

WESTWOOD ONE INC /DE/

Form 10-Q

November 09, 2006

Table of Contents

**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, 2006
OR**

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

For the transition period from _____ to _____

Commission file number 0-14691

WESTWOOD ONE, INC.

(Exact name of registrant as specified in its charter)

Delaware

**(State or other jurisdiction of
incorporation or organization)**

95-3980449

**(I.R.S. Employer
Identification No.)**

40 West 57th Street, 5th Floor, New York, NY

(Address of principal executive offices)

10019

(Zip Code)

(212) 641-2000

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X
No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act (Check one):
Large Accelerated Filer Accelerated Filer X Non-Accelerated Filer

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

Number of shares of stock outstanding at November 1, 2006 (excluding treasury shares):

Common Stock, par value \$.01 per share 86,270,095 shares

Class B Stock, par value \$.01 per share 291,796 shares

Table of Contents

WESTWOOD ONE, INC.
INDEX

	Page No.
 PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements	
<u>Consolidated Balance Sheets</u>	3
<u>Consolidated Statements of Operations</u>	4
<u>Consolidated Statements of Cash Flows</u>	5
<u>Notes to Consolidated Financial Statements</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	15
<u>Item 3. Qualitative and Quantitative Disclosures About Market Risk</u>	24
<u>Item 4. Controls and Procedures</u>	25
 PART II. OTHER INFORMATION	
II.	
<u>Item 1. Legal Proceedings</u>	26
<u>Item 1A. Risk Factors</u>	26
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	26
<u>Item 3. Defaults Upon Senior Securities</u>	27
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	27
<u>Item 5. Other Information</u>	27
<u>Item 6. Exhibits</u>	27
<u>SIGNATURES</u>	28
<u>Exhibit Index</u>	29
 CERTIFICATIONS	
<u>EX-31.A: CERTIFICATION</u>	
<u>EX-31.B: CERTIFICATION</u>	
<u>EX-32.A: CERTIFICATION</u>	
<u>EX-32.B: CERTIFICATION</u>	

Table of Contents

WESTWOOD ONE, INC.
CONSOLIDATED BALANCE SHEETS
(unaudited)
(In thousands, except share amounts)

	September 30, 2006	December 31, 2005 (Restated)
<u>ASSETS</u>		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 12,205	\$ 10,399
Accounts receivable, net of allowance for doubtful accounts of \$3,684 (2006) and \$2,797 (2005)	107,479	135,184
Prepaid and other assets	25,222	26,662
Total Current Assets	144,906	172,245
PROPERTY AND EQUIPMENT, NET	39,173	41,166
GOODWILL	982,219	982,219
INTANGIBLE ASSETS, NET	4,540	5,007
OTHER ASSETS	28,070	39,009
TOTAL ASSETS	\$ 1,198,908	\$ 1,239,646
<u>LIABILITIES AND SHAREHOLDERS EQUITY</u>		
CURRENT LIABILITIES:		
Accounts payable	\$ 18,756	\$ 15,044
Amounts payable to related parties	18,083	21,192
Deferred revenue	8,480	9,086
Accrued income taxes	1,574	21,861
Accrued expenses and other liabilities	47,852	32,968
Total Current Liabilities	94,745	100,151
LONG-TERM DEBT	406,414	427,514
OTHER LIABILITIES	7,361	7,952
TOTAL LIABILITIES	508,520	535,617
COMMITMENTS AND CONTINGENCIES		
SHAREHOLDERS EQUITY		
Preferred stock: authorized 10,000,000 shares, none outstanding		
Common stock, \$.01 par value: authorized, 252,751,250 shares; issued and outstanding, 85,955,556 (2006) and 86,673,821 (2005)	860	867
Class B stock, \$.01 par value: authorized, 3,000,000 shares; issued and outstanding, 291,796 (2006 and 2005)	3	3

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Additional paid-in capital	289,416	300,419
Unrealized gain on available for sale securities	4,152	
Accumulated earnings	395,957	402,740
TOTAL SHAREHOLDERS EQUITY	690,388	704,029
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	\$ 1,198,908	\$ 1,239,646

See accompanying notes to consolidated financial statements

3

Table of Contents

WESTWOOD ONE, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share amounts)

	Three Months Ended		Nine Months Ended	
	September 30, (Unaudited)		September 30, (Unaudited)	
	2006	2005 (Restated)	2006	2005 (Restated)
NET REVENUES	\$ 114,263	\$ 134,928	\$ 364,197	\$ 410,847
Operating Costs (includes related party expenses of \$17,117, \$18,094, \$58,853 and \$60,103, respectively)	82,010	88,799	285,329	282,188
Depreciation and Amortization (includes related party warrant amortization of \$2,427, \$2,427, \$7,281 and \$7,281, respectively)	5,239	5,194	15,424	15,597
Corporate General and Administrative Expenses (includes related party expenses of \$825, \$819, \$2,440 and \$2,367, respectively)	3,178	3,303	13,031	10,918
	90,427	97,296	313,784	308,703
OPERATING INCOME	23,836	37,632	50,413	102,144
Interest Expense	6,625	4,840	19,117	12,626
Other (Income) Expense	(154)	(133)	(389)	(319)
INCOME BEFORE INCOME TAXES	17,365	32,925	31,685	89,837
INCOME TAXES	6,881	12,856	12,558	34,460
NET INCOME	\$ 10,484	\$ 20,069	\$ 19,127	\$ 55,377
EARNINGS PER SHARE:				
BASIC	\$ 0.12	\$ 0.22	\$ 0.22	\$ 0.60
DILUTED	\$ 0.12	\$ 0.22	\$ 0.22	\$ 0.60
WEIGHTED AVERAGE SHARES OUTSTANDING:				
BASIC	86,246	90,338	87,287	91,940
DILUTED	86,248	90,487	87,299	92,490

Table of Contents

WESTWOOD ONE, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Nine Months Ended September 30, (Unaudited)	
	2006	2005 (Restated)
CASH FLOW FROM OPERATING ACTIVITIES:		
Net income	\$ 19,127	\$ 55,377
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	15,424	15,597
Disposal of property and equipment		88
Deferred taxes	(4,554)	(3,416)
Non-cash stock compensation	9,596	8,977
Amortization of deferred financing costs	250	250
	39,843	76,873
Changes in assets and liabilities:		
Accounts receivable	27,705	19,620
Prepaid and other assets	1,190	(5,731)
Deferred revenue	(606)	(4,109)
Income taxes payable and prepaid income taxes	(20,287)	11,819
Accounts payable and accrued expenses and other liabilities	17,414	11,928
Amounts payable to related parties	(3,109)	(998)
Net Cash Provided By Operating Activities	62,150	109,402
CASH FLOW FROM INVESTING ACTIVITIES:		
Capital expenditures	(5,258)	(2,889)
Repayment of loan receivable	2,000	
Acquisition of companies and other	75	(204)
Net Cash Used in Investing Activities	(3,183)	(3,093)
CASH FLOW FROM FINANCING ACTIVITIES:		
Issuance of common stock	302	2,559
Borrowings under bank and other long-term obligations	10,000	75,000
Debt repayments and payments of capital lease obligations	(30,509)	(35,477)
Dividend payments	(25,910)	(18,264)
Repurchase of common stock	(11,044)	(120,579)
Windfall tax benefits from stock option exercises		682
Net Cash Used in Financing Activities	(57,161)	(96,079)
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,806	10,230
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	10,399	10,932

CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$ 12,205	\$ 21,162
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See accompanying notes to consolidated financial statements

5

Table of Contents

WESTWOOD ONE, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except share and per share data)

NOTE 1 Basis of Presentation:

The accompanying Consolidated Balance Sheets as of September 30, 2006 and December 31, 2005, and the Consolidated Statements of Operations and the Consolidated Statements of Cash Flows for the three and nine month periods ended September 30, 2006 and 2005 are unaudited, but in the opinion of management include all adjustments necessary for a fair statement of the financial position, the results of operations and cash flows for the periods presented and have been prepared in a manner consistent with the audited financial statements for the year ended December 31, 2005, as restated (See Note 2). Results of operations for interim periods are not necessarily indicative of annual results. These financial statements should be read in conjunction with the audited financial statements and footnotes for the year ended December 31, 2005, included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission (the SEC) on February 27, 2006.

Subsequent to the second quarter of 2006, the Company identified a clerical error in their previously presented statement of cash flows for the six month period ending June 30, 2006. The error, in the amount of \$10,000, related to a debt repayment that was classified as a reduction in accounts payable resulting in an understatement of Net Cash Provided by Operating Activities and an understatement of Net Cash Used in Financing Activities. Consequently, for the six months ended June 30, 2006 Net Cash Provided by Operating Activities should have been \$39,869 and Net Cash Used in Financing Activities should have been \$38,341.

NOTE 2 Equity-Based Compensation:

Equity Compensation Plans

The Company established stock option plans in 1989 (the 1989 Plan) and 1999 (the 1999 Plan) which provide for the granting of options to directors, officers and key employees to purchase Company common stock at its market value on the date the options are granted. Under the 1989 Plan, 12,600,000 shares were reserved for grant through March 1999. The 1989 Plan expired, but certain grants made under the 1989 Plan remain outstanding at September 30, 2006. On September 22, 1999, the stockholders ratified the 1999 Plan which authorized the grant of up to 8,000,000 shares of Common Stock. Options granted under the 1999 Plan generally become exercisable after one year in 20% increments per year and expire within ten years from the date of grant.

On May 19, 2005, the Board modified the 1999 Plan by deleting the provisions of the 1999 Plan that provided for a mandatory annual grant of 10,000 stock options to outside directors. Also, on May 19, 2005, the stockholders of the Company approved the 2005 Equity Compensation Plan (the 2005 Plan). Among other things, the 2005 Plan provides for the granting of restricted stock and restricted stock units (RSUs) of the Company. A maximum of 9,200,000 shares of common stock of the Company is authorized for the issuance of awards under the 2005 Plan.

Beginning on May 19, 2005, outside directors automatically receive a grant of RSUs equal to \$100 in value on the date of each Company annual meeting of stockholders. Newly appointed outside directors receive an initial grant of RSUs equal to \$150 in value on the date such director is appointed to the Company's Board. Such awards are governed by the 2005 Plan.

Options and restricted stock granted under the 2005 Plan generally vest in 25% increments per year, at the end of each year, and options expire within ten years from the date of grant. RSUs awarded to directors generally vest over a three-year period in equal one-third increments per year. Directors' RSUs vest automatically, in full, upon a change in control or upon their retirement, as defined in the 2005 Plan. RSUs are payable in shares of the Company's common stock. Recipients of restricted stock and RSUs are entitled to receive dividend equivalents (subject to vesting) when and if the Company pays a cash dividend on its common stock.

Table of Contents

WESTWOOD ONE, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except share and per share data)

Restricted stock has the same cash dividend and voting rights as other common stock and is considered to be currently issued and outstanding. Restricted stock and RSUs have dividend equivalent rights equal to the cash dividend paid on common stock. RSUs do not have the voting rights of common stock, and the shares underlying the RSUs are not considered issued and outstanding.

At September 30, 2006 there were 10,733,800 shares available for grant under the Company's equity compensation plans.

Adoption of SFAS 123R

Prior to January 1, 2006, the Company accounted for equity-based compensation under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25 (APB No. 25), Accounting for Stock Issued to Employees, and the related Interpretations, as permitted by Financial Accounting Standards Board Statement No. 123, Accounting for Stock Based Compensation. No share based compensation expense was recognized in the Statement of Operations as all option grants had an exercise price equal to the market value of the underlying common stock on the date of grant and the number of shares was fixed, except for a non-cash stock compensation charge of \$391 recorded in 2004 in connection with the change in status of an employee to an independent contractor, and \$400 recorded in 2005 in connection with the grant of RSUs to certain individuals.

Effective January 1, 2006, the Company adopted Financial Accounting Standards Board Statement of Financial Accounting Standards No. 123 (Revised 2004), Share-Based Payment (SFAS 123R). SFAS 123R eliminates the alternative set forth in APB 25 allowing companies to use the intrinsic value method of accounting and requires that companies record expense for stock compensation on a fair value based method. In connection with the adoption of SFAS 123R, the Company has elected to utilize the modified retrospective transition alternative and has restated all prior periods to reflect stock compensation expense in accordance with SFAS 123. The restatements for each of the 2005 fiscal quarters are, and will continue to be, included in the Company's 2006 quarterly filings on Forms 10-Q.

As a result of adopting SFAS 123R, the Company's income before income taxes was \$2,534 and \$2,740 lower for the three month periods ended September 30, 2006 and 2005, respectively, and \$8,074 and \$8,799 lower for the nine month periods ended September 30, 2006 and 2005, respectively, than if it had continued to account for the share-based compensation under APB No. 25. Income taxes were \$994 and \$1,056 lower for the three month periods and \$3,192 and \$3,530 lower for the nine month periods ended September 30, 2006 and 2005, respectively.

Prior to the adoption of SFAS 123R, the Company presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the Consolidated Statements of Cash Flows. SFAS 123R requires that cash flows resulting from tax deductions that are in excess of the compensation costs recognized for those options (known as Windfall Tax Benefits) be classified as financing cash flows.

The following is a summary of the adjustments to the consolidated financial statements as a result of these restatements:

Selected Balance Sheet Data:

	December 31, 2005		
	As previously reported	Adjustment	As restated
Deferred tax (liability) /asset	\$ (10,619)	\$ 19,388	\$ 8,769
Paid-in capital	211,610	88,809	300,419
Retained earnings	472,161	(69,421)	402,740

Table of Contents

WESTWOOD ONE, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except share and per share data)

Selected Statement of Operations Data:

	Three Months Ended September 30, 2005			Nine Months Ended September 30, 2005		
	As previously reported	Adjustment	As restated	As previously reported	Adjustment	As restated
Operating Costs	\$87,166	\$ 1,633	\$88,799	\$276,895	\$ 5,293	\$282,188
Corporate General and Administrative Expenses	2,196	1,107	3,303	7,412	3,506	10,918
Income Before Income Taxes	35,665	(2,740)	32,925	98,636	(8,799)	89,837
Income Taxes	13,912	(1,056)	12,856	37,990	(3,530)	34,460
Net Income	21,753	(1,684)	20,069	60,646	(5,269)	55,377
Basic Earnings Per Share	\$ 0.24	\$ (0.02)	\$ 0.22	\$ 0.66	\$ (0.06)	\$ 0.60
Diluted Earnings Per Share	\$ 0.24	\$ (0.02)	\$ 0.22	\$ 0.66	\$ (0.06)	\$ 0.60

Equity Compensation Activity

The Company has awarded RSUs to Board members and certain key executives, which vest over three and four years, respectively. The cost of the RSUs, which is determined to be the fair market value of the shares at the date of grant net of estimated forfeitures, is expensed ratably over the vesting period, or period to retirement eligibility if shorter. The Company's RSU activity during the nine month period ended September 30, 2006 follows:

	2006 Shares	Aggregate Grant Date Fair Value	Weighted Average Grant Date Fair Value Per Share
<u>RSUs:</u>			
Outstanding at December 31, 2005	100,683	\$ 1,819	\$ 18.07
Granted during the period	180,777	2,194	12.14
Dividend equivalents during the period	7,721	65	8.39
Forfeited during the period	(44,075)	(733)	16.64
Converted to common stock	(1,735)	(34)	19.70
Outstanding at end of period	243,371	\$ 3,311	\$ 13.60

As of September 30, 2006, there was \$1,993 of unearned compensation cost related to the RSUs granted. That cost is expected to be recognized over a weighted-average period of 1.69 years. The total compensation expense recognized related to RSUs was \$338 and \$145 for the three month periods ended September 30, 2006 and 2005, respectively, and \$948 and \$178 for the nine month periods ended September 30, 2006 and 2005, respectively. These costs have been included in corporate, general and administrative expenses in the accompanying Statement of Operations.

The Company has awarded restricted shares of common stock to certain key employees. The awards have restriction periods tied solely to employment and vest over four years. The cost of these restricted stock awards,

calculated as the fair market value of the shares on the date of grant net of estimated forfeitures, is expensed ratably over the vesting period. The Company's restricted stock activity during the nine month period ended September 30, 2006 follows:

8

Table of Contents

WESTWOOD ONE, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except share and per share data)

	2006 Shares	Grant Date Fair Value	Weighted Average Grant Date Fair Value Per Share
<u>RESTRICTED STOCK:</u>			
Unvested at December 31, 2005		\$	\$
Granted during the period (1)	341,705	\$4,521	13.23
Vested during the period			
Forfeited during the period	(14,268)	(203)	14.21
Unvested at September 30, 2006	327,437	\$4,318	\$13.18

(1) Amount includes dividend equivalents on unvested shares

As of September 30, 2006, there was \$2,994 of unearned compensation cost related to restricted stock grants. That cost is expected to be recognized over a weighted-average period of 3.25 years. The total compensation expense recognized related to restricted stock is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	2005*	2006	2005*
<u>Included In:</u>				
Corporate General and Administrative Expenses	\$ 35	\$	\$ 73	\$
Operating Costs	192		501	
Total	\$227	\$	\$574	\$

*There was no restricted stock issued as of September 30, 2005.

The Company's stock option activity during the nine month period ended September 30, 2006 follows:

	2006 Shares	Weighted Average Exercise Price
<u>STOCK OPTIONS:</u>		
Outstanding at December 31, 2005	7,787,589	\$25.07
Granted during the period	755,560	14.42
Exercised during the period	(30,000)	10.09
Cancelled during the period	(1,708,068)	25.08
Forfeited during the period	(579,082)	22.93
Expired during the Period	(7,500)	20.73
Outstanding at September 30, 2006	6,218,499	\$24.05

At September 30, 2006, options to purchase 3,632,726 shares of Common Stock were currently vested and exercisable at a weighted average exercise price of \$25.17. The aggregate intrinsic value of the options outstanding at

September 30, 2006 was \$25, and the aggregate intrinsic value of the options vested and exercisable at September 30, 2006 was \$25.

Table of Contents

WESTWOOD ONE, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except share and per share data)

The aggregate intrinsic value of options exercised was \$0 and \$242 during the three months, and \$42 and \$2,698 during the nine months, ended September 30, 2006 and 2005 respectively. The aggregate intrinsic value of vested and exercisable options represents the total pre-tax intrinsic value (the difference between the Company's closing stock price on the last trading day of the third quarter of fiscal 2006 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on September 30, 2006. This amount changes based on the fair market value of the Company's stock.

As of September 30, 2006, there was \$17,568 of unearned compensation cost related to stock options granted under the plans. That cost is expected to be recognized over a weighted-average period of 2.49 years. The total compensation expense recognized related to options is as follows:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
<u>Included In:</u>	2006	2005	2006	2005
Corporate General and Administrative Expenses	\$1,067	\$1,107	\$3,503	\$3,506
Operating Costs	1,467	1,633	4,571	5,293
Total	\$2,534	\$2,740	\$8,074	\$8,799

The aggregate estimated fair value of options vesting was \$2,745 and \$4,715 during the three months and \$5,029 and \$25,405 during the nine months ended September 30, 2006 and 2005, respectively. The weighted average fair value of the options granted was \$5.57 and \$6.05 during the nine months ended September 30, 2006 and 2005, respectively. The estimated fair value of options granted was measured on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

Three Months Ended Nine Months Ended