COGENT COMMUNICATIONS HOLDINGS, INC.
Form 10-Q
November 07, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x 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

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

Commission File No. 000-51829

COGENT COMMUNICATIONS HOLDINGS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	**46-5706863**

(State of Incorporation) (I.R.S. Employer Identification Number)

1015 31st Street N.W.

Washington, D.C. 20007

(Address of Principal Executive Offices and Zip Code)

(202) 295-4200

(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, and (2) has been subject to such filing requirements for the past 90 days. Yes x 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 x 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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Common Stock, $.001 par value 46,240,836 Shares Outstanding as of October 31, 2014

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

COGENT COMMUNICATIONS HOLDINGS, INC., AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

AS OF SEPTEMBER 30, 2014 AND DECEMBER 31, 2013

(IN THOUSANDS, EXCEPT SHARE DATA)

	September 30, 2014 (Unaudited)	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	$ 311,779	$ 304,866
Accounts receivable, net of allowance for doubtful accounts of $2,012 and $1,871, respectively	31,770	30,628
Prepaid expenses and other current assets	20,705	18,777
Total current assets	364,254	354,271
Property and equipment, net	357,699	341,193
Deferred tax assets - noncurrent	49,175	50,861
Deposits and other assets - $392 and $448 restricted, respectively	13,333	8,776
Total assets	$ 784,461	$ 755,101
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 16,303	$ 14,098
Accrued liabilities	31,257	31,465
Convertible senior notes - current portion, net of discount of $3,099 (Note 3)		88,879
Current maturities, capital lease obligations	8,980	9,252
Total current liabilities	56,540	143,694
Senior secured notes including premium of $4,535 and $5,423, respectively	244,535	245,423
Senior unsecured notes	200,000	
Capital lease obligations, net of current maturities	153,495	152,527
Other long term liabilities	21,227	19,965
Total liabilities	675,797	561,609
Commitments and contingencies:		
Stockholders equity:		
Common stock, $0.001 par value; 75,000,000 shares authorized; 46,449,080 and 47,334,218 shares issued and outstanding, respectively	46	47
Additional paid-in capital	467,846	508,256
Accumulated other comprehensive income foreign currency translation	(3,404)	2,136
Accumulated deficit	(355,824)	(316,947)
Total stockholders equity	108,664	193,492
Total liabilities and stockholders equity	$ 784,461	$ 755,101

The accompanying notes are an integral part of these condensed consolidated balance sheets.

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COGENT COMMUNICATIONS HOLDINGS, INC., AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2014 AND SEPTEMBER 30, 2013

(IN THOUSANDS, EXCEPT SHARE AND PER SHARE AMOUNTS)

	Three Months Ended September 30, 2014 (Unaudited)	Three Months Ended September 30, 2013 (Unaudited)
Service revenue	$ 95,691	$ 87,761
Operating expenses:		
Network operations (including $114 and $114 of equity-based compensation expense, respectively, exclusive of depreciation and amortization shown separately below)	40,407	37,441
Selling, general, and administrative (including $2,578 and $1,947 of equity-based compensation expense, respectively)	27,353	21,719
Gain on equipment transaction	(3,114)	
Depreciation and amortization	17,431	16,024
Total operating expenses	82,077	75,184
Operating income	13,614	12,577
Interest income and other, net	140	292
Interest expense	(12,662)	(10,568)
Income before income taxes	1,092	2,301
Income tax provision	(1,276)	(179)
Net (loss) income	$ (184)	$ 2,122
Comprehensive (loss) income:		
Net (loss) income	$ (184)	$ 2,122
Foreign currency translation adjustment	(5,034)	2,341
Comprehensive (loss) income	$ (5,218)	$ 4,463
Net (loss) income per common share:		
Basic and diluted net (loss) income per common share	$ (0.00)	$ 0.05
Dividends declared per common share	$ 0.30	$ 0.14
Weighted-average common shares - basic	45,629,079	46,171,194
Weighted-average common shares - diluted	45,629,079	46,823,167

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

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COGENT COMMUNICATIONS HOLDINGS, INC., AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2014 AND SEPTEMBER 30, 2013

(IN THOUSANDS, EXCEPT SHARE AND PER SHARE AMOUNTS)

	Nine Months Ended September 30, 2014 (Unaudited)	Nine Months Ended September 30, 2013 (Unaudited)
Service revenue	$ 283,252	$ 258,118
Operating expenses:		
Network operations (including $341 and $395 of equity-based compensation expense, respectively, exclusive of depreciation and amortization shown separately below)	118,848	111,825
Selling, general, and administrative (including $6,229 and $6,317 of equity-based compensation expense, respectively)	79,775	64,410
Gains on equipment transactions	(8,140)	
Depreciation and amortization	51,937	47,798
Total operating expenses	242,420	224,033
Operating income	40,832	34,085
Interest income and other, net	544	1,537
Interest expense	(37,756)	(30,653)
Income before income taxes	3,620	4,969
Income tax provision	(2,471)	(879)
Net income	$ 1,149	$ 4,090
Comprehensive (loss) income:		
Net income	$ 1,149	$ 4,090
Foreign currency translation adjustment	(5,540)	874
Comprehensive (loss) income	$ (4,391)	$ 4,964
Net income per common share:		
Basic and diluted net income per common share	$ 0.02	$ 0.09
Dividends declared per common share	$ 0.86	$ 0.39
Weighted-average common shares - basic	46,111,192	46,145,642
Weighted-average common shares - diluted	46,526,523	46,905,154

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

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COGENT COMMUNICATIONS HOLDINGS, INC., AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2014 AND SEPTEMBER 30, 2013

(IN THOUSANDS)

	Nine months Ended September 30, 2014 (Unaudited)	Nine months Ended September 30, 2013 (Unaudited)
Cash flows from operating activities:		
Net income	$ 1,149	$ 4,090
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	51,937	47,798
Amortization of debt discount and premium	2,269	4,696
Equity-based compensation expense (net of amounts capitalized)	6,570	6,712
(Gains) losses equipment transactions and other, net	(7,780)	(24)
Deferred income taxes	1,911	418
Changes in operating assets and liabilities:		
Accounts receivable	(2,081)	(4,509)
Prepaid expenses and other current assets	(2,890)	(2,767)
Accounts payable, accrued liabilities and other long-term liabilities	4,616	(4,478)
Deposits and other assets	(596)	627
Net cash provided by operating activities	55,105	52,563
Cash flows from investing activities:		
Purchases of property and equipment	(47,010)	(38,936)
Proceeds from dispositions of assets	91	42
Net cash used in investing activities	(46,919)	(38,894)
Cash flows from financing activities:		
Dividends paid	(40,026)	(18,146)
Purchases of common stock	(48,027)	
Repayment of convertible senior notes	(91,978)	
Net proceeds from issuance of senior secured notes		69,882
Net proceeds from issuance of senior unsecured notes	195,824	
Proceeds from exercises of stock options	438	974
Principal payments of capital lease obligations	(15,439)	(8,930)
Net cash provided by financing activities	792	43,780
Effect of exchange rates changes on cash	(2,065)	41
Net increase in cash and cash equivalents	6,913	57,490
Cash and cash equivalents, beginning of period	304,866	247,285
Cash and cash equivalents, end of period	$ 311,779	$ 304,775
Supplemental disclosure of non-cash financing activities:		
Non-cash component of network equipment obtained in exchange transactions	$ 8,014	$
Capital lease obligations incurred	$ 19,107	$ 27,649

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

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COGENT COMMUNICATIONS HOLDINGS, INC., AND SUBSIDIARIES

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Description of the business and recent developments:

Reorganization and merger

On May 15, 2014, pursuant to the Agreement and Plan of Reorganization (the Merger Agreement) by and among Cogent Communications Group, Inc. (Group), a Delaware corporation, Cogent Communications Holdings, Inc., a Delaware corporation (Holdings) and Cogent Communications Merger Sub, Inc., a Delaware corporation (Merger Sub), Group adopted a new holding company organizational structure whereby Group is now a wholly owned subsidiary of Holdings. Holdings is a successor issuer to Group pursuant to Rule 12g-3(a) under the Securities Exchange Act of 1934, as amended (the Exchange Act). In connection with the succession, the common stock of Holdings is deemed to be registered under Section 12(b) of the Exchange Act by operation of law.

The holding company organizational structure was effected by a merger (the Merger) structured as a tax-free transaction and conducted pursuant to Section 251(g) of Delaware General Corporation Law which provides for the formation of a holding company structure without a vote of the stockholders of the constituent corporations. Because the holding company organizational structure has occurred at the parent company level, the remainder of the Company s subsidiaries, operations and customers were not affected by the Merger. Accordingly, the historical financial statements reflect the effect of the reorganization for all periods presented. Under the terms of the Merger Agreement, Merger Sub merged with and into Group, with Group surviving the Merger and becoming a direct, wholly owned subsidiary of Holdings.

Pursuant to the Merger Agreement, all of the outstanding capital stock of Group was converted, on a share for share basis, into the common stock of Holdings. As a result, each former stockholder of Group became the owner of an identical number of shares of common stock of Holdings, evidencing the same proportional interests in the Company (as defined below) and having the same designations, rights, powers and preferences, qualifications, limitations and restrictions, as those that the stockholder held in Group. Additionally, each outstanding option to purchase shares of common stock of Group was automatically converted into an option to purchase, upon the same terms and conditions, an identical number of shares of Holding s common stock. Each outstanding restricted share of common stock of Group was also converted into a restricted share of common stock of Holdings upon the same terms and conditions. The directors and executive officers of the Company immediately after completion of the Merger are comprised of the same persons who were directors of and executive officers of Group immediately prior to the Merger.

References to the Company for events that occurred prior to May 15, 2014 refer to Cogent Communications Group, Inc. and its subsidiaries and on and after May 15, 2014 the Company refers to Cogent Communications Holdings, Inc. and its subsidiaries.

Description of business

The Company is a Delaware corporation and is headquartered in Washington, DC. The Company is a facilities-based provider of low-cost, high-speed Internet access and Internet Protocol (IP) communications services. The Company s network is specifically designed and optimized to transmit data using IP. The Company delivers its services primarily to small and medium-sized businesses, communications service providers and other bandwidth-intensive organizations in North America, Europe and Japan.

The Company offers on-net Internet access services exclusively through its own facilities, which run from its network to its customers premises. The Company is not dependent on local telephone companies to serve its customers for its on-net Internet access services because of its integrated network architecture. The Company offers its on-net services to customers located in buildings that are physically connected to its network. The Company s on-net service consists of high-speed Internet access and IP connectivity ranging from 100 Megabits per second to 100 Gigabits per second of bandwidth. The Company provides its on-net Internet access services to its net-centric and corporate customers. The Company s net-centric customers include bandwidth-intensive users such as universities, other Internet service providers, telephone companies, cable television companies, web hosting companies, content delivery network companies and commercial content and application service providers. These net-centric customers obtain the Company s services in colocation facilities and in the Company s data centers. The Company operates data centers throughout North America and Europe that allow its customers to collocate their equipment and access the Company s network. The Company s corporate customers are located in multi-tenant office buildings and typically include law firms, financial services firms, advertising and marketing firms and other professional services businesses.

In addition to providing its on-net services, the Company provides Internet connectivity to customers that are not located in buildings directly connected to its network. The Company provides this off-net service primarily to corporate customers using other carriers facilities to provide the last mile portion of the link from the customers premises to the Company s network. The Company also provides certain non-core services that resulted from acquisitions. The Company continues to support but does not actively sell these non-core services.

Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, the unaudited condensed consolidated financial statements reflect all normal recurring adjustments that the Company considers necessary for the fair presentation of its results of operations and

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cash flows for the interim periods covered, and of the financial position of the Company at the date of the interim condensed consolidated balance sheet. Certain information and footnote disclosures normally included in the annual consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. The operating results for interim periods are not necessarily indicative of the operating results for the entire year. While the Company believes that the disclosures are adequate to not make the information misleading, these interim condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes included in its 2013 annual report on Form 10-K.

The accompanying unaudited consolidated financial statements include all wholly-owned subsidiaries. All inter-company accounts and activity have been eliminated.

Use of estimates

The preparation of consolidated financial statements in conformity with United States generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from these estimates.

Financial instruments

At September 30, 2014, the carrying amount of cash and cash equivalents, accounts receivable, prepaid and other current assets, accounts payable and accrued expenses approximated fair value because of the short-term nature of these instruments. The Company measures its cash equivalents at amortized cost, which approximates fair value based upon quoted market prices (Level 1). Based upon recent trading prices (Level 2 market approach) at September 30, 2014 the fair value of the Company s $200.0 million senior unsecured notes was $197.0 million and the fair value of the Company s $240.0 million senior secured notes was $252.0 million.

The Company was party to letters of credit totaling $0.4 million as of September 30, 2014. These letters of credit are secured by investments that are restricted and included in other assets.

Basic and diluted net income (loss) per common share

Basic earnings per share (EPS) excludes dilution for common stock equivalents and is computed by dividing net income or (loss) available to common stockholders by the weighted-average number of common shares outstanding for the period. Diluted EPS is based on the weighted-average number of shares of common stock outstanding during each period, adjusted for the effect of dilutive common stock equivalents.

Shares of restricted stock are included in the computation of basic EPS as they vest and are included in diluted EPS, to the extent they are dilutive, determined using the treasury stock method. As of September 30, 2014 and 2013, 1.1 million and 1.2 million unvested shares of restricted common stock, respectively, are not included in the computation of basic income per share, as these shares were not vested. Using the if-converted method, the shares issuable upon conversion of the Company s convertible senior notes (the Convertible Notes) were anti-dilutive for the three and nine months ended September 30, 2013. Accordingly, that impact has been excluded from the computation of diluted loss per share. The Convertible Notes were convertible into 1.9 million shares of the Company s common stock at September 30, 2013. The Convertible Notes were repaid in June 2014 and are no longer outstanding. For the three and nine months ended September 30, 2014 and 2013, the Company s employees exercised options for 7,623, 32,658, 15,839 and 72,802 common shares, respectively.

The following details the determination of diluted weighted average shares:

	Nine Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2013
Weighted average common shares - basic	46,111,192	46,171,194	46,145,642
Dilutive effect of stock options	62,998	70,557	76,632
Dilutive effect of restricted stock	352,333	581,416	682,880
Weighted average common shares - diluted	46,526,523	46,823,167	46,905,154

Recent Accounting Pronouncements

On May 28, 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

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In July 2013, the FASB issued ASU 2013-11, *Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*. Prior to the issuance of ASU 2013-11 there was no explicit guidance on the presentation of unrecognized tax benefits when such carryforwards exist. ASU 2013-11 requires entities to present an unrecognized tax benefit as a reduction of a deferred tax asset for a net operating loss (NOL) carryforward whenever the NOL or tax credit carryforward would be available to reduce the additional taxable income or tax due if the tax position was disallowed. The ASU was effective for fiscal years beginning after December 15, 2013, and interim periods within those years. The adoption of this guidance did not have any effect on our consolidated financial statements.

2. Property and equipment:

Depreciation and amortization expense related to property and equipment and capital leases was $17.4 million $51.9 million, $16.0 million and $47.8 million for the three and nine months ended September 30, 2014 and 2013, respectively. The Company capitalized salaries and related benefits of employees working directly on the construction and build-out of its network of $2.0 million, $5.9 million, $1.8 million and $5.6 million for the three and nine months ended September 30, 2014 and 2013, respectively.

In the nine months ended September 30, 2014, the Company exchanged certain used network equipment for new network equipment and cash consideration. The fair value of the equipment received was estimated to be $16.8 million resulting in gains of $8.0 million. The estimated fair value of the equipment received was based upon the cash consideration price the Company pays for the new network equipment on a standalone basis (level 3).

3. Long-term debt:

Senior unsecured notes

On April 9, 2014, Cogent Communications Finance, Inc. (Cogent Finance), a newly formed financing subsidiary of Group, completed an offering of $200.0 million in aggregate principal amount at par of 5.625% Senior Notes due 2021 (the 2021 Notes). The 2021 Notes were sold in private offerings for resale to qualified institutional buyers pursuant to SEC Rule 144A. The offering closed into escrow pursuant to an escrow agreement, dated as of April 9, 2014 (the Escrow Agreement). The term Issuer refers to Cogent Finance prior to the release of the funds from the escrow account (such date of release, the Escrow Release Date) and to Group after the Escrow Release Date. As a condition to releasing the funds from escrow the Company redeemed its remaining outstanding Convertible Notes on June 20, 2014 (the Redemption Transaction). After consummation of the Redemption Transaction, Cogent Finance merged with Group, with Group continuing as the surviving corporation (the Finance Merger). At the time of consummation of the Finance Merger, Group assumed the obligations of Cogent Finance under the 2021 Notes and the indenture governing the 2021 Notes (the Indenture) and Group and each of Group s domestic subsidiaries became party to the Indenture pursuant to a supplemental indenture to the Indenture and the obligations under the Indenture became obligations solely of Group and each of Group s domestic subsidiaries. Holdings also provided a guarantee of the 2021 Notes but Holdings is not subject to any of the covenants under the Indenture. After the conditions to the release of the escrow proceeds were satisfied, on June 25, 2014 (the Escrow Release Date) the proceeds from the 2021 Notes were released. The net proceeds from the offering were $195.8 million after deducting discounts and commissions and offering expenses. Issuance costs are included in deposits and other assets. The net proceeds from the offering are intended to be used for general corporate purposes.

The 2021 Notes were issued pursuant to, and are governed by the Indenture between Cogent Finance and the trustee. The 2021 Notes bear interest at a rate of 5.625% per year and will mature on April 15, 2021. Interest began to accrue on the 2021 Notes on April 9, 2014 and will be paid semi-annually on April 15 and October 15, commencing on October 15, 2014. Following the Escrow Release Date, the 2021 Notes became Group s senior unsecured obligations and are guaranteed on a senior unsecured basis by the Company. The 2021 Notes are effectively subordinated in right of payment to all of Group s and each guarantor s secured indebtedness, including the Group s existing $240.0 million of senior secured notes and future secured indebtedness, if any, to the extent of the value of the assets securing such indebtedness. The 2021 Notes are equal in right of payment with Group s and each guarantor s unsecured indebtedness that is not subordinated in right of payment to the 2021 Notes. The 2021 Notes will rank senior in right of payment to Group s and each guarantor s future subordinated debt, if any; and will be structurally subordinated in right of payment to all indebtedness and other liabilities of any of the Group s subsidiaries that are not guarantors, which will only consist of immaterial subsidiaries and foreign subsidiaries that do not guarantee other indebtedness of Group.

The Company may redeem the 2021 Notes, in whole or in part, at any time prior to April 15, 2017 at a price equal to 100% of the principal amount plus an applicable premium, plus accrued and unpaid interest, if any, to the date of redemption. The applicable premium means, with respect to a note at any date of redemption, the greater of (i) 1.0% of the then-outstanding principal amount of such note and (ii) the excess of (A) the present value at such date of redemption of (1) the redemption price of 104.219% plus (2) all remaining required interest payments due on such note through April 15, 2017 (excluding accrued but unpaid interest to the date of redemption), computed using a discount rate equal to the Treasury Rate as of such date of redemption plus 50 basis points, over (B) the then-outstanding principal amount of such note. The Company may also redeem the 2021 Notes, in whole or in part, at any time on or after April 15, 2017 at the applicable redemption prices specified under the indenture governing the 2021 Notes plus accrued and unpaid interest, if any, to the date of redemption. The redemption prices (expressed as a percentage of the principal amount) are 104.219% during the 12-month period beginning on April 15, 2017, 102.813% during the 12-month period beginning on April 15, 2018, 101.406% during the 12-month period beginning on April 15, 2019 and 100.0% during the 12-month period beginning on April 15, 2020 and thereafter. In addition, the Company may redeem up to 35% of the 2021 Notes before April 15, 2017 with the net cash proceeds from certain equity offerings at a redemption price of 105.625% of the principal amount plus accrued and unpaid interest. If the Company experiences specific kinds of changes of control, the Company must offer to repurchase all of the 2021 Notes at a purchase price of 101.0% of their principal amount, plus accrued and unpaid interest, if any, to the repurchase date.

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The indenture governing the 2021 Notes, among other things, limits the Company s ability to incur indebtedness; to pay dividends or make other distributions; to make certain investments and other restricted payments; to create liens; consolidate, merge, sell or otherwise dispose of all or substantially all of its assets; to incur restrictions on the ability of a subsidiary to pay dividends or make other payments; and to enter into certain transactions with its affiliates. Limitations on the ability to incur additional indebtedness (excluding IRU agreements incurred in the normal course of business) include a restriction on incurring additional indebtedness if the Company s consolidated leverage ratio, as defined in the Indenture is greater than 5.0. Permitted investments and payments that are not restricted include an amount of up to $150.0 million. This amount may be increased by the Company s consolidated cash flow, as defined in the Indenture as long as the Company s consolidated leverage ratio is less than 4.25. Holdings had cash and cash equivalents totaling $80.0 million as of September 30, 2014 which are not subject to these limitations.

Senior secured notes

On January 26, 2011 and on August 19, 2013, the Company issued its 8.375% Senior Secured Notes (the Senior Notes) due February 15, 2018, for aggregate principal amounts of $175.0 million and $65.0 million, respectively, in private offerings for resale to qualified institutional buyers pursuant to SEC Rule 144A. The Senior Notes are secured and bear interest at 8.375% per annum. Interest is payable in cash semiannually in arrears on February 15 and August 15, of each year. On January 26, 2011, the Company received net proceeds of $170.5 million after deducting $4.5 million of issuance costs from issuing $175.0 million of Senior Notes. On August 19, 2013, the Company received net proceeds of approximately $69.9 million after deducting $1.0 million of issuance costs from issuing $65.0 million of Senior Notes. The Senior Notes sold in August 2013 were sold at 109.00% of par value. The resulting $5.9 million premium is being amortized as a reduction to interest expense to the maturity date using the effective interest rate method. Issuance costs are included in deposits and other assets.

Convertible senior notes

In June 2007, the Company issued its Convertible Notes for an aggregate principal amount of $200.0 million in a private offering for resale to qualified institutional buyers pursuant to SEC Rule 144A. The Convertible Notes were scheduled to mature on June 15, 2027, were unsecured, and bore interest at 1.00% per annum. Interest was payable in cash semiannually in arrears on June 15 and December 15, of each year, beginning on December 15, 2007. The Company received net proceeds from the issuance of the Convertible Notes of approximately $195.1 million, after deducting the original issue discount of 2.25% and issuance costs. The discount and other issuance costs were being amortized to interest expense using the effective interest method through June 15, 2014, which was the earliest put date. In 2008, the Company purchased an aggregate of $108.0 million of face value of the Convertible Notes for $48.6 million in cash in a series of transactions resulting in $92.0 million of principal amount of the Convertible Notes remaining after these purchase transactions.

Holders of the Convertible Notes had the right to require the Company to repurchase for cash all or some of their notes on June 15, 2014, 2017 and 2022 at a redemption price of 100% of the principal amount plus accrued interest. Holders of $58.5 million of principal amount of the Convertible Notes issued a repurchase notice to the Company and on June 16, 2014 the Company repaid $58.5 million of Convertible Notes principal amount plus accrued interest. The Convertible Notes may have been redeemed by the Company at any time on and after June 20, 2014 at a redemption price of 100% of the principal amount plus accrued interest. On June 20, 2014 the Company redeemed the remaining $33.5 million principal amount of the Convertible Notes.

The debt and equity components for the Convertible Notes and of December 31, 2013 were as follows (in thousands):

	December 31, 2013
Principal amount	$ 91,978
Unamortized discount	(3,099)
Net carrying amount	88,879
Additional paid-in capital	74,933

The amount of interest expense recognized and effective interest rate for the Convertible Notes were as follows (in thousands):

	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Contractual coupon interest	$ 230	$ 419	$ 690
Amortization of discount and costs on Notes	1,619	3,106	4,755
Interest expense	$ 1,849	$ 3,525	$ 5,445
Effective interest rate	8.7%	8.7%	8.7%

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4. Commitments and contingencies:

Current and potential litigation

In accordance with the accounting guidance for contingencies, the Company accrues its estimate of a contingent liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Where it is probable that a liability has been incurred and there is a range of expected loss for which no amount in the range is more likely than any other amount, the Company accrues at the low end of the range. The Company reviews its accruals at least quarterly and adjusts them to reflect the impact of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular matter. The Company has taken certain positions related to its obligations for leased circuit and dark fiber obligations for which it is reasonably possible could result in a loss of up to $2.0 million in excess of the amount accrued at September 30, 2014.

Certain former sales employees of the Company filed a collective action against the Company in December 2011 in the United States District Court, Southern District of Texas, Houston Division alleging misclassification of the Company s sales employees throughout the U.S. in violation of the Fair Labor Standards Act. The lawsuit seeks to recover pay for allegedly unpaid overtime and other damages, including attorney s fees. In March 2014, the judge de-certified the collective action. Each of the former employees that opted-in to the collective action retains the right to file an individual action. Approximately 70 former employees have done so. In several of the jurisdictions in which the lawsuits have been filed the plaintiffs seek certification of a collective action related to the employees in that jurisdiction. The Company denies the claims and believes that the claims for unpaid overtime are without merit. The Company believes its classification of sales employees is in compliance with applicable law.

In the normal course of business the Company is involved in other legal activities and claims. Because such matters are subject to many uncertainties and the outcomes are not predictable with assurance, the liability related to these legal actions and claims cannot be determined with certainty. Management does not believe that such claims and actions will have a material impact on the Company s financial condition or results of operations. Judgment is required in estimating the ultimate outcome of any dispute resolution process, as well as any other amounts that may be incurred to conclude the negotiations or settle any litigation. Actual results may differ from these estimates under different assumptions or conditions and such differences could be material.

5. Income taxes:

The effective income tax rates for the three and nine months ended September 30, 2014 and 2013 are different from the U.S. federal income tax statutory rate of 35.0% primarily due to the impact of discrete expenses. Since the Company is near breakeven these discrete items result in a significant impact on the effective income tax rate during the period. Additional deviation from the U.S. federal income tax statutory rate are due to permanent differences resulting from non-deductible equity-based compensation expense and from the impact of state taxes and foreign losses that have not met the criteria for recording as an income tax benefit. The components of income (loss) before income taxes consist of the following (in thousands):

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013

Domestic	$	7,874	$	8,011
Foreign		(6,782)		(5,710)
Total	$	1,092	$	2,301

		Nine Months Ended September 30, 2014		Nine Months Ended September 30, 2013
Domestic	$	23,888	$	22,150
Foreign		(20,268)		(17,181)
Total	$	3,620	$	4,969

6. Common stock buyback program:

The Company s board of directors has approved through February 29, 2016, purchases of the Company s common stock under a buyback program (the Buyback Program). At September 30, 2014, there was approximately $47.7 million remaining for purchases under the Buyback Program. During the three and nine months ended September 30, 2014, the Company purchased 475,803 shares and 1,402,691 shares of its common stock for $15.9 million and $48.0 million, respectively. There were no purchases made during the nine months ended September 30, 2013.

7. Dividends on common stock:

Dividends are recorded as a reduction to retained earnings. Dividends on unvested restricted shares of common stock are paid as the awards vest. The Company s initial quarterly dividend payment was made in the third quarter of 2012. In addition to the Company s regular quarterly dividends, in 2013, the Company s board of directors approved an additional return of capital program (the Capital Program). Under the Capital Program the Company plans on returning additional capital to the Company s shareholders each quarter through either stock buybacks or a special dividend or a combination of stock buybacks and a special dividend. The aggregate payment under the Capital Program initially was a minimum of $10.0 million each quarter and was increased to be a minimum of $10.5 million each quarter. Amounts paid under the Capital Program are in addition to the Company s regular quarterly dividend payments. The initial $10.0 million ($0.22 per share) quarterly dividend payment under the

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Capital Program was paid on December 20, 2013. The Company bought $14.2 million, $17.9 million and $15.9 million of its stock in the first, second and third quarters of 2014, respectively, which were greater than the minimum quarterly amount under the Capital Program; as a result, special dividends under the Capital Program are not included with the second, third and fourth quarter 2014 dividend payments.

On November 3, 2014, the Company s board of directors approved the payment of the Company s regular quarterly dividend of $0.31 per common share and an increase to the minimum quarterly amount under the Capital Program to $12.0 million. The dividend for the fourth quarter of 2014 will be paid to holders of record on November 26, 2014. This estimated $14.1 million dividend payment is expected to be made on December 12, 2014.

A summary of the Company s quarterly dividends paid since its initial dividend payment is as follows (in thousands, except per share amounts):

Dividend Period	Amount per Common Share	Record Date	Payment Date	Dividends Paid
Q3 2012	$ 0.10	August 22, 2012	September 12, 2012	$ 4,537
Q4 2012	$ 0.11	November 21, 2012	December 12, 2102	$ 5,012
Q1 2013	$ 0.12	March 4, 2013	March 15, 2013	$ 5,489
Q2 2013	$ 0.13	May 31, 2013	June 18, 2013	$ 6,145
Q3 2013	$ 0.14	September 5, 2013	September 25, 2013	$ 6,512
Q4 2013	$ 0.37	November 27, 2013	December 20, 2013	$ 17,206
Q1 2014	$ 0.39	March 7, 2014	March 27, 2014	$ 18,352
Q2 2014	$ 0.17	May 30, 2014	June 18, 2014	$ 7,882
Q3 2014	$ 0.30	August 29, 2014	September 19, 2014	$ 13,792

The payment of any future dividends and any other returns of capital will be at the discretion of the Company s board of directors and may be reduced, eliminated or increased and will be dependent upon the Company s financial position, results of operations, available cash, cash flow, capital requirements and other factors deemed relevant by the Company s board of directors.

8. Related party transactions:

Office lease

The Company s headquarters is located in an office building owned by Niobium LLC (a successor to 6715 Kenilworth Avenue Partnership). The two owners of the company are the Company s Chief Executive Officer, David Schaeffer, who has a 51% interest in the partnership and his wife who has a 49% interest. The Company paid $0.2 million and $0.4 million in the three and nine months ended September 30, 2014 and paid $0.2 million and $0.5 million in the three and nine months ended September 30, 2013, for rent and related costs (including taxes and utilities) to this company, respectively. The lease ends on August 31, 2016.

9. Segment information:

The Company operates as one operating segment. The Company s service revenue and long lived assets by geographic region are as follows (in thousands):

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
Revenues				
North America	$ 76,089	$ 69,327	$ 223,701	$ 203,923
Europe	19,602	18,434	59,551	54,195
Total	$ 95,691	$ 87,761	$ 283,252	$ 258,118

	September 30, 2014	December 31, 2013
Long lived assets, net		
North America	$ 265,850	$ 251,352
Europe	91,885	89,879
Total	$ 357,735	$ 341,231

The majority of North American revenue consists of services delivered within the United States.

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ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis together with our condensed consolidated financial statements and related notes included in this report. The discussion in this report contains forward-looking statements that involve risks and uncertainties, such as statements of our plans, objectives, expectations and intentions. The cautionary statements made in this report should be read as applying to all related forward-looking statements wherever they appear in this report. Our actual results could differ materially from those discussed here. Factors that could cause or contribute to these differences include, but are not limited to:

Future economic instability in the global economy, which could affect spending on Internet services; the impact of changing foreign exchange rates (in particular the Euro to US dollar and Canadian dollar to US dollar exchange rates) on the translation of our non-US dollar denominated revenues, expenses, assets and liabilities; legal and operational difficulties in new markets; the imposition of a requirement that we contribute to the US Universal Service Fund; changes in government policy and/or regulation, including rules regarding data protection and cyber security; increasing competition leading to lower prices for our services; our ability to attract new customers and to increase and maintain the volume of traffic on our network; the ability to maintain our Internet peering arrangements on favorable terms; our reliance on an equipment vendor, Cisco Systems Inc., and the potential for hardware or software problems associated with such equipment; the dependence of our network on the quality and dependability of third-party fiber providers; our ability to retain certain customers that comprise a significant portion of our revenue base; the management of network failures and/or disruptions; and outcomes in litigation as well as other risks discussed from time to time in our filings with the Securities and Exchange Commission, including, without limitation, our annual report on Form 10-K for the fiscal year ended December 31, 2013.

General Overview

We are a leading facilities-based provider of low-cost, high-speed Internet access and IP communications services. Our network is specifically designed and optimized to transmit data using IP. We deliver our services primarily to small and medium-sized businesses, communications service providers and other bandwidth-intensive organizations in North America, Europe and in Japan.

Our on-net service consists of high-speed Internet access and IP connectivity ranging from 100 Megabits per second to 100 Gigabits per second of bandwidth. We offer our on-net services to customers located in buildings that are physically connected to our network. We provide on-net Internet access to net-centric and corporate customers. Our net-centric customers include bandwidth-intensive users such as universities, other Internet service providers, telephone companies, cable television companies, web hosting companies, content delivery networks and commercial content and application service providers. These net-centric customers generally receive our services in colocation facilities and in our data centers. Our corporate customers are located in multi-tenant office buildings and typically include law firms, financial services firms, advertising and marketing firms and other professional services businesses.

Our off-net services are sold to businesses that are connected to our network primarily by means of last mile access service lines obtained from other carriers, primarily in the form of point-to-point, Carrier Ethernet, TDM, POS, and/or SDH circuits. Our non-core services, which consist primarily of legacy services of companies whose assets or businesses we have acquired, primarily include voice services (only provided in Toronto, Canada). We do not actively market these non-core services and expect the service revenue associated with them to continue to decline.

Our network is comprised of in-building riser facilities, metropolitan optical fiber networks, metropolitan traffic aggregation points and inter-city transport facilities. Our network is physically connected entirely through our facilities to 2,090 buildings in which we provide our on-net services, including 1,440 multi-tenant office buildings. We also provide on-net services in carrier-neutral colocation facilities, Cogent controlled data centers and single-tenant office buildings. We operate 49 Cogent controlled data centers totaling 550,000 square feet. Because of our integrated network architecture, we are not dependent on local telephone companies to serve our on-net customers. We emphasize the sale of our on-net services because we believe we have a competitive advantage in providing these services and these services generate gross profit margins that are greater than the gross profit margins of our off-net services.

We believe our key growth opportunity is provided by our high-capacity network, which provides us with the ability to add a significant number of customers to our network with minimal direct incremental costs. Our focus is to add customers to our network in a way that maximizes its use and at the same time provides us with a profitable customer mix. We are responding to this opportunity by increasing our sales and marketing efforts including increasing our number of sales representatives and expanding our network to locations that we believe can be economically integrated and represent significant concentrations of Internet traffic. One of our keys to developing a profitable business will be to carefully match the cost of extending our network to reach new customers with the revenue expected to be generated by those customers. In addition, we may add customers to our network through strategic acquisitions.

We believe some of the most important trends in our industry are the continued long-term growth in Internet traffic and a decline in Internet access prices on a per megabit basis. The effective price per megabit for our corporate customers is declining as the bandwidth utilization and connection size of our corporate customer connections increases. As Internet traffic continues to grow and prices per unit of traffic continue to decline, we believe we can continue to load our network and gain market share from less efficient network operators. However, continued erosion in Internet access prices will likely have a negative impact on the rate at which we can increase our revenues and our profitability. Our revenue may also be negatively affected if we are unable to grow our Internet traffic or if the rate of growth of Internet traffic does not offset our expected decline in per unit pricing. We do not know if Internet traffic will increase or decrease, or the rate at which it will increase or decrease. Changes in

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Internet traffic will be a function of the number of users, the amount of time users spend on the Internet, the applications for which the Internet is used, the bandwidth intensity of these applications and the pricing of Internet services, and other factors.

The growth in Internet traffic has a more significant impact on our net-centric customers who represent the majority of the traffic on our network and who tend to consume the majority of their allocated bandwidth on their connections. Net-centric customers tend to purchase their service on a price per megabit basis. Our corporate customers tend to utilize a small portion of their allocated bandwidth on their connections and tend to purchase their service on a per connection basis.

We are a facilities-based provider of Internet access and communications services. Facilities-based providers require significant physical assets, or network facilities, to provide their services. Typically when a facilities-based network services provider begins providing its services in a new jurisdiction losses are incurred for several years until economies of scale have been achieved. Our foreign operations are in Europe, Canada, Mexico and Japan. Europe accounts for roughly 80% of our foreign operations. Our European operations have incurred losses and will continue to do so until our European customer base and revenues have grown sufficiently to achieve economies of scale.

Due to our strategic acquisitions of network assets and equipment, we believe we are well positioned to grow our revenue base. We continue to purchase and deploy network equipment to parts of our network to maximize the utilization of our assets and to expand and increase the capacity of our network. Our future capital expenditures will be based primarily on the expansion of our network and the addition of on-net buildings. We plan to continue to expand our network and to increase the number of on-net buildings we serve including multi-tenant office buildings and carrier neutral data centers. Many factors can affect our ability to add buildings to our network. These factors include the willingness of building owners to grant us access rights, the availability of optical fiber networks to serve those buildings, the cost to connect buildings to our network and equipment availability.

Three Months Ended September 30, 2014 Compared to the Three Months Ended September 30, 2013

The following summary table presents a comparison of our results of operations with respect to certain key financial measures. The comparisons illustrated in the table are discussed in greater detail below.

	Three months ended September 30,		Percent Change
	2014	2013	
	(in thousands)		
Service revenue	$ 95,691	$ 87,761	9.0%
On-net revenue	71,059	64,548	10.1%
Off-net revenue	24,330	22,767	6.9%
Non-core revenue	302	446	(32.3)%
Network operations expenses (1)	40,407	37,441	7.9%
Selling, general, and administrative expenses (2)	27,353	21,719	25.9%
Depreciation and amortization expenses	17,431	16,024	8.8%
Gain on equipment transaction	3,114		NM
Interest expense	12,662	10,568	19.8%
Income tax provision	1,276	179	NM

(1) Includes equity-based compensation expenses of $114 and $114 in the three months ended September 30, 2014 and 2013, respectively.

(2) Includes equity-based compensation expenses of $2,578 and $1,947 in the three months ended September 30, 2014 and 2013, respectively.

NM not meaningful

	Three Months Ended September 30,				Percent Change
	2014		2013		
Other Operating Data					
Average Revenue Per Unit (ARPU)					
ARPU on net	$	624	$	660	(5.5)%
ARPU off-net	$	1,451	$	1,579	(8.1)%
Average Price per Megabit installed base	$	1.93	$	2.52	(23.4)%
Customer Connections end of period					
On-net		38,559		33,310	15.8%
Off-net		5,694		4,886	16.5%
Non-core		377		443	(14.9)%

Service Revenue. Our service revenue increased 9.0% for the three months ended September 30, 2014 from the three months ended September 30, 2013. The impact of exchange rates resulted in a decrease of revenues for the three months ended September 30, 2014 of approximately $0.2 million. All foreign currency comparisons herein reflect our third quarter 2014 results translated at the average foreign

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currency exchange rates for the third quarter of 2013. For the three months ended September 30, 2014 and 2013, on-net, off-net and non-core revenues represented 74.3%, 25.4% and 0.3% and 73.6%, 25.9% and 0.5% of our service revenue, respectively.

Revenues from our corporate and net centric customers represented 53.5% and 46.5% of total service revenue, respectively, for the three months ended September 30, 2014 and represented 52.2% and 47.8% of total service revenue, respectively, for the three months ended September 30, 2013. Revenues from corporate customers increased 11.8% to $51.2 million for the three months ended September 30, 2014 from $45.8 million for the three months ended September 30, 2013. Revenues from our net-centric customers increased 6.1% to $44.5 million for the three months ended September 30, 2014 from $41.9 million for the three months ended September 30, 2013.

Our on-net revenues increased 10.1% for the three months ended September 30, 2014 from the three months ended September 30, 2013. We increased the number of our on-net customer connections by 15.8% at September 30, 2014 from September 30, 2013. On-net customer connections increased at a greater rate than on-net revenues primarily due to the 5.5% decline in our on-net ARPU, primarily from a decline in ARPU for our net centric customers. ARPU is determined by dividing revenue for the period by the average customer connections for that period. Our average price per megabit for our installed base of customers is determined by dividing the aggregate monthly recurring fixed charges for those customers by the aggregate committed data rate for the same customers. The decline in on-net ARPU is partly attributed to volume and term based pricing discounts. Additionally, on-net customers who cancel their service from our installed base of customers, in general, have an ARPU that is greater than the ARPU for our new customers due to declining prices primarily for our on-net services sold to our net-centric customers. These trends resulted in the reduction to our on-net ARPU and a 23.4% decline in our average price per megabit for our installed base of customers.

Our off-net revenues increased 6.9% for the three months ended September 30, 2014 from the three months ended September 30, 2013. Our off-net revenues increased as we increased the number of our off-net customer connections by 16.5% at September 30, 2014 from September 30, 2013. Our off-net customer connections increased at a greater rate than our off-net revenue primarily due to the 8.1% decrease in our off-net ARPU.

Our non-core revenues decreased 32.3% for the three months ended September 30, 2014 from the three months ended September 30, 2013. The number of our non-core customer connections decreased 14.9% at September 30, 2014 from September 30, 2013. We do not actively market these acquired non-core services and expect that the service revenue associated with them will continue to decline.

Network Operations Expenses. Network operations expenses include the costs of personnel associated with service delivery, network management and customer support, network facilities costs, fiber and equipment maintenance fees, leased circuit costs, and access and facilities fees paid to building owners. Non-cash equity-based compensation expense is included in network operations expenses consistent with the classification of the employee s salary and other compensation. Our network operations expenses, including non-cash equity-based compensation expense, increased 7.9% for the three months ended September 30, 2014 from the three months ended September 30, 2013. The increase is primarily attributable to an increase in costs related to our network and facilities expansion activities and the increase in our off-net revenues. When we provide off-net services we also assume the cost of the associated tail-circuits.

Selling, General, and Administrative (SG&A) Expenses. Our SG&A expenses, including non-cash equity-based compensation expense, increased 25.9% for the three months ended September 30, 2014 from the three months ended September 30, 2013. Non-cash equity-based compensation expense is included in SG&A expenses consistent with the classification of the employee s salary and other compensation and was $2.6 million for the three months ended September 30, 2014 and $1.9 million for the three months ended September 30, 2013. SG&A expenses increased primarily from an increase in salaries and related costs required to support our expansion and the increase in our sales efforts and a

$1.8 million increase in our legal fees primarily associated with regulatory matters. Our sales force headcount increased by 16.8% from September 30, 2013 to 452 at September 30, 2014.

Depreciation and Amortization Expenses. Our depreciation and amortization expense increased 8.8% for the three months ended September 30, 2014 from the three months ended September 30, 2013. The increase is primarily due to the depreciation expense associated with the increase in deployed fixed assets.

Gain on Equipment Transaction. In the three months ended September 30, 2014, we exchanged certain used network equipment for new network equipment and cash consideration resulting in gains of $3.1 million based upon the estimated fair value of the new network equipment less the carrying amount of the returned used network equipment and the cash paid.

Interest Expense. Interest expense results from interest incurred on our $200.0 million of senior unsecured notes that we issued on April 9, 2014, our $65.0 million of senior secured notes that we issued on August 19, 2013, our $175.0 million of senior secured notes that we issued on January 26, 2011, our $92.0 million of convertible senior notes that we issued in June 2007, and interest on our capital lease obligations. Our interest expense increased 19.8% for the three months ended September 30, 2014 from the three months ended September 30, 2013. The increase is attributed to approximately $2.9 million of interest expense related to the issuance of our $200.0 million of senior unsecured notes outstanding since April 9, 2014 and $0.6 million of interest expense related to the issuance of our $65.0 million of Senior Secured Notes outstanding since August 19, 2013, partly offset by the decline of $1.8 million of interest expense from our convertible notes that we repaid in June 2014.

Income Tax Provision. Our income tax provision was $1.3 million for the three months ended September 30, 2014 and $0.2 million for the three months ended September 30, 2013. The effective income tax rates are different from the U.S. federal income tax statutory rate of 35.0% primarily due to the impact of discrete expenses. Since we are near breakeven these discrete items result in a significant impact on the effective

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income tax rate during the period. Additional deviation from the U.S. federal income tax statutory rate are due to permanent differences resulting from non-deductible equity-based compensation expense and from the impact of state taxes and foreign losses that have not met the criteria for recording as an income tax benefit.

Buildings On-net. As of September 30, 2014 and 2013, we had a total of 2,090 and 1,955 on-net buildings connected to our network, respectively.

Nine Months Ended September 30, 2014 Compared to the Nine Months Ended September 30, 2013

The following summary table presents a comparison of our results of operations with respect to certain key financial measures. The comparisons illustrated in the table are discussed in greater detail below.

	Nine months ended September 30,		
	2014	2013	Percent Change
	(in thousands)		
Service revenue	$ 283,252	$ 258,118	9.7%
On-net revenue	210,557	188,919	11.5%
Off-net revenue	71,687	67,681	5.9%
Non-core revenue	1,008	1,518	(33.6)%
Network operations expenses (1)	118,848	111,825	6.3%
Selling, general, and administrative expenses (2)	79,775	64,410	23.9%
Depreciation and amortization expenses	51,937	47,798	8.7%
Gains on equipment transactions	8,140		NM
Interest expense	37,756	30,653	23.2%
Income tax provision	2,471	879	NM%

(1) Includes equity-based compensation expenses of $341 and $395 in the nine months ended September 30, 2014 and 2013, respectively.

(2) Includes equity-based compensation expenses of $6,229 and $6,317 in the nine months ended September 30, 2014 and 2013, respectively.

NM not meaningful

	Nine Months Ended September 30,		
	2014	2013	Percent Change
Other Operating Data			
Average Revenue Per Unit (ARPU)			
ARPU on net	$ 639	$ 664	(3.8)%
ARPU off-net	$ 1,478	$ 1,608	(8.1)%
Average Price per Megabit installed base	$ 2.04	$ 2.70	(24.4)%
Customer Connections end of period			
On-net	38,559	33,310	15.8%

Off-net	5,694	4,886	16.5%
Non-core	377	443	(14.9)%

Service Revenue. Our service revenue increased 9.7% for the nine months ended September 30, 2014 from the nine months ended September 30, 2013. The impact of exchange rates resulted in an increase of revenues for the nine months ended September 30, 2014 of approximately $0.7 million. All foreign currency comparisons herein reflect our results for the nine months ended September 30, 2014 translated at the average foreign currency exchange rates for the nine months ended September 30, 2013. For the nine months ended September 30, 2014 and 2013, on-net, off-net and non-core revenues represented 74.3%, 25.3% and 0.4% and 73.2%, 26.2% and 0.6% of our service revenue, respectively.

Revenues from our corporate and net centric customers represented 52.5% and 47.5% of total service revenue, respectively, for the nine months ended September 30, 2014 and represented 51.6% and 48.4% of total service revenue, respectively, for the nine months ended September 30, 2013. Revenues from corporate customers increased 11.6% to $148.6 million for the nine months ended September 30, 2014 from $133.2 million for the nine months ended September 30, 2013. Revenues from our net-centric customers increased 7.8% to $134.6 million for the nine months ended September 30, 2014 from $124.9 million for the nine months ended September 30, 2013.

Our on-net revenues increased 11.5% for the nine months ended September 30, 2014 from the nine months ended September 30, 2013. We increased the number of our on-net customer connections by 15.8% at September 30, 2014 from September 30, 2013. On-net customer connections increased at a greater rate than on-net revenues primarily due to a 3.8% decline in our on-net ARPU, primarily from a decline in ARPU for our net-centric customers. ARPU is determined by dividing revenue for the period by the average customer connections for that period. Our average price per megabit for our installed base of customers is determined by dividing the aggregate monthly recurring fixed charges for those customers by the aggregate committed data rate for the same customers. The decline in on-net ARPU is partly attributed to volume and term based pricing discounts. Additionally, on-net customers who cancel their service from our installed base of customers, in general, have an ARPU

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that is greater than the ARPU for our new customers due to declining prices primarily for our on-net services sold to our net-centric customers. These trends resulted in the reduction to our on-net ARPU and a 24.4% decline in our average price per megabit for our installed base of customers.

Our off-net revenues increased 5.9% for the nine months ended September 30, 2014 from the nine months ended September 30, 2013. Our off-net revenues increased as we increased the number of our off-net customer connections by 16.5% at September 30, 2014 from September 30, 2013. Our off-net customer connections increased at a greater rate than our off-net revenue primarily due to the 8.1% decrease in our off-net ARPU.

Our non-core revenues decreased 33.6% for the nine months ended September 30, 2014 from the nine months ended September 30, 2013. The number of our non-core customer connections decreased 14.9% September 30, 2014 from September 30, 2013. We do not actively market these acquired non-core services and expect that the service revenue associated with them will continue to decline.

Network Operations Expenses. Network operations expenses include the costs of personnel associated with service delivery, network management and customer support, network facilities costs, fiber and equipment maintenance fees, leased circuit costs, and access and facilities fees paid to building owners. Non-cash equity-based compensation expense is included in network operations expenses consistent with the classification of the employee s salary and other compensation. Our network operations expenses, including non-cash equity-based compensation expense, increased 6.3% for the nine months ended September 30, 2014 from the nine months ended September 30, 2013. The increase is primarily attributable to an increase in costs related to our network and facilities expansion activities and the increase in our off-net revenues. When we provide off-net services we also assume the cost of the associated tail-circuits.

Selling, General, and Administrative (SG&A) Expenses. Our SG&A expenses, including non-cash equity-based compensation expense, increased 23.9% for the nine months ended September 30, 2014 from the nine months ended September 30, 2013. Non-cash equity-based compensation expense is included in SG&A expenses consistent with the classification of the employee s salary and other compensation and was $6.2 million for the nine months ended September 30, 2014 and $6.3 million for the nine months ended September 30, 2013. SG&A expenses increased primarily from an increase in salaries and related costs required to support our expansion and an increase in our sales efforts and a $3.8 million increase in our legal fees primarily associated with regulatory matters. Our sales force headcount increased by 16.8% from September 30, 2013 to 452 at September 30, 2014.

Depreciation and Amortization Expenses. Our depreciation and amortization expense increased 8.7% for the nine months ended September 30, 2014 from the nine months ended September 30, 2013. The increase is primarily due to the depreciation expense associated with the increase in deployed fixed assets.

Gains on Equipment Transactions. In the nine months ended September 30, 2014, we exchanged certain used network equipment for new network equipment and cash consideration resulting in gains of $8.1 million based upon the estimated fair value of the new network equipment less the carrying amount of the returned used network equipment and the cash paid.

Interest Expense. Interest expense results from interest incurred on our $200.0 million of senior unsecured notes that we issued on April 9, 2014, our $65.0 million of senior secured notes that we issued on August 19, 2013, our $175.0 million of senior secured notes that we issued on

January 26, 2011, our $92.0 million of convertible senior notes that we issued in June 2007, and interest on our capital lease obligations. Our interest expense increased 23.2% for the nine months ended September 30, 2014 from the nine months ended September 30, 2013. The increase is attributed to $5.6 million of interest expense related to the issuance of our $200.0 million of senior unsecured notes outstanding since April 9, 2014 and $2.8 million of interest expense related to the issuance of our $65.0 million of Senior Secured Notes outstanding since August 19, 2013 partly offset by a reduction of $1.9 million of interest from our convertible notes that we repaid in June 2014.

Income Tax Provision. Our income tax expense was $2.5 million for the nine months ended September 30, 2014 and $0.9 million for the nine months ended September 30, 2013. The effective income tax rates are different from the U.S. federal income tax statutory rate of 35.0% primarily due to the impact of discrete expenses. Since we are near breakeven these discrete items result in a significant impact on the effective income tax rate during the period. Additional deviation from the U.S. federal income tax statutory rate are due to permanent differences resulting from non-deductible equity-based compensation expense and from the impact of state taxes and foreign losses that have not met the criteria for recording as an income tax benefit.

Buildings On-net. As of September 30, 2014 and 2013, we had a total of 2,090 and 1,955 on-net buildings connected to our network, respectively.

Liquidity and Capital Resources

In assessing our liquidity, management reviews and analyzes our current cash balances, accounts receivable, accounts payable, accrued liabilities, capital expenditure commitments, and required capital lease and debt payments and other obligations.

Cash Flows

The following table sets forth our consolidated cash flows.

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(in thousands)	Nine months ended September 30, 2014	2013
Net cash provided by operating activities	$ 55,105	$ 52,563
Net cash used in investing activities	(46,919)	(38,894)
Net cash provided by financing activities	792	43,780
Effect of exchange rates on cash	(2,065)	41
Net increase in cash and cash equivalents during period	$ 6,913	$ 57,490

Net Cash Provided by Operating Activities. Our primary sources of operating cash are receipts from our customers who are billed on a monthly basis for our services. Our primary uses of operating cash are payments made to our vendors, employees and interest payments made to our capital lease vendors and our note holders. Net cash provided by operating activities was $55.1 million for the nine months ended September 30, 2014 compared to net cash provided by operating activities of $52.6 million for the nine months ended September 30, 2013. The change in cash provided by operating activities is primarily due to an increase in our operating income.

Net Cash Used In Investing Activities. Net cash used in investing activities was $46.9 million for the nine months ended September 30, 2014 and $38.9 million for the nine months ended September 30, 2013. Our primary use of cash for investing activities is for purchases of property and equipment. Purchases of property and equipment were $47.0 million and $38.9 million for the nine months ended September 30, 2014 and 2013, respectively. The changes in purchases of property and equipment are primarily due to the timing and scope of our network expansion activities including geographic expansion and adding buildings to our network.

Net Cash Provided By Financing Activities. Net cash provided by financing activities was $0.8 million for the nine months ended September 30, 2014 and was $43.8 million for the nine months ended September 30, 2013. Our primary uses of cash for financing activities are for principal payments under our capital lease obligations, dividend payments, stock purchases and in the nine months ended September 30, 2014 the repayment of our senior convertible notes. In June 2014 we repaid our $92.0 million of senior convertible notes and received net proceeds of $195.8 million from the issuance of our senior unsecured notes. During the nine months ended September 30, 2014 we paid $48.0 million for purchases of our common stock. There were no stock purchases in the nine months ended September 30, 2013. Principal payments under our capital lease were $15.4 million and $8.9 million for the nine months ended September 30, 2014 and 2013, respectively. We began paying a quarterly dividend on our common stock in the third quarter of 2012. During the nine months ended September 30, 2014 and 2013 we paid $40.0 million and $18.1 million, respectively, for our quarterly dividend payments.

Cash Position and Indebtedness

Our total indebtedness at September 30, 2014 was $607.0 million and our total cash and cash equivalents were $311.8 million. Our total indebtedness at September 30, 2014 includes $162.5 million of capital lease obligations for dark fiber under long term IRU agreements.

Summarized Financial Information of Holdings

Holdings is an unrestricted subsidiary as defined under the indenture governing the 2012 Notes and Holdings is also a guarantor under the 2021 Notes. Under the indenture we are required to disclose financial information of Holdings including its assets, liabilities and its operating results (Holdings Financial Information). The Holdings Financial Information as of and for the nine months ended September 30, 2014 is detailed below (in thousands).

		September 30, 2014 (Unaudited)
Cash and cash equivalents	$	80,007
Total assets	$	80,007
Investment from subsidiaries	$	100,216
Common stock		46
Retained deficit		(20,255)
Total equity	$	80,007

		Nine Months Ended September 30, 2014 (Unaudited)
Equity-based compensation expense		3,779
Interest income		7
Net loss	$	(3,772)

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Common Stock Buyback Program

Our board of directors has approved through February 29, 2016, our common stock under a buyback program (the Buyback Program). We purchased approximately 1.4 million shares for $48.0 million during the nine months ended September 30, 2014. There were no purchases of common stock during the nine months ended September 30, 2013. As of September 30, 2014 there was a total of $47.7 million available under the Buyback Program.

Dividends on Common Stock

Our initial quarterly dividend payment was made in the third quarter of 2012. In addition to our regular quarterly dividends, our board of directors has approved our Capital Program as described in Note 7 to our interim condensed consolidated financial statements. Our dividend for the fourth quarter of 2014 of $0.31 per share will be made to holders of record on November 26, 2014. This estimated $14.1 million dividend payment is expected to be paid on December 12, 2014.

The payment of any future dividends and any other returns of capital will be at the discretion of our board of directors and may be reduced, eliminated or increased and will be dependent upon our financial position, results of operations, available cash, cash flow, capital requirements and other factors deemed relevant by our board of directors.

Contractual Obligations and Commitments

There have been no material changes to our contractual obligations and commitments included in Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations of our annual report on Form 10-K for the year ended December 31, 2013, except for the issuance of our $200.0 million of our senior unsecured notes and the $92.0 million repayment of our senior convertible notes as described in Note 3 to our interim condensed consolidated financial statements.

Future Capital Requirements

We believe that our cash on hand and cash generated from our operating activities will be adequate to meet our working capital, capital expenditure, debt service, dividend payments and other cash requirements if we execute our business plan.

Any future acquisitions or other significant unplanned costs or cash requirements in excess of amounts we currently hold may require that we raise additional funds through the issuance of debt or equity. We cannot assure you that such financing will be available on terms acceptable to us or our stockholders, or at all. Insufficient funds may require us to delay or scale back the number of buildings and markets that we add to our network, reduce our planned increase in our sales and marketing efforts, impact our returns to shareholders including our dividends payments

and purchases of our common stock, or require us to otherwise alter our business plan or take other actions that could have a material adverse effect on our business, results of operations and financial condition. If issuing equity securities raises additional funds, substantial dilution to existing stockholders may result.

Off-Balance Sheet Arrangements

We do not have relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. In addition, we do not engage in trading activities involving non-exchange traded contracts. As such, we are not materially exposed to any financing, liquidity, market or credit risks that could arise if we had engaged in these relationships.

Critical Accounting Policies and Significant Estimates

Management believes that as of September 30, 2014, there have been no material changes to our critical accounting policies and significant estimates from those listed in Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations of our annual report on Form 10-K for the year ended December 31, 2013.

Recent Accounting Pronouncements

Recent Accounting Pronouncements to be Adopted

On May 28, 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The new standard is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. We are evaluating the effect that ASU 2014-09 will have on our consolidated financial statements and related disclosures. We have not yet selected a transition method nor have we determined the effect of the standard on our ongoing financial reporting.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Management believes that as of September 30, 2014, there have been no material changes to our exposures to market risk from those disclosed in Item 7A Quantitative and Qualitative Disclosures About Market Risk, of our annual report on Form 10-K for the year ended December 31, 2013.

ITEM 4. CONTROLS AND PROCEDURES.

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As required by SEC Rule 13a-15(b), an evaluation was performed under the supervision and with the participation of our management, including our principal executive officer and our principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this report. Based upon that evaluation, our management, including our principal executive officer and our principal financial officer, concluded that the design and operation of these disclosure controls and procedures were effective at the reasonable assurance level.

There has been no change in our internal control over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are involved in legal proceedings in the normal course of our business that we do not expect to have a material impact on our operations or results of operations. Note 4 of our interim condensed consolidated financial statements includes information on these proceedings.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Our Board of Directors had authorized a plan to permit the repurchase of our common stock in negotiated and open market transactions. We may purchase shares from time to time depending on market, economic, and other factors. The authorization will continue through February 29, 2016.

The following table summarizes our common stock repurchases during the third quarter of 2014 made pursuant to this authorization. During the quarter, we did not purchase shares outside of this program, and all purchases were made by or on behalf of the Company and not by any affiliated purchaser (as defined by Rule 10b-18 of the Securities Exchange Act of 1934).

Issuer Purchases of Equity Securities

Period	Total Number of Shares (or Units) Purchased	Average Price Paid per Share (or (Unit)	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
July 1-31, 2014	130,681	$ 33.82	1,364,509	$ 59,263,063
August 1-31, 2014	147,429	$ 33.03	1,511,938	$ 54,393,674
September 1-30, 2014	197,693	$ 33.66	1,709,631	$ 47,739,529

ITEM 6. EXHIBITS.

(a) Exhibits

Exhibit Number	Description
31.1	Certification of Chief Executive Officer (filed herewith)
31.2	Certification of Chief Financial Officer (filed herewith)
32.1	Certification of Chief Executive Officer (furnished herewith)
32.2	Certification of Chief Financial Officer (furnished herewith)
101.1	The following materials from the Registrant s Quarterly Report on Form 10-Q for the quarter ended September 30, 2014, formatted in Extensible Business Reporting Language (XBRL), include: (i) the Condensed Consolidated Statements of Comprehensive Income, (ii) the Condensed Consolidated Balance Sheets, (iii) the Condensed Consolidated Statements of Cash Flows, and (iv) related notes (filed herewith).

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: November 7, 2014	**COGENT COMMUNICATIONS HOLDINGS, INC.**	
	By:	/s/ David Schaeffer Name: David Schaeffer Title: Chairman of the Board and Chief Executive Officer
Date: November 7, 2014	By:	/s/ Thaddeus G. Weed Name: Thaddeus G. Weed Title: Chief Financial Officer (Principal Accounting Officer)

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Exhibit Index

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