OPPENHEIMER HOLDINGS INC
Form 10-Q
November 10, 2011

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As filed with the Securities and Exchange Commission on November 10, 2011.

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

þ **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**

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: 1-12043**

**OPPENHEIMER HOLDINGS INC.**

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware<br>(State or other jurisdiction of incorporation or organization) | 98-0080034<br>(I.R.S. Employer Identification No.) |

125 Broad Street
New York, New York 10004
(Address of principal executive offices) (Zip Code)
(212) 668-8000
(Registrant s telephone number, including area code)
None
(Former name, former address and former fiscal year, if changed since last report)

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 þ 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 þ 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 smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

| | | | |
|---|---|---|---|
| Large accelerated filer o | Accelerated filer þ | Non-accelerated filer o | Smaller reporting company o |

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

The number of shares of the Company s Class A non-voting common stock and Class B voting common stock (being the only classes of common stock of the Company) outstanding on October 31, 2011 was 13,572,265 and 99,680 shares, respectively.

OPPENHEIMER HOLDINGS INC.
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## PART I
## FINANCIAL INFORMATION

### Item. 1 Financial Statements

OPPENHEIMER HOLDINGS INC.
CONDENSED CONSOLIDATED BALANCE SHEETS (unaudited)

| *(Expressed in thousands of dollars)* | September 30, 2011 | December 31, 2010 |
|---|---|---|
| ASSETS | | |
| Cash and cash equivalents | $ 87,496 | $ 52,854 |
| Cash and securities segregated for regulatory and other purposes | 199,948 | 142,446 |
| Deposits with clearing organizations | 22,574 | 23,228 |
| Receivable from brokers and clearing organizations | 335,266 | 302,844 |
| Receivable from customers, net of allowance for doubtful accounts of $2,399 ($2,716 in 2010) | 893,571 | 924,817 |
| Income taxes receivable | 5,135 | 5,142 |
| Securities purchased under agreement to resell | 589,665 | 347,070 |
| Securities owned, including amounts pledged of $402,666 ($102,501 in 2010), at fair value | 796,865 | 367,019 |
| Notes receivable, net | 55,965 | 59,786 |
| Office facilities, net | 18,047 | 22,875 |
| Intangible assets, net | 37,735 | 40,979 |
| Goodwill | 137,889 | 137,889 |
| Other | 166,306 | 198,665 |
| | $ 3,346,462 | $ 2,625,614 |

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

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OPPENHEIMER HOLDINGS INC.
CONDENSED CONSOLIDATED BALANCE SHEETS (unaudited)

| *(Expressed in thousands of dollars)* | September 30, 2011 | December 31, 2010 |
|---|---|---|
| LIABILITIES AND EQUITY | | |
| Liabilities | | |
| Drafts payable | $ 46,049 | $ 61,055 |
| Bank call loans | 59,300 | 147,000 |
| Payable to brokers and clearing organizations | 426,590 | 372,697 |
| Payable to customers | 576,981 | 406,916 |
| Securities sold under agreement to repurchase | 860,360 | 390,456 |
| Securities sold, but not yet purchased, at fair value | 210,980 | 160,052 |
| Accrued compensation | 129,050 | 175,938 |
| Accounts payable and other liabilities | 308,233 | 265,535 |
| Senior secured note | 200,000 | |
| Senior secured credit note | | 22,503 |
| Subordinated note | | 100,000 |
| Deferred income tax, net | 13,637 | 11,186 |
| Excess of fair value of acquired assets over cost | 7,020 | 7,020 |
| | 2,838,200 | 2,120,358 |
| Equity | | |
| Oppenheimer Holdings Inc. stockholders equity Share capital | | |
| Class A non-voting common stock | | |
| (2011 13,570,945 shares issued and outstanding | | |
| 2010 13,268,522 shares issued and outstanding) | 62,551 | 51,768 |
| Class B voting common stock | | |
| 99,680 shares issued and outstanding | 133 | 133 |
| | 62,684 | 51,901 |
| Contributed capital | 35,951 | 47,808 |
| Retained earnings | 404,685 | 402,308 |
| Accumulated other comprehensive income | 135 | 207 |
| Stockholders equity | 503,455 | 502,224 |
| Noncontrolling interest | 4,807 | 3,032 |
| Total equity | 508,262 | 505,256 |
| | $ 3,346,462 | $ 2,625,614 |

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

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OPPENHEIMER HOLDINGS INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| *Expressed in thousands of dollars, except share and per share amounts* | 2011 | 2010 | 2011 | 2010 |
| REVENUE: | | | | |
| Commissions | $ 123,267 | $ 120,940 | $ 380,912 | $ 398,719 |
| Principal transactions, net | 8,233 | 22,646 | 32,537 | 60,803 |
| Interest | 15,161 | 11,220 | 43,599 | 31,996 |
| Investment banking | 29,199 | 21,791 | 91,357 | 83,311 |
| Advisory fees | 50,696 | 43,356 | 149,200 | 130,134 |
| Other | 5,063 | 15,190 | 31,949 | 34,550 |
| | 231,619 | 235,143 | 729,554 | 739,513 |
| EXPENSES: | | | | |
| Compensation and related expenses | 148,951 | 159,486 | 479,802 | 485,765 |
| Clearing and exchange fees | 6,514 | 5,525 | 19,127 | 19,910 |
| Communications and technology | 15,138 | 15,838 | 47,146 | 48,578 |
| Occupancy and equipment costs | 18,977 | 18,162 | 56,047 | 54,884 |
| Interest | 10,230 | 6,546 | 28,673 | 18,016 |
| Other | 27,545 | 22,127 | 82,962 | 75,615 |
| | 227,355 | 227,684 | 713,757 | 702,768 |
| Profit before income taxes | 4,264 | 7,459 | 15,797 | 36,745 |
| Income tax provision | 1,805 | 3,210 | 7,139 | 14,871 |
| Net profit for the period | 2,459 | 4,249 | 8,658 | 21,874 |
| Less net profit attributable to non-controlling interest, net of tax | 353 | 595 | 1,775 | 1,505 |
| Net profit attributable to Oppenheimer Holdings Inc. | $ 2,106 | $ 3,654 | $ 6,883 | $ 20,369 |
| Profit per share attributable to Oppenheimer Holdings Inc.: | | | | |
| Basic | $ 0.15 | $ 0.27 | $ 0.51 | $ 1.53 |
| Diluted | $ 0.15 | $ 0.26 | $ 0.49 | $ 1.46 |
| Weighted average common shares: | | | | |
| Basic | 13,670,604 | 13,355,468 | 13,627,122 | 13,334,214 |
| Diluted | 13,915,897 | 13,956,711 | 13,922,637 | 13,920,725 |
| Dividends declared per share | $ 0.11 | $ 0.11 | $ 0.33 | $ 0.33 |

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

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OPPENHEIMER HOLDINGS INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(unaudited)

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| *Expressed in thousands of dollars* | 2011 | 2010 | 2011 | 2010 |
| Net profit for the period | $ 2,459 | $ 4,249 | $ 8,658 | $ 21,874 |
| Other comprehensive income: | | | | |
| Currency translation adjustment | (1,513) | 1,290 | (1,394) | 1,059 |
| Change in cash flow hedges, net of tax | | (146) | 1,322 | (963) |
| Comprehensive income for the period | 946 | 5,393 | 8,586 | 21,970 |
| Comprehensive income attributable to non-controlling interests | 353 | 595 | 1,775 | 1,505 |
| Comprehensive income attributable to Oppenheimer Holdings Inc. | $ 593 | $ 4,798 | $ 6,811 | $ 20,465 |

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

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OPPENHEIMER HOLDINGS INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

| *Expressed in thousands of dollars* | Nine months ended September 30, 2011 | 2010 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net profit for the period | $ 8,658 | $ 21,874 |
| Adjustments to reconcile net profit to net cash provided by (used in) operating activities: | | |
| Non-cash items included in net profit: | | |
| Depreciation and amortization | 9,299 | 9,053 |
| Deferred income tax | 2,451 | 32,336 |
| Amortization of notes receivable | 15,103 | 15,062 |
| Amortization of debt issuance costs | 734 | 742 |
| Amortization of intangibles | 3,244 | 3,243 |
| Provision for credit losses | (317) | 336 |
| Share-based compensation | 118 | 3,979 |
| Decrease (increase) in operating assets: | | |
| Cash and securities segregated for regulatory and other purposes | (57,502) | (43,280) |
| Deposits with clearing organizations | 654 | (6,632) |
| Receivable from brokers and clearing organizations | (32,422) | 1,824 |
| Receivable from customers | 31,563 | (11,595) |
| Income taxes receivable | 7 | (30,566) |
| Securities purchased under agreement to resell | (242,595) | (61,713) |
| Securities owned | (429,846) | (183,638) |
| Notes receivable | (11,282) | (16,966) |
| Other | 29,625 | (19,252) |
| Increase (decrease) in operating liabilities: | | |
| Drafts payable | (15,006) | (9,767) |
| Payable to brokers and clearing organizations | 55,215 | (30,972) |
| Payable to customers | 170,065 | (57,791) |
| Securities sold under agreement to repurchase | 469,904 | 290,496 |
| Securities sold, but not yet purchased | 50,928 | (9,132) |
| Accrued compensation | (46,796) | (36,971) |
| Accounts payable and other liabilities | 42,698 | 75,501 |
| Cash provided by (used in) operating activities | 54,500 | (63,829) |

(Continued on next page)

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OPPENHEIMER HOLDINGS INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited) Continued

| *Expressed in thousands of dollars* | Nine months ended September 30, 2011 | 2010 |
|---|---|---|
| Cash flows from investing activities: | | |
| Purchase of office facilities | (3,865) | (11,877) |
| Cash used in investing activities | (3,865) | (11,877) |
| Cash flows from financing activities: | | |
| Cash dividends paid on Class A non-voting and Class B voting common stock | (4,506) | (4,401) |
| Issuance of Class A non-voting common stock | 337 | 2,132 |
| Tax shortfall from share-based compensation | (1,621) | (101) |
| Senior secured note issuance. | 200,000 | |
| Senior secured credit note repayment | (22,503) | (9,500) |
| Subordinated note repayment | (100,000) | |
| Increase (decrease) in bank call loans, net | (87,700) | 68,800 |
| Cash (used in) provided by financing activities | (15,993) | 56,930 |
| Net increase (decrease) in cash and cash equivalents | 34,642 | (18,776) |
| Cash and cash equivalents, beginning of period | 52,854 | 68,918 |
| Cash and cash equivalents, end of period | $ 87,496 | $ 50,142 |
| Schedule of non-cash investing and financing activities: | | |
| Employee share plan issuance | $ 10,446 | $ 1,765 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid during the periods for interest | $ 15,309 | $ 15,933 |
| Cash paid during the periods for income taxes | $ 7,680 | $ 11,402 |

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

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OPPENHEIMER HOLDINGS INC.
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (unaudited)

| *Expressed in thousands of dollars* | Nine months ended September 30, 2011 | 2010 |
|---|---|---|
| **Share capital** | | |
| Balance at beginning of period | $ 51,901 | $ 47,824 |
| Issuance of Class A non-voting common stock | 10,783 | 3,897 |
| Balance at end of period | $ 62,684 | $ 51,721 |
| **Contributed capital** | | |
| Balance at beginning of period | $ 47,808 | $ 41,978 |
| Vested employee share plan awards | (13,348) | (1,710) |
| Tax shortfall from share-based awards | (1,621) | (101) |
| Share-based compensation expense | 3,112 | 5,919 |
| Balance at end of period | $ 35,951 | $ 46,086 |
| **Retained earnings** | | |
| Balance at beginning of period | $ 402,308 | $ 369,697 |
| Net profit for the period attributable to Oppenheimer Holdings Inc. | 6,883 | 20,369 |
| Dividends ($0.33 per share in 2011 and 2010) | (4,506) | (4,401) |
| Balance at end of period | $ 404,685 | $ 385,665 |
| **Accumulated other comprehensive income (loss)** | | |
| Balance at beginning of period | $ 207 | $ (543) |
| Currency translation adjustment | (1,394) | 1,059 |
| Change in cash flow hedges, net of tax | 1,322 | (963) |
| Balance at end of period | $ 135 | $ (447) |
| **Stockholders Equity** | $ 503,455 | $ 483,025 |
| **Non-controlling interest** | | |
| Balance at beginning of period | $ 3,032 | $ |
| Grant of non-controlling interest | | 731 |
| Net profit attributable to non-controlling interest for the period, net of tax | 1,775 | 1,505 |
| Balance at end of period | $ 4,807 | $ 2,236 |
| **Total equity** | $ 508,262 | $ 485,261 |

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

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OPPENHEIMER HOLDINGS INC.

Notes to Condensed Consolidated Financial Statements (Unaudited)

**1. Summary of significant accounting policies**

Oppenheimer Holdings Inc. ( OPY ) is incorporated under the laws of the State of Delaware. The consolidated financial statements include the accounts of OPY and its subsidiaries (together, the Company ). The principal subsidiaries of OPY are Oppenheimer & Co. Inc. ( Oppenheimer ), a registered broker dealer in securities, Oppenheimer Asset Management Inc. ( OAM ) and its wholly owned subsidiary, Oppenheimer Investment Management Inc. ( OIM ), both registered investment advisors under the Investment Advisors Act of 1940, Oppenheimer Trust Company, a limited purpose trust company chartered by the State of New Jersey to provide fiduciary services such as trust and estate administration and investment management, Oppenheimer Multifamily Housing and Healthcare Finance, Inc. (formerly Evanston Financial Corporation) ( OMHHF ), which is engaged in mortgage brokerage and servicing, and OPY Credit Corp., which offers syndication as well as trading of issued corporate loans. Oppenheimer Europe Ltd. (formerly Oppenheimer E.U. Ltd.) ( Oppenheimer Europe ), based in the United Kingdom, provides institutional equities and fixed income brokerage and corporate financial services and is regulated by the Financial Services Authority. Oppenheimer Investments Asia Limited, based in Hong Kong, China, provides assistance in accessing the U.S. equities markets and limited mergers and acquisitions advisory services to Asia-based companies. Oppenheimer operates as Fahnestock & Co. Inc. in Latin America. Oppenheimer owns Freedom Investments, Inc. ( Freedom ), a registered broker dealer in securities, which also operates as the BUYandHOLD division of Freedom, offering on-line discount brokerage and dollar-based investing services, and Oppenheimer Israel (OPCO) Ltd., which is engaged in offering investment services in the State of Israel as a local broker dealer.

The Company s condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ). These accounting principles are set out in the notes to the Company s consolidated financial statements for the year ended December 31, 2010 included in its Annual Report on Form 10-K for the year then ended.

Accounting standards require the Company to present non-controlling interests (previously referred to as minority interests) as a separate component of stockholders equity on the Company s condensed consolidated balance sheet. As of September 30, 2011, the Company owned 67.34% of OMHHF and the non-controlling interest recorded in the condensed consolidated balance sheet was $4.8 million.

The condensed consolidated financial statements include all adjustments, which in the opinion of management are normal and recurring and necessary for a fair statement of the results of operations, financial position and cash flows for the interim periods presented. The nature of the Company s business is such that the results of operations for the interim periods are not necessarily indicative of the results to be expected for a full year.

Disclosures reflected in these condensed consolidated financial statements comply in all material respects with those required pursuant to the rules and regulations of the United States Securities and Exchange Commission ( SEC ) with respect to quarterly financial reporting.

Certain prior period amounts appearing in the notes to the condensed consolidated financial statements pertaining to the fair value measurement of derivative contracts have been reclassified to conform with current presentation.

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## 2. New accounting pronouncements

*Recently Adopted*

In December 2010, the Financial Accounting Standards Board (the FASB ) issued ASU No. 2010-28, Intangibles Goodwill and Other, which modified Step 1 of the goodwill impairment test for reporting units with a zero or negative carrying value, stating that under such circumstances an entity should perform Step 2 of the impairment analysis when it is more likely than not that goodwill is impaired. The Company adopted this requirement in the period ending March 31, 2011 with no impact on its financial statements.

In February 2010, the FASB issued ASU No. 2010-10, Consolidation Amendments for Certain Investment Funds , that will indefinitely defer the effective date of the updated Variable Interest Entity ( VIE ) accounting guidance for certain investment funds. To qualify for the deferral, the investment fund needs to meet certain attributes of an investment company, does not have explicit or implicit obligations to fund losses of the entity and is not a securitization entity, an asset-backed financing entity, or an entity formerly considered a qualifying special-purpose entity ( QSPE ). The Company s investment funds meet the conditions in ASU No. 2010-10 and qualify for the deferral adoption. Therefore, the Company is not required to consolidate any of its investment funds which are VIEs until further guidance is issued.

In January 2010, the FASB issued ASU No. 2010-06, Fair Value Measurement . ASU No. 2010-06 requires new disclosures regarding transfers of assets and liabilities measured at fair value in and out of Level 1 and 2 of the fair value hierarchy. A reporting entity should disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfer. ASU No. 2010-06 also provides additional guidance on the level of disaggregation of fair value measurements and disclosures regarding inputs and valuation techniques. The Company adopted this disclosure requirement in the three months ended March 31, 2010. In addition, ASU No.2010-06 requires the reconciliation of beginning and ending balances for fair value measurements using significant unobservable inputs (i.e., Level 3) to be presented on a gross basis. The Company adopted this requirement in the period ended March 31, 2011. See note 5 for further information.

*Recently Issued*

In April 2011, the FASB issued ASU No. 2011-03, Transfers and Servicing: Reconsideration of Effective Control for Repurchase Agreements, which removes the requirement to consider whether sufficient collateral is held when determining whether to account for repurchase agreements and other agreements that both entitle and obligate the transferor to repurchase or redeem financial assets before their maturity as sales or as secured financings. The guidance is effective prospectively for transactions beginning on January 1, 2012. The Company does not believe that the adoption of this guidance will have an impact on its financial condition, results of operations or cash flows.

In May 2011, the FASB issued ASU No. 2011-04, Fair Value Measurement: Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS, which provides clarifying guidance on how to measure fair value and has additional disclosure requirements. The amendments prohibit the use of blockage factors at all levels of the fair value hierarchy and provide guidance on measuring financial instruments that are managed on a net portfolio basis. Additional disclosure requirements include transfers between Levels 1 and 2 and, for Level 3 fair value measurements, a description of the valuation processes and additional information about unobservable inputs impacting Level 3 measurements. The updates are effective for the reporting period ending December 31, 2011. The Company is currently evaluating the impact, if any, that these updates will have on its financial condition, results of operations and cash flows.

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In June 2011, the FASB issued ASU No. 2011-05, Presentation of Comprehensive Income , requiring entities to present items of net income and other comprehensive income either in one continuous statement (referred to as the statement of comprehensive income) or in two separate, but consecutive, statements of net income and other comprehensive income. The Company intends to adopt this requirement in the period ending December 31, 2011.

In September, 2011, the FASB issued ASU No. 2011-08, Testing Goodwill for Impairment , which gives entities the option of performing a qualitative assessment before the quantitative analysis. If entities determine the fair value of a reporting unit is more likely than not less than the carrying amount based on the qualitative factors, the two-step quantitative test would be required. Otherwise, further testing would not be needed. The ASU is effective for fiscal years beginning after December 15, 2011 and early adoption is permitted. The Company is currently evaluating whether it will early adopt the ASU.

**3. Revision to financial statements**

During the three months ended September 30, 2011, the Company identified historical errors relating to its tax treatment of deferred compensation obligations assumed as part of the 2003 acquisition of the Private Client Division from Canadian Imperial Bank of Commerce ( CIBC ) that affected prior periods. As a result, the Company has determined the need to reestablish book basis of goodwill related to the 2003 transaction in the amount of $5.4 million. Further analysis revealed uncertain tax positions, that were inadvertently taken as a result of the errors, leading to the establishment of a reserve in the amount of $3 million, including accrued interest, as well as cumulative adjustments to current and deferred tax items of $6.6 million primarily related to periods prior to 2008.

The Company assessed the impact of the errors, including the impact of previously disclosed out-of-period adjustments, on its prior period financial statements included in the December 31, 2010 Form 10-K and concluded that these errors were not material, individually or in the aggregate, to any of those financial statements. Although the effect of these errors was not material to any previously issued financial statements, the cumulative effect of correcting these historical errors in the current year would have been material for the fiscal year 2011. Consequently, the Company has revised its prior period financial statements by adjusting opening retained earnings as of January 1, 2010 in the amount of $7.5 million. As part of this revision process, the Company also reversed other previously disclosed out-of-period adjustments (see below for more details), which were immaterial, and recorded them instead in the periods in which the errors originated. These revisions have no net impact on the Company s net cash amounts provided by (used in) operating, financing or investing activities for the any of the periods previously reported, nor in the current period.

The financial statements as of September 30, 2010, and for the three and nine-month periods then ended and as of December 31, 2010, included herein have been prepared in light of the cumulative revisions above. The financial statements for all other periods affected by the revisions can continue to be relied upon, and will be revised to reflect the revisions discussed above, the next time such financial statements are included in future reports for comparative purposes.

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As previously disclosed, the Company identified certain over-accruals in compensation and related expenses related to prior periods which the Company adjusted during the three month period ended March 31, 2010. These previously recorded out-of-period adjustments, which were not material to any prior period, resulted in an increase to compensation and related expenses of $3.7 million for the year ended December 31, 2010. The over-accruals occurred in the Global High Yield ( GHY ) loan sales and trading business and were the result of duplicate production related compensation expenses being accrued. In addition, the Company had other out-of-period adjustments in 2010 that offset the over-accrual of GHY compensation totaling $1.1 million that were also corrected in the three month period ended March 31, 2010. Most notably was the reversal of a legal accrual of $1 million related to the settlement of an Auction Rate Securities ( ARS ) case and the recognition of a fair value adjustment of $1.1 million related to ARS as a result of this legal settlement (net effect of $67,000). The remaining out-of-period adjustments, individually of lesser amounts, in the aggregate were