Miami-Dade County, Florida. The Calder facility is adjacent to Sun Life Stadium, home of the Miami Dolphins, and consists of approximately 231 acres of land with a one-mile dirt track, seating for 15,000 persons, food and beverage facilities, barns and stabling facilities. During 2014, Calder raced from January to June. Effective July 1, 2014, TSG assumed racing operations at the facility, as more fully described in subheading "J. Government Regulation, Florida" in Item 1. "Business" of this Annual Report on Form 10-K. We continue to assess potential alternative uses of the Calder facility not associated with the TSG lease agreement, and during 2014, we accelerated depreciation expense related to Calder's barns, which are not expected to be utilized subsequent to December 31, 2014.

Fair Grounds

The Fair Grounds racetrack facility, located in New Orleans, Louisiana, consists of approximately 145 acres of land, a one-mile dirt track, a seven-eighths (7/8) mile turf track, a grandstand and a stabling area. The facility includes clubhouse and grandstand seating for approximately 5,000 persons, a general admissions area and food and beverage facilities ranging from concessions to clubhouse dining. The stable area consists of a receiving barn, feed rooms, tack rooms, detention barns and living quarters that can accommodate 132 persons and approximately 2,000 horses. The Fair Grounds facility also features a saddling paddock, parking areas and office facilities.

Arlington

The Arlington racetrack, located in Arlington Heights, Illinois, was constructed in 1927 and reopened its doors in 1989 after a fire four years earlier. The racetrack sits on 336 acres, has a one and one-eighth (1 1/8) mile synthetic track, a one-mile turf track and a five-eighths (5/8) mile training track. The facility includes a clubhouse, grandstand and suite seating for 6,045 persons and food and beverage facilities. The stable area has 34 barns able to accommodate approximately 2,200 horses and a temporary housing unit that accommodates 288 persons. The Arlington facility also features a saddling paddock, parking areas and office facilities.

Racing Calendar

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The following table is a summary of our expected 2015 and actual 2014 live thoroughbred racing dates for each of our racetracks. Racing dates are generally approved annually by the respective state racing authorities:

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	2015		2014	
Racetrack	Racing Dates	# of Days	Racing Dates	# of Days
Churchill Downs				
Spring Meet	April 25 - June 27	38	April 26 - June 29	38
September Meet	Sept. 11- Sept. 27	11	Sept. 4 - Sept. 28	12
Fall Meet	Nov. 1 - Nov. 29	21	Oct. 26 - Nov. 30	24
		70		74
Calder Race Course				
Calder Meet	N/A	—	Jan. 1 - June 30	79
Tropical Meet	N/A	—	N/A	—
		—		79
Arlington	April 27 - Sept. 30	77	May 2 - Sept. 28	89
Fair Grounds				
Winter Meet 13/14				