SINCLAIR BROADCAST GROUP INC
Form 10-Q
November 09, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

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

For the transition period from to .

Commission File Number: **000-26076**

SINCLAIR BROADCAST GROUP, INC.

(Exact name of Registrant as specified in its charter)

Maryland	**52-1494660**

(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)

10706 Beaver Dam Road
Hunt Valley, Maryland 21030
(Address of principal executive offices)

(410) 568-1500

(Registrant s telephone number, including area code)

None

(Former name, former address and former fiscal year-if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

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 o Accelerated filer x Non-accelerated filer 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.

Title of each class	Number of shares outstanding as of November 3, 2006
Class A Common Stock	47,393,356
Class B Common Stock	38,348,331

SINCLAIR BROADCAST GROUP, INC.

FORM 10-Q
FOR THE QUARTER ENDED SEPTEMBER 30, 2006

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SINCLAIR BROADCAST GROUP, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share data)

	As of September 30, 2006 (Unaudited)	As of December 31, 2005
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 32,495	$ 9,655
Accounts receivable, net of allowance for doubtful accounts of $3,773 and $4,596, respectively	118,004	127,913
Affiliate receivable	4,263	14
Current portion of program contract costs	74,728	51,528
Income taxes receivable	2,581	
Prepaid expenses and other current assets	8,938	17,616
Deferred barter costs	2,942	2,027
Assets held for sale		3,678
Deferred tax assets	9,446	10,591
Total current assets	253,397	223,022
PROGRAM CONTRACT COSTS, less current portion	59,302	36,494
PROPERTY AND EQUIPMENT, net	283,732	304,355
GOODWILL, net	1,017,524	1,040,234
BROADCAST LICENSES, net	409,620	409,620
DEFINITE-LIVED INTANGIBLE ASSETS, net	212,820	224,673
OTHER ASSETS	37,788	44,907
Total assets	$ 2,274,183	$ 2,283,305
LIABILITIES AND SHAREHOLDERS EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 2,543	$ 3,799
Income taxes payable		2,662
Accrued liabilities	79,508	84,623
Current portion of notes payable, capital leases and commercial bank financing	33,848	33,802
Current portion of notes and capital leases payable to affiliates	4,238	4,135
Current portion of program contracts payable	94,196	88,510
Deferred barter revenues	3,230	2,501
Deferred gain on sale of broadcast assets		3,249
Liabilities held for sale		1,407
Total current liabilities	217,563	224,688
LONG-TERM LIABILITIES:		
Notes payable, capital leases and commercial bank financing, less current portion	1,354,432	1,397,649
Notes payable and capital leases to affiliates, less current portion	15,179	15,152
Program contracts payable, less current portion	103,438	65,239
Deferred tax liabilities	284,186	277,451
Other long-term liabilities	31,586	52,438
Total liabilities	2,006,384	2,032,617
MINORITY INTEREST IN CONSOLIDATED ENTITIES	728	966

SHAREHOLDERS EQUITY:		
Class A Common Stock, $.01 par value, 500,000,000 shares authorized, 47,375,788 and 47,122,407 shares issued and outstanding, respectively	474	471
Class B Common Stock, $.01 par value, 140,000,000 shares authorized, 38,348,331 shares issued and outstanding, convertible into Class A Common Stock	383	383
Additional paid-in capital	595,372	593,259
Accumulated deficit	(329,158)	(344,391)
Total shareholders equity	267,071	249,722
Total liabilities and shareholders equity	$ 2,274,183	$ 2,283,305

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

SINCLAIR BROADCAST GROUP, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share data) (Unaudited)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
REVENUES:				
Station broadcast revenues, net of agency commissions	$ 152,362	$ 149,027	$ 464,058	$ 456,572
Revenues realized from station barter arrangements	12,772	12,039	38,206	41,551
Other operating divisions revenues	3,324	4,724	14,753	15,160
Total revenues	168,458	165,790	517,017	513,283
OPERATING EXPENSES:				
Station production expenses	36,148	35,605	111,342	112,597
Station selling, general and administrative expenses	34,853	34,541	103,633	103,691
Expenses recognized from station barter arrangements	11,451	11,158	34,779	38,447
Amortization of program contract costs and net realizable value adjustments	24,122	18,587	65,428	52,131
Other operating divisions expenses	3,346	3,699	15,108	14,000
Depreciation of property and equipment	10,907	12,175	35,881	38,337
Corporate general and administrative expenses	5,141	5,259	17,059	15,345
Amortization of definite-lived intangible assets and other assets	4,435	4,475	13,195	13,529
Total operating expenses	130,403	125,499	396,425	388,077
Operating income	38,055	40,291	120,592	125,206
OTHER INCOME (EXPENSE):				
Interest expense and amortization of debt discount and deferred financing costs	(28,448)	(31,113)	(86,783)	(88,950)
Interest income	913	187	1,263	416
Gain (loss) from sale of assets	4	(69)	(265)	(69)
Loss from extinguishment of debt	(25)		(904)	(1,631)
Unrealized gain from derivative instruments		5,761	2,907	17,487
Income (loss) from equity and cost investees	57	24	6,192	(389)
Other (expense) income, net	(34)	206	448	755
Total other expense	(27,533)	(25,004)	(77,142)	(72,381)
Income from continuing operations before income taxes	10,522	15,287	43,450	52,825
INCOME TAX BENEFIT (PROVISION)	12,318	(2,267)	(2,741)	(16,008)
Income from continuing operations	22,840	13,020	40,709	36,817
DISCONTINUED OPERATIONS:				
(Loss) income from discontinued operations, net of related income tax (provision) benefit of ($275), ($343), $329 and ($2,413), respectively	(275)	701	383	4,841
Gain from discontinued operations, net of related income tax (provision) benefit of $0, ($10,494), $259 and ($80,002), respectively		17,508	1,774	146,024
NET INCOME	22,565	31,229	42,866	187,682
PREFERRED STOCK DIVIDENDS				(5,004)
EXCESS OF PREFERRED STOCK CARRYING VALUE OVER REDEMPTION VALUE				26,201
NET INCOME AVAILABLE TO COMMON SHAREHOLDERS	$ 22,565	$ 31,229	$ 42,866	$ 208,879
BASIC AND DILUTED EARNINGS PER COMMON SHARE:				
Basic earnings per share from continuing operations	$ 0.27	$ 0.15	$ 0.48	$ 0.68
Basic earnings per share from discontinued operations	$	$ 0.21	$ 0.03	$ 1.76
Basic earnings per share	$ 0.26	$ 0.36	$ 0.50	$ 2.44
Diluted earnings per share from continuing operations	$ 0.26	$ 0.15	$ 0.48	$ 0.67
Diluted earnings per share from discontinued operations	$	$ 0.21	$ 0.03	$ 1.64
Diluted earnings per share	$ 0.25	$ 0.36	$ 0.50	$ 2.31
Weighted average shares outstanding	85,719	85,428	85,650	85,353
Weighted average shares and equivalent shares outstanding	99,149	85,448	85,655	92,065

Dividends declared per share	$ 0.125	$ 0.075	$ 0.325	$ 0.200

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

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SINCLAIR BROADCAST GROUP, INC.

CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2006
(in thousands) (Unaudited)

	Class A Common Stock	Class B Common Stock	Additional Paid-In Capital	Accumulated Deficit	Total Shareholders Equity
BALANCE, December 31, 2005	$ 471	$ 383	$ 593,259	$ (344,391)	$ 249,722
Dividends declared on Class A and Class B Common Stock				(27,633)	(27,633)
Class A Common Stock issued pursuant to stock-based compensation plans	3		2,113		2,116
Net income				42,866	42,866
BALANCE, September 30, 2006	$ 474	$ 383	$ 595,372	$ (329,158)	$ 267,071

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

SINCLAIR BROADCAST GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands) (Unaudited)

	Nine Months Ended September 30, 2006	2005
CASH FLOWS FROM (USED IN) OPERATING ACTIVITIES:		
Net income	$ 42,866	$ 187,682
Adjustments to reconcile net income to net cash flows from operating activities:		
Amortization of debt discount, net of debt premium	1,563	86
Depreciation of property and equipment	35,881	38,879
Recognition of deferred revenue	(5,728)	(3,706)
Accretion of capital leases	335	529
(Income) loss from equity and cost investees	(6,192)	389
Loss on sale of property	265	69
Gain on sale of broadcast assets related to discontinued operations	(2,659)	(226,026)
Unrealized gain from derivative instruments	(2,907)	(17,487)
Amortization of definite-lived intangible assets and other assets	13,195	13,551
Amortization of program contract costs and net realizable value adjustments	65,428	52,737
Amortization of deferred financing costs	1,953	1,933
Stock-based compensation	1,442	1,160
Loss from extinguishment of debt, non-cash portion	854	1,079
Amortization of derivative instruments	403	404
Deferred tax provision related to operations	7,750	24,376
Deferred tax (benefit) provision related to discontinued operations	(1,177)	31,874
Net effect of change in deferred barter revenues and deferred barter costs	(186)	(247)
Changes in assets and liabilities, net of effects of acquisitions and dispositions:		
Decrease in accounts receivable, net	9,957	13,280
Increase in affiliate receivable	(4,250)	
Decrease in taxes receivable	(3,040)	624
Decrease in prepaid expenses and other current assets	8,718	7,101
Decrease in other long-term assets	500	5,221
Decrease in accounts payable and accrued liabilities	(1,513)	(22,083)
Increase in income taxes payable	7,822	17,627
Decrease in other long-term liabilities	(2,267)	(1,272)
Decrease in minority interest	(57)	(334)
Dividends and distributions from equity and cost investees	6,355	1,707
Payments on program contracts payable	(68,170)	(79,103)
Net cash flows from operating activities	107,141	50,050
CASH FLOWS FROM (USED IN) INVESTING ACTIVITIES:		
Acquisition of property and equipment	(13,492)	(12,240)
Payments for acquisition of television stations	(1,710)	(11,040)
Investments in equity and cost investees	(153)	(970)
Proceeds from the sale of assets	1,394	59
Proceeds from the sale of broadcast assets related to discontinued operations	1,400	295,190
Proceeds from the sale of equity investees		21,500
Proceeds from insurance settlement		404
Loans to affiliates	(107)	(95)
Proceeds from loans to affiliates	105	93
Net cash flows (used in) from investing activities	(12,563)	292,901
CASH FLOWS FROM (USED IN) FINANCING ACTIVITIES:		
Proceeds from notes payable, commercial bank financing and capital leases	75,000	35,500
Repayments of notes payable, commercial bank financing and capital leases	(114,294)	(346,279)
Proceeds from exercise of stock options		73
Payments for deferred financing costs		(1,913)
Dividends paid on Series D Convertible Exchangeable Preferred Stock		(5,004)

Dividends paid on Class A and Class B Common Stock	(25,458)	(12,803)
Payments for derivative terminations	(3,750)	
Repayments of notes and capital leases to affiliates	(3,236)	(4,890)
Net cash flows used in financing activities	(71,738)	(335,316)
NET INCREASE IN CASH AND CASH EQUIVALENTS	22,840	7,635
CASH AND CASH EQUIVALENTS, beginning of period	9,655	10,491
CASH AND CASH EQUIVALENTS, end of period	$ 32,495	$ 18,126

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

SINCLAIR BROADCAST GROUP, INC.CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITYFOR THE

SINCLAIR BROADCAST GROUP, INC.
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Principles of Consolidation

The accompanying unaudited consolidated financial statements include the accounts of Sinclair Broadcast Group, Inc. and those of our wholly-owned and majority-owned subsidiaries and variable interest entities where we are deemed the primary beneficiary. Minority interest represents a minority owner s proportionate share of the equity in certain of our consolidated entities. All significant intercompany transactions and account balances have been eliminated in consolidation.

Discontinued Operations

In accordance with Statement of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we reported the financial position and results of operations of KOVR-TV in Sacramento, California, KSMO-TV in Kansas City, Missouri and WEMT-TV in Tri-Cities, Tennessee as discontinued operations in the accompanying consolidated balance sheets and consolidated statements of operations. Discontinued operations have not been segregated in the consolidated statements of cash flows; therefore, amounts for certain captions will not agree with the accompanying consolidated balance sheets and consolidated statements of operations. The operating results of KOVR, KSMO and WEMT are not included in our consolidated results from continuing operations for the three and nine months ended September 30, 2006 and 2005. In accordance with Emerging Issues Task Force Issue (EITF) No. 87-24, *Allocation of Interest to Discontinued Operations*, we have allocated $3.6 million of interest expense to discontinued operations for the nine months ended September 30, 2005. No interest expense was allocated for the three months ended September 30, 2006 and 2005 and for the nine months ended September 30, 2006. See *Note 9. Discontinued Operations,* for additional information.

Interim Financial Statements

The consolidated financial statements for the three and nine months ended September 30, 2006 and 2005 are unaudited. In the opinion of management, such financial statements have been presented on the same basis as the annual consolidated financial statements and include all adjustments, consisting only of normal recurring adjustments necessary for a fair presentation of the consolidated balance sheets, consolidated statements of operations and consolidated statements of cash flows for these periods.

As permitted under the applicable rules and regulations of the Securities and Exchange Commission, the consolidated financial statements do not include all disclosures normally included with audited consolidated financial statements and, accordingly, should be read together with the audited consolidated financial statements and notes thereto in our Annual Report on Form 10-K, as amended, for the year ended December 31, 2005. The consolidated statements of operations presented in the accompanying consolidated financial statements are not necessarily representative of operations for an entire year.

Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement No. 157, *Fair Value Measurements*. This statement defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. Early adoption is permitted. We are currently evaluating the effect this statement will have on our consolidated financial statements.

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. It prescribes the minimum recognition threshold a tax position must meet before being recognized in the financial statements and also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. In addition, FIN 48 replaces income tax guidance from FASB Statement No. 5, *Accounting for Contingencies.* This interpretation will be effective beginning on January 1, 2007. We are currently evaluating the effect FIN 48 will have on our consolidated financial statements.

On January 1, 2006, we adopted SFAS No. 123R, *Share-Based Payment* (SFAS 123R). SFAS 123R requires us to expense the fair value of grants of various stock-based compensation programs over the vesting period of the awards. We elected to adopt the Modified Prospective Application transition method which does not result in the restatement of previously issued consolidated financial statements. For additional information regarding our accounting under SFAS 123R, see *Note 2. Stock-Based Compensation*.

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Use of Estimates

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses in the consolidated financial statements and in the disclosures of contingent assets and liabilities. Actual results could differ from those estimates.

Network Compensation

On January 24, 2006, CBS Corporation (CBS) and Warner Bros. Entertainment (Warner Bros.) announced their intent to merge the operations of their respective networks, UPN and The WB, under a broadcasting network to be called The CW. On August 1, 2004, we entered into an affiliation agreement with UPN (for six stations) that was set to expire July 31, 2007. The agreement was for the networks to produce and distribute programming in exchange for each station s commitment to air the programming at specified times and for commercial announcement time during programming. Under this agreement, UPN was to pay us a fixed amount as revenue for each station during the first two years, in equal installments at the beginning of each month. No payment was due from UPN in the third year of the agreement. The amount received from UPN had been recognized over the term of the agreement and a pro-rata portion of the revenue had been deferred to be recognized in the third year.

On May 2, 2006, we entered into a Release and Settlement Agreement with The WB and UPN, in which we released The WB and UPN, and The WB and UPN released us, from any claims or other liabilities we or The WB or UPN may have arising out of or in connection with (a) any agreement, including any affiliation agreements entered into by us with The WB or UPN, and (b) any services previously performed by any one of the parties to the Release and Settlement Agreement for any other party to the Release and Settlement Agreement. As a result of this agreement, we have changed the revenue recognition period from an end date of July 31, 2007 to an end date of September 30, 2006, when UPN ceased broadcasting. For the three and nine months ended September 30, 2006, we recorded UPN network compensation of $0.2 million and $0.5 million, respectively.

Restructuring Costs

During the nine months ended September 30, 2006, we incurred costs associated with restructuring the news operations at certain of our stations. Specifically, on or before March 31, 2006, we ceased our locally produced news broadcasts in nine of our markets and consequently let go our news employees and cancelled our news-related contracts. The total one-time employee benefit costs related to this restructuring were $0.5 million and the total one-time contract cancellation and other exit costs were $0.5 million, all of which were recorded as station production expenses for the three months ended March 31, 2006.

The major components of the restructuring charges and the remaining accrual balance related to the restructuring plan as of September 30, 2006 follow (in thousands):

	Salary and Severance Costs	Contract Expenses	Other Exit Costs	Total
Balance at December 31, 2005	$	$	$	$
Restructuring charges	525	362	274	1,161
Amounts utilized	(342)	(7)	(47)	(396)
Balance at March 31, 2006	$ 183	$ 355	$ 227	$ 765
Restructuring charges		3	27	30
Amounts utilized	(183)	(175)	(157)	(515)
Balance at June 30, 2006	$	$ 183	$ 97	$ 280
Restructuring charges				
Amounts utilized		(67)	(48)	(115)
Balance at September 30, 2006	$	$ 116	$ 49	$ 165

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Reclassifications

Certain reclassifications have been made to the prior periods consolidated financial statements to conform with the current period s presentation.

2. STOCK-BASED COMPENSATION:

Description of Awards

We have five types of stock-based compensation awards: compensatory stock options (options), restricted stock awards (RSAs), an employee stock purchase plan (ESPP), employer matching contributions (the Match) for participants in our 401(k) plan and stock grants to our non-employee directors. Below is a summary of the key terms and methods of valuation of our stock-based compensation awards:

Options. In June 1996, our Board of Directors adopted, upon approval of the shareholders by proxy, the 1996 Long-Term Incentive Plan (LTIP). The purpose of the LTIP is to reward key individuals for making major contributions to our success and the success of our subsidiaries and to attract and retain the services of qualified and capable employees. Options granted pursuant to the LTIP must be exercised within 10 years following the grant date. A total of 14,000,000 shares of Class A Common Stock are reserved for awards under this plan. As of September 30, 2006, 9,913,684 shares (including forfeited shares) were available for future grants.

On April 21, 2005, we accelerated the vesting of 390,039 stock options, which were all of our outstanding unvested options at that time. We accelerated the vesting of these options to prevent recognizing an expense of approximately $0.8 million, before taxes, in 2006 and future periods. The acceleration of the vesting resulted in a modification to the original options. In accordance with FASB Interpretation No. 44, *Accounting for Certain Transactions Involving Stock-Based Compensation* (FIN 44), we recorded an immaterial compensation charge based on the intrinsic value of the awards (as defined by FIN 44) as measured on the modification date. The exercise prices of these options range from $7.39 to $15.19 per share and there was no material impact to earnings as a result of this acceleration because most options had an exercise price that was above the trading price on the vesting date. We have not issued any options subsequent to accelerating the vesting. There were no options exercised during the nine months ended September 30, 2006.

The summary of changes in outstanding options included in the footnotes to our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2005, as amended, included information related to these plans. The following is a summary of changes in outstanding stock options:

	Options	**Weighted-Average Exercise Price**	**Exercisable**	**Weighted-Average Exercise Price**
Outstanding at end of 2005	6,352,720	$ 15.78	6,352,720	$ 15.78
2006 Activity:				
Granted				
Exercised				
Forfeited	(3,107,570)	$ 15.08		
Outstanding at September 30, 2006	3,245,150	$ 16.24	3,245,150	$ 16.24

We do not expect to issue options in future periods, and instead, we expect to issue RSAs, discussed below. Therefore, the adoption of SFAS 123R did not have a material effect on our consolidated income, cash flows and basic and diluted earnings per share.

In the event the Board of Directors decides to issue options, we would be required to determine the method we would use to estimate the fair value, such as the Black-Scholes method or a lattice method. Additionally, we would be required to estimate certain assumptions, including expected volatility and estimated forfeitures.

RSAs. RSAs are granted to employees pursuant to the LTIP. RSAs have certain restrictions that lapse over three years at 25%, 25% and 50%, respectively. As the restrictions lapse, the stock may be freely traded on the open market. On April 3, 2006, we awarded 40,000 RSAs that had a fair value of $7.81 per share, which was the value of the stock on the trading date immediately prior to the grant date. For the three and nine months ended September 30, 2006, we recorded expense of less than $0.1 million and we will cont