Warner Music Group Corp.
Form 10-Q
August 08, 2013
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# 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 June 30, 2013**

**OR**

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

**Commission File Number 001-32502**

# Warner Music Group Corp.

**(Exact name of Registrant as specified in its charter)**

| | |
|---|---|
| **Delaware** | **13-4271875** |
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. Employer Identification No.)** |

**75 Rockefeller Plaza**

**New York, NY 10019**

**(Address of principal executive offices)**

**(212) 275-2000**

**(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 ¨ No x

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 ¨

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

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

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

There is no public market for the Registrant s common stock. As of August 8, 2013 the number of shares of the Registrant s common stock, par value $0.001 per share, outstanding was 1,055. All of the Registrant s common stock is owned by affiliates of Access Industries, Inc. The Registrant has filed all Exchange Act reports for the preceding 12 months.

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**WARNER MUSIC GROUP CORP.**

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**ITEM 1. FINANCIAL STATEMENTS**

**Warner Music Group Corp.**

**Consolidated Balance Sheets**

| | June 30, 2013 (unaudited) | September 30, 2012 (audited) |
|---|---|---|
| | (in millions) | |
| **Assets** | | |
| Current assets: | | |
| Cash and equivalents | $ 102 | $ 302 |
| Accounts receivable, less allowances of $49 and $63 million | 309 | 398 |
| Inventories | 25 | 28 |
| Royalty advances expected to be recouped within one year | 119 | 116 |
| Deferred tax assets | 51 | 51 |
| Other current assets | 61 | 44 |
| Total current assets | 667 | 939 |
| Royalty advances expected to be recouped after one year | 145 | 142 |
| Property, plant and equipment, net | 135 | 152 |
| Goodwill | 1,393 | 1,380 |
| Intangible assets subject to amortization, net | 2,357 | 2,499 |
| Intangible assets not subject to amortization | 102 | 102 |
| Other assets | 91 | 64 |
| Total assets | $ 4,890 | $ 5,278 |
| **Liabilities and Equity** | | |
| Current liabilities: | | |
| Accounts payable | $ 121 | $ 156 |
| Accrued royalties | 1,017 | 997 |
| Accrued liabilities | 201 | 253 |
| Accrued interest | 56 | 89 |
| Deferred revenue | 126 | 101 |
| Current portion of long-term debt | 29 | |
| Other current liabilities | 6 | 10 |
| Total current liabilities | 1,556 | 1,606 |
| Long-term debt | 2,037 | 2,206 |
| Deferred tax liabilities | 346 | 375 |
| Other noncurrent liabilities | 157 | 147 |
| Total liabilities | 4,096 | 4,334 |
| Equity: | | |
| Common stock ($0.001 par value; 10,000 shares authorized; 1,055 and 1,000 shares issued and outstanding) | | |
| Additional paid-in capital | 1,128 | 1,129 |
| Accumulated deficit | (283) | (143) |
| Accumulated other comprehensive loss, net | (69) | (59) |
| Total Warner Music Group Corp. equity | 776 | 927 |
| Noncontrolling interest | 18 | 17 |

| | | |
|---|---|---|
| Total equity | 794 | 944 |
| Total liabilities and equity | $ 4,890 | $ 5,278 |

See accompanying notes

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**Warner Music Group Corp.**

**Consolidated Statements of Operations (Unaudited)**

| | Three Months Ended June 30, 2013 | Three Months Ended June 30, 2012 | Nine Months Ended June 30, 2013 | Nine Months Ended June 30, 2012 |
|---|---|---|---|---|
| | (in millions) | | | |
| Revenues | $ 663 | $ 651 | $ 2,107 | $ 2,049 |
| Costs and expenses: | | | | |
| Cost of revenues | (371) | (353) | (1,108) | (1,091) |
| Selling, general and administrative expenses (a) | (236) | (244) | (740) | (745) |
| Amortization of intangible assets | (48) | (47) | (143) | (145) |
| Total costs and expenses | (655) | (644) | (1,991) | (1,981) |
| Operating income | 8 | 7 | 116 | 68 |
| Loss on extinguishment of debt | (2) | | (85) | |
| Interest expense, net | (47) | (56) | (149) | (169) |
| Other (expense) income, net | (2) | 6 | (11) | 6 |
| Loss before income taxes | (43) | (43) | (129) | (95) |
| Income tax (expense) benefit | (19) | 11 | (8) | 3 |
| Net loss | (62) | (32) | (137) | (92) |
| Less: income attributable to noncontrolling interest | (1) | | (4) | (2) |
| Net loss attributable to Warner Music Group Corp. | $ (63) | $ (32) | $ (141) | $ (94) |
| (a) Includes depreciation expense of: | $ (13) | $ (12) | $ (38) | $ (37) |

See accompanying notes

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**Warner Music Group Corp.**

**Consolidated Statement of Comprehensive Loss (Unaudited)**

| | Three Months Ended June 30, | | Nine Months Ended June 30, | |
|---|---|---|---|---|
| | 2013 | 2012 | 2013 | 2012 |
| | (in millions) | | | |
| Net loss | $ (62) | $ (32) | $ (137) | $ (92) |
| Other comprehensive income (loss), net of tax: | | | | |
| Foreign currency translation adjustment | 4 | (20) | (8) | (28) |
| Deferred (losses) gains on derivative financial instruments | (2) | 1 | (2) | 1 |
| Other comprehensive income (loss), net of tax: | 2 | (19) | (10) | (27) |
| Total comprehensive loss | (60) | (51) | (147) | (119) |
| Less: comprehensive income attributable to noncontrolling interest | (1) | | (4) | (2) |
| Comprehensive loss attributable to Warner Music Group Corp. | $ (61) | $ (51) | $ (151) | $ (121) |

See accompanying notes

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**Warner Music Group Corp.**

**Consolidated Statements of Cash Flows (Unaudited)**

| | Nine Months Ended June 30, 2013 | 2012 |
|---|---|---|
| | (in millions) | |
| **Cash flows from operating activities** | | |
| Net loss | $ (137) | $ (92) |
| Adjustments to reconcile net loss to net cash provided by operating activities: | | |
| Loss on extinguishment of debt | 85 | |
| Depreciation and amortization | 181 | 182 |
| Deferred income taxes | (13) | (11) |
| Gain on sale of building | | (1) |
| Non-cash interest expense (income) | 8 | (2) |
| Equity losses (gains), including distributions | 3 | (1) |
| Non-cash stock-based compensation | 8 | |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 81 | 49 |
| Inventories | 2 | 1 |
| Royalty advances | (9) | 33 |
| Accounts payable and accrued liabilities | (80) | (40) |
| Royalty payables | 41 | 58 |
| Accrued interest | (33) | (23) |
| Deferred income | 25 | (1) |
| Other balance sheet changes | (15) | (45) |
| Net cash provided by operating activities | 147 | 107 |
| **Cash flows from investing activities** | | |
| Investment and acquisition of businesses | (18) | (5) |
| Acquisition of publishing rights | (35) | (21) |
| Proceeds from the sale of music catalog | | 2 |
| Proceeds from the sale of building | | 12 |
| Capital expenditures | (23) | (24) |
| Net cash used in investing activities | (76) | (36) |
| **Cash flows from financing activities** | | |
| Repayment of Acquisition Corp. 9.5% Senior Subordinated Notes | (1,250) | |
| Proceeds from issuance of Acquisition Corp 6.0% Senior Secured Notes | 500 | |
| Repayment of Acquisition Corp 6.0% Senior Secured Notes | (50) | |
| Proceeds from issuance of Acquisition Corp 6.25% Senior Secured Notes | 227 | |
| Repayment of Acquisition Corp 6.25% Senior Secured Notes | (23) | |
| Proceeds from Acquisition Corp Term Loan Facility | 594 | |
| Repayment of Term Loan | (110) | |
| Proceeds from draw down of the Revolving Credit Facility | 111 | |
| Repayment of the Revolving Credit Facility | (86) | |
| Tender/call premiums paid on early redemption of debt | (95) | |
| Consent fees paid on early redemption of debt | (34) | |
| Deferred financing costs paid | (42) | |
| Distribution to noncontrolling interest holders | (2) | (2) |

| | | |
|---|---|---|
| Net cash used in financing activities | (260) | (2) |
| Effect of exchange rate changes on cash and equivalents | (11) | (4) |
| Net (decrease) increase in cash and equivalents | (200) | 65 |
| Cash and equivalents at beginning of period | 302 | 154 |
| Cash and equivalents at end of period | $ 102 | $ 219 |

See accompanying notes

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**Warner Music Group Corp.**

**Consolidated Statement of Equity (Unaudited)**

| | Common Stock Shares | Common Stock Value | Additional Paid-in Capital | Accumulated Deficit | Accumulated Other Comprehensive Loss | Total Warner Music Group Corp. Equity | Noncontrolling Interests | Total Equity |
|---|---|---|---|---|---|---|---|---|
| | (in millions, except per share amounts) | | | | | | | |
| Balance at September 30, 2012 | **1,000** | **$ 0.001** | **$ 1,129** | **$ (143)** | **$ (59)** | **$ 927** | **$ 17** | **$ 944** |
| Net loss | | | | (141) | | (141) | 4 | (137) |
| Deconsolidation of entity | | | (1) | | | (1) | | (1) |
| Acquisition of noncontrolling interest | | | | 1 | | 1 | (1) | |
| Other comprehensive loss | | | | | (10) | (10) | | (10) |
| Distribution to noncontrolling interests | | | | | | | (2) | (2) |
| Stock dividend | 55 | | | | | | | |
| Balance at June 30, 2013 | **1,055** | **$ 0.001** | **$ 1,128** | **$ (283)** | **$ (69)** | **$ 776** | **$ 18** | **$ 794** |

See accompanying notes

**Warner Music Group Corp.**

**Notes to Consolidated Interim Financial Statements (Unaudited)**

**1. Description of Business**

Warner Music Group Corp. (the Company ) was formed on November 21, 2003. The Company is the direct parent of WMG Holdings Corp. ( Holdings ), which is the direct parent of WMG Acquisition Corp. ( Acquisition Corp. ). Acquisition Corp. is one of the world s major music-based content companies.

Pursuant to an Agreement and Plan of Merger, dated as of May 6, 2011 (the Merger Agreement ), by and among the Company, AI Entertainment Holdings LLC, a Delaware limited liability company ( Parent ) and an affiliate of Access Industries, Inc. ( Access ), and Airplanes Merger Sub, Inc., a Delaware corporation and a wholly owned subsidiary of Parent ( Merger Sub ), on July 20, 2011 (the Merger Closing Date ), Merger Sub merged with and into the Company with the Company surviving as a wholly owned subsidiary of Parent (the Merger ). In connection with the Merger, the Company delisted its common stock from listing on the NYSE. The Company continues to file with the SEC current and periodic reports that would be required to be filed with the SEC pursuant to Section 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act ) in accordance with certain covenants contained in the instruments covering its outstanding indebtedness.

The Company classifies its business interests into two fundamental operations: Recorded Music and Music Publishing. A brief description of these operations is presented below.

*Recorded Music Operations*

The Company s Recorded Music business primarily consists of the discovery and development of artists and the related marketing, distribution and licensing of recorded music produced by such artists. The Company plays an integral role in virtually all aspects of the recorded music value chain from discovering and developing talent to producing albums and promoting artists and their products.

In the U.S., Recorded Music operations are conducted principally through the Company s major record labels Warner Bros. Records and the Atlantic Records Group. The Company s Recorded Music operations also include Rhino, a division that specializes in marketing the Company s music catalog through compilations and reissuances of previously released music and video titles, as well as in the licensing of recordings to and from third parties for various uses, including film and television soundtracks. The Company also conducts its Recorded Music operations through a collection of additional record labels, including, among others, Asylum, East West, Elektra, Nonesuch, Parlophone, Reprise, Roadrunner, Rykodisc, Sire and Word.

Outside the U.S., Recorded Music activities are conducted in more than 50 countries primarily through various subsidiaries, affiliates and non-affiliated licensees. Internationally the Company engages in the same activities as in the U.S.: discovering and signing artists and distributing, marketing and selling their recorded music. In most cases, the Company also markets and distributes the records of those artists for whom the Company s U.S. record labels have international rights. In certain smaller markets, the Company licenses to unaffiliated third-party record labels the right to distribute its records. The Company s international artist services operations also include a network of concert promoters through which the Company provides resources to coordinate tours for the Company s artists and other artists. On July 1, 2013, the Company completed its acquisition of Parlophone Label Group ( PLG ) from Universal Music Group, a division of Vivendi. In addition to the Parlophone label, PLG included the Chrysalis/Ensign labels in the United Kingdom, EMI Classics and Virgin Classics and the EMI operating companies in Belgium, Czech Republic, Denmark, France, Norway, Poland, Portugal, Slovakia, Spain and Sweden.

Recorded Music distribution operations include Warner-Elektra-Atlantic Corporation ( WEA Corp. ), which markets and sells music and DVD products to retailers and wholesale distributors in the U.S., Alternative Distribution Alliance ( ADA ), which distributes the products of independent labels to retail and wholesale distributors in the U.S., various distribution centers and ventures operated internationally, an 80% interest in Word, which specializes in the distribution of music products in the Christian retail marketplace, and ADA Global, which provides distribution services outside of the U.S. through a network of affiliated and non-affiliated distributors.

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In addition to the Company s Recorded Music products being sold in physical retail outlets, the Company s Recorded Music products are also sold in physical form to online physical retailers such as Amazon.com, barnesandnoble.com and bestbuy.com and in digital form to online digital retailers such as Apple s iTunes and Google Play, and are otherwise exploited by online subscription services such as Spotify, Rhapsody and Deezer, and Internet radio services such as Pandora and iHeart Radio.

The Company has integrated the sale of digital content into all aspects of its Recorded Music and Music Publishing businesses including Artist & Repertoire ( A&R ), marketing, promotion and distribution. The Company s business development executives work closely with A&R departments to make sure that while a record is being made, digital assets are also created with all distribution channels in mind, including subscription services, social networking sites, online portals and music-centered destinations. The Company works side by side with its mobile and online partners to test new concepts. The Company believes existing and new digital businesses will be a significant source of growth for at least the next several years and will provide new opportunities to successfully monetize its assets and create new revenue streams. The proportion of digital revenues attributed to each distribution channel varies by region and since digital music is in the relatively early stages of growth, proportions may change as the roll out of new technologies continues. As an owner of musical content, the Company believes it is well positioned to take advantage of growth in digital distribution and emerging technologies to maximize the value of its assets.

The Company is also diversifying its revenues beyond its traditional businesses by entering into expanded-rights deals with recording artists in order to partner with artists in other areas of their careers. Under these agreements, the Company provides services to and participates in artists activities outside the traditional recorded music business. The Company has built artist services capabilities and platforms for exploiting this broader set of music-related rights and participating more broadly in the monetization of the artist brands it helps create.

The Company believes that entering into expanded-rights deals and enhancing its artist services capabilities will permit it to diversify revenue streams and capitalize on revenue opportunities in merchandising, fan clubs, sponsorship and touring. This will provide for improved long-term relationships with artists and allow the Company to more effectively connect artists and fans.

*Music Publishing Operations*

Where recorded music is focused on exploiting a particular recording of a song, music publishing is an intellectual property business focused on the exploitation of the song itself. In return for promoting, placing, marketing and administering the creative output of a songwriter, or engaging in those activities for other rights holders, the Company s Music Publishing business, Warner/Chappell Music, garners a share of the revenues generated from use of the song.

Warner/Chappell is headquartered in Los Angeles with operations in over 50 countries through various subsidiaries, affiliates and non-affiliated licensees. Warner/Chappell owns or controls rights to more than one million musical compositions, including numerous pop hits, American standards, folk songs and motion picture and theatrical compositions. Assembled over decades, its award-winning catalog includes over 65,000 songwriters and composers and a diverse range of genres including pop, rock, jazz, country, R&B, hip-hop, rap, reggae, Latin, folk, blues, symphonic, soul, Broadway, techno, alternative, gospel and other Christian music. Warner/Chappell also administers the music and soundtracks of several third-party television and film producers and studios, including Lucasfilm, Ltd., Hallmark Entertainment and Disney Music Publishing. Since 2012, Warner/Chappell has been making an effort to build up its film and TV music business, with the acquisitions of certain songs and recordings from numerous critically acclaimed films and TV shows. These acquisitions will help Warner/Chappell take advantage of the higher margins and strong synchronization and performance income in the TV/film space. The Company s production music library business includes Non-Stop Music, Groove Addicts Production Music Library, Carlin Recorded Music Library and 615 Music, and is collectively branded as Warner/Chappell Production Music.

**2. Basis of Presentation**

**Interim Financial Statements**

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. ( U.S. GAAP ) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine month periods ended June 30, 2013 are not necessarily indicative of the results that may be expected for the fiscal year ended September 30, 2013.

The consolidated balance sheet at September 30, 2012 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by U.S. GAAP for complete financial statements.

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For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2012 (File No. 001-32502).

**Basis of Consolidation**

The accompanying financial statements present the consolidated accounts of all entities in which the Company has a controlling voting interest and/or variable interest entities required to be consolidated in accordance with U.S. GAAP. All inter-company balances and transactions have been eliminated. Certain reclassifications have been made to the prior fiscal years consolidated financial statements to conform with the current fiscal-year presentation.

Financial Accounting Standards Board ( FASB ) Accounting Standards Codification ( ASC ) Topic 810, Consolidation ( ASC 810 ) requires the Company first evaluate its investments to determine if any investments qualify as a variable interest entity ( VIE ). A VIE is consolidated if the Company is deemed to be the primary beneficiary of the VIE, which is the party involved with the VIE that has both (i) the power to control the most significant activities of the VIE and (ii) either the obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE. If an entity is not deemed to be a VIE, the Company consolidates the entity if the Company has a controlling voting interest.

The Company maintains a 52-53 week fiscal year ending on the Friday nearest to each reporting date. As such, all references to June 30, 2013 and June 30, 2012 relate to the three-month periods ended June 28, 2013 and June 29, 2012, respectively. For convenience purposes, the Company continues to date its financial statements as of June 30.

The Company has performed a review of all subsequent events through the date the financial statements were issued, and has determined that other than as described in Note 12, no additional disclosures are necessary.

**New Accounting Pronouncements**

During the first quarter of fiscal 2013, the Company adopted ASU 2011-05, Presentation of Comprehensive Income. ASU 2011-05 requires entities to present items of net income and other comprehensive income either in one continuous statement, referred to as the statement of comprehensive income, or in two separate, but consecutive, statements of operations and other comprehensive income. The Company simultaneously adopted ASU 2011-12, Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. ASU 2011-12 defers the requirement to present components of reclassifications of comprehensive income on the statement of comprehensive income, with all other requirements of ASU 2011-05 unaffected. The adoption of these standard updates did not have a significant impact on the Company s financial statements, other than presentation.

During the first quarter of fiscal 2013, the Company adopted ASU 2011-08, Testing Goodwill for Impairment. ASU 2011-08 provides entities with an option to perform a qualitative assessment to determine whether further impairment testing is necessary. The adoption of this standard update did not have an impact on the Company s financial statements.

During the first quarter of fiscal 2013, the Company adopted ASU 2012-02, Intangibles-Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment, which provides entities with an option to perform a qualitative assessment to determine whether it is more likely than not that the indefinite-lived intangible asset is impaired. The adoption of this standard update did not have an impact on the Company s financial statements.

In December 2011, the FASB issued ASU 2011-11, Disclosures about Offsetting Assets and Liabilities. In January 2013, the FASB issued ASU 2013-01, Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities, to clarify which financial assets and financial liabilities are included within the scope of ASU 2011-11. These ASUs require additional quantitative and qualitative disclosures over financial instruments and derivative instruments that are offset on the balance sheet or subject to master netting arrangements. Both ASUs are effective for annual and interim reporting periods for fiscal years beginning on or after January 1, 2013. The adoption of these standards is not expected to have a significant impact on the Company s financial statements, other than presentation.

In February 2013, the FASB issued ASU 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. This ASU requires entities to disclose, in one place, information about the amounts reclassified out of accumulated other comprehensive income by component. ASU 2013-02 is effective for annual and interim reporting periods for fiscal years beginning after December 15, 2012. The adoption of this standard is not expected to have a significant impact on the Company s financial statements, other than disclosure.

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**3. Accumulated Other Comprehensive (Loss) Income**

Comprehensive (loss) income consists of net loss and other gains and losses affecting equity that, under U.S. GAAP, are excluded from net (loss) income. For the Company, the components of other comprehensive (loss) income primarily consist of foreign currency translation gains and losses and deferred gains and losses on financial instruments designated as hedges under FASB ASC Topic 815, *Derivatives and Hedging* ( ASC 815 ), which include foreign exchange contracts. The following summary sets forth the components of accumulated other comprehensive loss, net of related taxes (in millions):

| | Foreign Currency Translation Loss | Minimum Pension Liability | Deferred Gains (Losses) On Derivative Financial Instruments (in millions) | Accumulated Other Comprehensive Loss |
|---|---|---|---|---|
| **Balance at September 30, 2012** | **$ (54)** | **$ (6)** | **$ 1** | **$ (59)** |
| Activity through June 30, 2013 | (8) | | (2) | (10) |
| **Balance at June 30, 2013** | **$ (62)** | **$ (6)** | **$ (1)** | **$ (69)** |

**4. Goodwill and Intangible Assets**

**Goodwill**

The following analysis details the changes in goodwill for each reportable segment during the nine months ended June 30, 2013 (in millions):

| | Recorded Music | Music Publishing (in millions) | Total |
|---|---|---|---|
| **Balance at September 30, 2012** | **$ 916** | **$ 464** | **$ 1,380** |
| Acquisitions | 10 | | 10 |
| Dispositions | | | |
| Other adjustments | 3 | | 3 |
| **Balance at June 30, 2013** | **$ 929** | **$ 464** | **$ 1,393** |

The increase in goodwill during the nine months ended June 30, 2013 primarily related to the acquisition of recorded music assets.

The Company performs its annual goodwill impairment test in accordance with FASB ASC Topic 350, *Intangibles Goodwill and other* ( ASC 350 ) during the fourth quarter of each fiscal year. The Company will conduct an earlier review if events or circumstances occur that would suggest the carrying value of the Company s goodwill may not be recoverable. No indicators of impairment were identified during the current period that required the Company to perform an interim assessment or recoverability test.

**Other Intangible Assets**

Other intangible assets consist of the following (in millions):

| | June 30, 2013 | September 30, 2012 |
|---|---|---|
| | (in millions) | |
| Intangible assets subject to amortization: | | |
| Recorded Music catalog | $ 538 | $ 547 |
| Music Publishing copyrights | 1,521 | 1,508 |
| Artist and songwriter contracts | 657 | 667 |
| Trademarks | 7 | 7 |
| | 2,723 | 2,729 |
| Accumulated amortization | (366) | (230) |
| Total net intangible assets subject to amortization | 2,357 | 2,499 |
| Intangible assets not subject to amortization: | | |
| Trademarks and brands | 102 | 102 |
| Total net other intangible assets | $ 2,459 | $ 2,601 |

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**5. Debt**

**Debt Capitalization**

Long-term debt, including the current portion, consists of the following (in millions):

| | June 30, 2013 | September 30, 2012 |
|---|---|---|
| | (in millions) | |
| Old Revolving Credit Facility (a) | $ | $ |
| New Revolving Credit Facility (b) | 25 | |
| Term Loan Facility due 2020 Acquisition Corp (c) | 485 | |
| 9.5% Senior Secured Notes due 2016 Acquisition Corp (d) | | 1,151 |
| 9.5% Senior Secured Notes due 2016 Acquisition Corp (e) | | 156 |
| 6.00% Senior Secured Notes due 2021 Acquisition Corp | 450 | |
| 6.25% Senior Secured Notes due 2021 Acquisition Corp (f) | 205 | |
| 11.5% Senior Notes due 2018 Acquisition Corp (g) | 751 | 749 |
| 13.75% Senior Notes due 2019 Holdings | 150 | 150 |
| Total debt | $ 2,066 | $ 2,206 |
| Less: current portion | 29 | |
| Total long term debt | $ 2,037 | $ 2,206 |

(a) Reflects $60 million of commitments under the Old Revolving Credit Facility, less letters of credit outstanding of approximately $1 million at September 30, 2012. There were no loans outstanding under the Old Revolving Credit Facility as of September 30, 2012. The Old Revolving Credit Facility was retired in connection with the 2012 Refinancing (as described below) and replaced with the New Revolving Credit Facility.

(b) Reflects $150 million of commitments under the New Revolving Credit Facility, less letters of credit outstanding of approximately $1 million at June 30, 2013. There were $25 million of loans outstanding under the New Revolving Credit Facility as of June 30, 2013, all of which was included in the current portion of long term debt.

(c) Principal amount of $490 million less unamortized discount of $5 million. Of this amount, $4 million, representing the scheduled amortization of the Term Loan, was included in the current portion of long term debt at June 30, 2013.

(d) Face amount of $1.1 billion plus unamortized premiums of $51 million at September 30, 2012. All outstanding amounts were repaid in full as part of the 2012 Refinancing.

(e) Face amount of $150 million plus unamortized premiums of $6 million at September 30, 2012. All outstanding amounts were repaid in full as part of the 2012 Refinancing.

(f) Face amount of 158 million. Amount above represents the dollar equivalent of such notes at June 30, 2013.

(g) Face amount of $765 million less unamortized discounts of $14 million and $16 million at June 30, 2013 and September 30, 2012, respectively.

***2012 Debt Refinancing***

On November 1, 2012, the Company completed a refinancing (the 2012 Refinancing ) of its then outstanding senior secured notes due 2016 (the Old Secured Notes ). In connection with the 2012 Refinancing, the Company issued new senior secured notes consisting of $500 million aggregate principal amount of Senior Secured Notes due 2021 and 175 million aggregate principal amount of Senior Secured Notes due 2021 (the New Secured Notes ) and entered into new senior secured credit facilities consisting of a $600 million term loan facility (the Term Loan Facility ) and a $150 million revolving credit facility (the New Revolving Credit Facility and, together with Term Loan Facility, the New Senior Credit Facilities ). Acquisition Corp. is the borrower under the New Revolving Credit Facility (the Revolving Borrower ) and under the Term Loan Facility (the Term Loan Borrower ). The proceeds from the 2012 Refinancing, together with $101 million of the Company s available cash, were used to pay the total consideration due in connection with the tender offers for all of the Company s previously outstanding $1.250 billion 9.50% senior secured notes due 2016 (the Old Secured Notes ) as well as associated fees and expenses and to redeem all of the remaining notes not tendered in the tender offers. The Company also retired its existing $60 million Revolving Credit Facility (the Old Revolving Credit Facility ) in connection with the 2012 Refinancing, replacing it with the New Revolving Credit Facility. The Company also borrowed $31 million under the New Revolving Credit Facility as part of the 2012 Refinancing, which loans were repaid in full on December 3, 2012.

In connection with the 2012 Refinancing, the Company made a redemption payment of $1.377 billion, which included the repayment of the Company s previously outstanding $1.250 billion Old Secured Notes, tender/call premiums of $93 million and consent fees of approximately $34 million. The Company also paid approximately $45 million in accrued interest through the closing date.

The Company recorded a loss on extinguishment of debt of approximately $83 million in connection with the 2012 Refinancing in the nine months ended June 30, 2013, which represents the difference between the redemption payment and the carrying value of the debt at the refinancing date, which included the principal value of $1.250 billion, plus unamortized premiums of $55 million, less unamortized debt issuance costs of $11 million related to the Old Secured Notes.

***Modification of Term Loan Facility and Drawdown of Incremental Term Loan Facility***

On May 9, 2013, Acquisition Corp. prepaid $102.5 million in aggregate principal amount of term loans under the Term Loan Facility (the Term Loan Repayment ). Also on May 9, 2013, Acquisition Corp. entered into an amendment to the Term Loan Facility among Acquisition Corp, Holdings, the subsidiaries of Acquisition Corp. party thereto, Credit Suisse AG, as administrative agent, and the other financial institutions and lenders from time to time party thereto (the Term Loan Credit Agreement Amendment ), providing for a $820 million delayed draw senior secured term loan facility (the Incremental Term Loan Facility ). On July 1, 2013, Acquisition Corp. drew down the $820 million Incremental Term Loan Facility to fund the acquisition of PLG, pay fees, costs and expenses related to the acquisition and for general corporate purposes of Acquisition Corp. and its subsidiaries.

As part of the amendment to the Term Loan Facility, the interest rate, maturity date, and scheduled amortization were changed.

The loans under the Term Loan Credit Agreement Amendment bear interest at Term Loan Borrower s election at a rate equal to (i) the Term Loan LIBOR Rate plus 2.75% per annum or (ii) the Term Loan Base Rate plus 1.75% per annum. The Term Loan LIBOR Rate shall be deemed to be not less than 1.00%. If there is a payment default at any time, then the interest rate applicable to overdue principal and interest will be the rate otherwise applicable to such loan plus 2.0% per annum. Default interest will also be payable on other overdue amounts at a rate of 2.0% per annum above the amount that would apply to an alternative base rate loan.

The Term Loans under the amended Term Loan Facility will amortize in equal quarterly installments in aggregate annual amounts equal to 1.00% of the original principal amount of the amended Term Loan Facility with the balance payable on maturity date of the Term Loans. The next quarterly installment will be due December 31, 2013. The amended Term Loan Facility matures on July 1, 2020, with a springing maturity date on July 2, 2018 in the event that more than $153 million aggregate principal amount of the 11.50% Senior Notes of Acquisition Corp. due October 1, 2018 are outstanding on June 28, 2018 unless, on June 28, 2018, the senior secured indebtedness to EBITDA ratio of Acquisition Corp. is less than or equal to 3.50 to 1.00.

***Debt Redemptions***

On June 21, 2013, Acquisition Corp. redeemed 10% of its Senior Secured Notes due 2021, representing repayment of $50 million in aggregate principal amount of its outstanding 6.000% Senior Secured Notes due 2021 and €17.5 million in aggregate principal amount of its outstanding 6.250% Senior Secured Notes due 2021. The Company recorded a loss on extinguishment of debt of approximately $2 million, which represents the premium paid on early redemption.

***Interest Rates***

The loans under the Amended Revolving Credit Agreement bear interest at Revolving Borrower s election at a rate equal to (i) Revolving LIBOR Rate plus 2.00% per annum, or (ii) the Revolving Base Rate plus 1.00% per annum. If there is a payment default at any time, then the interest rate applicable to overdue principal will be the rate otherwise applicable to such loan plus 2.0% per annum. Default interest will also be payable on other overdue amounts at a rate of 2.0% per annum above the amount that would apply to an alternative base rate loan. The New Revolving Credit Facility bears a facility fee equal to 0.50%, payable quarterly in arrears, based on the daily commitments during the preceding quarter. The New Revolving Credit Facility bears customary letter of credit fees. Acquisition Corp. is also required to pay certain upfront fees to lenders and agency fees to the agent under the New Revolving Credit Facility, in the amounts and at the times agreed between the relevant parties.

***Maturity of New Revolving Credit Facility***

The New Revolving Credit Facility matures on November 1, 2017.

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*Maturities of Senior Notes*

As of June 30, 2013, there are no scheduled maturities until 2018 ($765 million). Thereafter, $805 million is scheduled to mature.

*Interest Expense*

Total interest expense, net was $47 million and $56 million for the three months ended June 30, 2013 and June 30, 2012, respectively and $149 million and $169 million for the nine months ended June 30, 2013 and June 30, 2012, respectively. The weighted-average interest rate of the Company s total debt was 8.1% and 10.5% at June 30, 2013 and June 30, 2012, respectively.

**6. Share-Based Compensation Plan**

The Company accounts for share-based payments as required by FASB ASC Topic 718, Compensation-Stock Compensation ( ASC 718 ). ASC 718 requires all share-based payments to employees to be recognized as compensation expense. Under the recognition provision of ASC 718, liability classified stock-based compensation costs are measured each reporting date until settlement. The Company s policy is to measure share-based compensation costs using the intrinsic value method instead of fair value as it is not practical to estimate the volatility of its share price.

Effective January 1, 2013, eligible individuals were invited to participate in the Senior Management Free Cash Flow Plan (the Plan ). Eligible individuals include any employee, consultant or officer of the Company or any of its affiliates, who is selected by the Company s compensation committee to participate in the Plan. Under the Plan, participants are allocated a specific portion of the Company s free cash flow to use to purchase the equivalent of Company stock through a purposely established LLC holding company. The Company s Board of Directors authorized the LLC (the LLC ) to purchase up to 82.1918 shares of the Company s common stock pursuant to the Plan; there are currently 55 shares issued and outstanding to the LLC. The Company will allocate shares to active participants each Plan year at the time that annual free cash flow bonuses for such Plan year are determined and may grant unallocated shares under the Plan to certain members of current or future management.

At the time that annual free cash flow bonuses for such Plan year are determined, a participant shall be granted and credited an equal number of deferred equity units and related matching equity units based on their respective allocation. Deferred equity units granted under the Plan generally will vest between one and seven years and the redemption price will equal the fair market value of the Company s stock on the date of the settlement. Matching equity units granted under the Plan generally will vest between three and seven years and the redemption price will equal the excess, if any, of the then fair market value of one Company fractional share over the grant date fair value. All deferred and matching equity units will be settled in three installments in December 2018, 2019, and 2020. The deferred units will be settled at the participant s election for cash equal to the fair market value or one fractional company share. The matching units will be settled for cash equal to the redemption price. In December 2020, all outstanding shares become mandatorily redeemable at the then fair market value. Due to this mandatory redemption clause, the Company has classified the awards under the Plan as liability instruments. Dividend distributions, if any, are also paid out on vested units and are calculated on the same basis as the Company s common shares. The Company has applied a graded (tranche-by-tranche) attribution method and expenses deferred stock-based compensation on an accelerated basis over the vesting period of the share award.

The following is a summary of the Company s share awards for the period ended June 30, 2013:

| | Deferred Equity Units | Matching Equity Units | Deferred Equity Units Weighted-Average Exercise Price | Matching Equity Units Weighted-Average Exercise Price | Deferred Equity Units Weighted-Average Grant-Date Intrinsic Value | Matching Equity Units Weighted-Average Grant-Date Intrinsic Value |
|---|---|---|---|---|---|---|
| **Unvested units at January 1, 2013** | | | $ | $ | $ | $ |
| Granted | 25 | 25 | 107.13 | 107.13 | 107.13 | 107.13 |
| Vested | | | | | | |
| Forfeited | (1) | (1) | 107.13 | 107.13 | 107.13 | 107.13 |
| **Unvested units at June 30, 2013** | **24** | **24** | **107.13** | **107.13** | **107.13** | **107.13** |

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The weighted-average grant date intrinsic value of share awards for the period ended June 30, 2013 was $107.13. There were no shares that vested in the period. There was no such activity in the comparable prior year period.

***Compensation Expense***

The Company recognized non-cash compensation expense related to its stock-based compensation plan of $4 million for the three months ended June 30, 2013 and $8 million for the nine months ended June 30, 2013. There was no such expense in the comparable prior year period. Of the $4 million, $3 million related to awards for employees and $1 million related to awards for non-employees for the quarter ended June 30, 2013. Of the $8 million, $6 million related to awards for employees and $2 million related to awards for non-employees.

In addition, as of June 30, 2013, the Company had approximately $18 million of unrecognized compensation costs related to its unvested share awards. The remaining weighted average period over which total compensation related to unvested awards is expected to be recognized is 2 years.

**7. Commitments and Contingencies**

*Pricing of Digital Music Downloads*

On December 20, 2005 and February 3, 2006, the Attorney General of the State of New York served the Company with requests for information in connection with an industry-wide investigation as to the pricing of digital music downloads. On February 28, 2006, the Antitrust Division of the U.S. Department of Justice served us with a Civil Investigative Demand, also seeking information relating to the pricing of digitally downloaded music. Both investigations were ultimately closed, but subsequent to the announcements of the investigations, more than thirty putative class action lawsuits were filed concerning the pricing of digital music downloads. The lawsuits were consolidated in the Southern District of New York. The consolidated amended complaint, filed on April 13, 2007, alleges conspiracy among record companies to delay the release of their content for digital distribution, inflate their pricing of CDs and fix prices for digital downloads. The complaint seeks unspecified compensatory, statutory and treble damages. On October 9, 2008, the District Court issued an order dismissing the case as to all defendants, including us. However, on January 12, 2010, the Second Circuit vacated the judgment of the District Court and remanded the case for further proceedings and on January 10, 2011, the Supreme Court denied the defendants petition for Certiorari.

Upon remand to the District Court, all defendants, including the Company, filed a renewed motion to dismiss challenging, among other things, plaintiffs state law claims and standing to bring certain claims. The renewed motion was based mainly on arguments made in defendants original motion to dismiss, but not addressed by the District Court. On July 18, 2011, the District Court granted defendants motion in part, and denied it in part. Notably, all claims on behalf of the CD-purchaser class were dismissed with prejudice. However, a wide variety of state and federal claims remain, for the class of Internet Music purchasers. The parties have filed amended pleadings complying with the court s order, and the case is currently in discovery. The Company intends to defend against these lawsuits vigorously, but is unable to predict the outcome of these suits. Regardless of the merits of the claims, this and any related litigation could continue to be costly, and divert the time and resources of management. The potential outcomes of these claims that are reasonably possible cannot be determined at this time and an estimate of the reasonably possible loss or range of loss cannot presently be made.

*Music Download Putative Class Action Suits*

Five putative class action lawsuits have been filed against the Company in Federal Court in the Northern District of California between February 2, 2012 and March 10, 2012. The lawsuits, which were brought by various recording artists, all allege that the Company has improperly calculated the royalties due to them for certain digital music sales under the terms of their recording contracts. The named plaintiffs purport to raise these claims on their own behalf and, as a putative class action, on behalf of other similarly situated artists. Plaintiffs base their claims on a previous ruling that held another recorded music company had breached the specific recording contracts at issue in that case through its payment of royalties for music downloads and ringtones. In the wake of that ruling, a number of recording artists have initiated suits seeking similar relief against all of the major record companies, including us. Plaintiffs seek to have the interpretation of the contracts in that prior case applied to their different and separate contracts.

On April 10, 2012, the Company filed a motion to dismiss various claims in one of the lawsuits, with the intention of filing similar motions in the remaining suits, on the various applicable response dates. Meanwhile, certain plaintiffs counsel moved to be appointed as interim lead counsel, and other plaintiffs counsel moved to consolidate the various actions. In a June 1, 2012 Order, the court consolidated the cases and appointed interim co-lead class counsel. Plaintiffs filed a consolidated, master complaint on August 21, 2012. All deadlines have been stayed until August 29, 2013 to allow for settlement of this dispute. If a settlement has not been reached by that date and if the parties agree that further settlement discussions would be fruitful, the parties can file a joint statement/stipulation seeking additional time for further settlement negotiations. In the alternative, the parties would file a joint statement/stipulation with the Court alerting the Court to the fact that settlement could not be reached and resetting a litigation schedule. Settlement discussions are ongoing. Regardless of the merits of the claims, this and any related litigation could continue to be costly, and divert the time and resources of management. Based on an evaluation of potential outcomes of these claims that are reasonably possible and an estimate of the reasonably possible loss or range of loss possible, the Company has recorded what it believes is an appropriate reserve related to these cases, which amount is not material.

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*Other Matters*

In addition to the matters discussed above, the Company is involved in various litigation and regulatory proceedings arising in the normal course of business. Where it is determined, in consultation with counsel based on litigation and settlement risks, that a loss is probable and estimable in a given matter, the Company establishes an accrual. In none of the currently pending proceedings is the amount of accrual material. An estimate of the reasonably possible loss or range of loss in excess of the amounts already accrued cannot be made at this time due to various factors typical in contested proceedings, including (1) the results of ongoing discovery; (2) uncertain damage theories and demands; (3) a less than complete factual record; (4) uncertainty concerning legal theories and their resolution by courts or regulators; and (5) the unpredictable nature of the opposing party and its demands. However, the Company cannot predict with certainty the outcome of any litigation or the potential for future litigation. As such, the Company continuously monitors these proceedings as they develop and adjusts any accrual or disclosure as needed. Regardless of the outcome, litigation could have an adverse impact on the Company, including the Company s brand value, because of defense costs, diversion of management resources and other factors and it could have a material effect on the Company s results of operations for a given reporting period.

**8. Derivative Financial Instruments**

**Foreign Currency Risk Management**

The Company uses derivative financial instruments, primarily foreign currency forward exchange contracts ( FX Contracts ) for the purpose of managing foreign currency exchange risk by reducing the effects of fluctuations in foreign currency exchange rates.

The Company enters into FX Contracts primarily to hedge its royalty payments and balance sheet items denominated in foreign currency, including Euro denominated debt. The Company applies hedge accounting to FX Contracts for cash flows related to royalty payments. During the quarter, the Company also entered into FX contracts to hedge the PLG acquisition purchase price from exchange rate fluctuations, which also qualified for hedge accounting. In conjunction with the completion of the Transaction (defined below), the contracts were settled with an immaterial impact. The Company records these FX Contracts in the consolidated balance sheet at fair value and changes in fair value are recognized in Other Comprehensive Income ( OCI ) for unrealized items and recognized in earnings for realized items. The Company elects to not apply hedge accounting to foreign currency exposures related to balance sheet items. The Company records these FX Contracts in the consolidated balance sheet at fair value and changes in fair value are immediately recognized in earnings. Fair value is determined by using observable market transactions of spot and forward rates (i.e., Level 2 inputs) which is discussed further in Note 11.

Netting provisions are provided for in existing International Swap and Derivative Association Inc. ( ISDA ) agreements in situations where the Company executes multiple contracts with the same counterparty. As a result, net assets or liabilities resulting from foreign exchange derivatives subject to these netting agreements are classified within other current assets or other current liabilities in the Company s consolidated balance sheets.

Historically, the Company has used, and continues to use, foreign exchange forward contracts and foreign exchange options primarily to hedge the risk that unremitted or future royalties and license fees owed to its domestic companies for the sale, or anticipated sale, of U.S.-copyrighted products abroad may be adversely affected by changes in foreign currency exchange rates. The Company focuses on managing the level of exposure to the risk of foreign currency exchange rate fluctuations on its major currencies, which include the Euro, British pound sterling, Japanese yen, Canadian dollar, Swedish krona and Australian dollar. In addition, the Company currently hedges foreign currency risk associated with financing transactions such as third-party and inter-company debt and other balance sheet items.

For royalty related hedges, the Company records foreign exchange contracts at fair value on its balance sheet and the related gains or losses on these contracts are deferred in equity (as a component of comprehensive loss). These deferred gains and losses are recognized in income in the period in which the related royalties and license fees being hedged are received and recognized in income. However, to the extent that any of these contracts are not considered to be perfectly effective in offsetting the change in the value of the royalties and license fees being hedged, any changes in fair value relating to the ineffective portion of these contracts are immediately recognized in income. For hedges of financing transactions and other balance sheet items, hedge gains and losses are taken directly to the statement of operations where there is an equal and offsetting entry related to the underlying exposure. Gains and losses on foreign exchange contracts generally are included as a component of other income (expense), net, in the Company s consolidated statement of operations.

As of June 30, 2013, the Company had outstanding hedge contracts for the sale of $295 million and the purchase of $1.014 billion of foreign currencies at fixed rates, which included the contract to hedge the PLG acquisition purchase price. As of June 30, 2013, the Company had $1 million of deferred losses in comprehensive loss

related to foreign exchange hedging. As of September 30, 2012, the Company had outstanding hedge contracts for the sale of $349 million and the purchase of $21 million of foreign currencies at fixed rates. As of September 30, 2012, the Company had $1 million of deferred gains in comprehensive loss related to foreign exchange hedging.

**Interest Rate Risk Management**

The Company has $2.066 billion of debt outstanding at June 30, 2013, of which $510 million is variable rate debt. As such, the Company is exposed to changes in interest rates. The Company currently manages this exposure through the fixed-to-floating debt ratio; at June 30, 2013, 75% of the Company s debt was at a fixed rate. In addition, at June 30, 2013, all of the Company s floating rate debt under our Term Loan Facility was subject to a LIBOR floor of 1.0%, which is in excess of the current LIBOR rate. The LIBOR floor has effectively turned these LIBOR loans into fixed-rate debt until such time as the LIBOR rate moves higher than the floor.

In addition to the $510 million of variable rate debt, the Company also had $1.556 billion of fixed-rate debt. Based on the level of interest rates prevailing at June 30, 2013, the fair value of this fixed-rate debt was approximately $1.725 billion. The fair value of the Company s debt instruments are determined using quoted market prices from less active markets or by using quoted market prices for instruments with identical terms and maturities; both approaches are considered a Level 2 measurement. Further, based on the amount of its fixed-rate debt, a 25 basis point increase or decrease in the level of interest rates would increase or decrease the fair value of the fixed-rate debt by approximately $11 million. This potential increase or decrease is based on the simplified assumption that the level of fixed-rate debt remains constant with an immediate across the board increase or decrease in the level of interest rates with no subsequent changes in rates for the remainder of the period.

The Company monitors its positions with, and the credit quality of, the financial institutions that are party to any of its financial transactions.

**9. Segment Information**

As discussed more fully in Note 1, based on the nature of its products and services, the Company classifies its business interests into two fundamental operations: Recorded Music and Music Publishing. Information as to each of these operations is set forth below. The Company evaluates performance based on several factors, of which the primary financial measure is operating income (loss) before non-cash depreciation of tangible assets and non-cash amortization of intangible assets ( OIBDA ). The Company has supplemented its analysis of OIBDA results by segment with an analysis of operating income (loss) by segment.

The accounting policies of the Company s business segments are the same as those described in the summary of significant accounting policies included in the Company s Annual Report on Form 10-K for the fiscal year ended September 30, 2012. The Company accounts for intersegment sales at fair value as if the sales were to third parties. While inter-company transactions are treated like third-party transactions to determine segment performance, the revenues (and corresponding expenses recognized by the segment that is counterparty to the transaction) are eliminated in consolidation, therefore, do not themselves impact the consolidated results. Segment information consists of the following (in millions):

| Three Months Ended | Recorded Music | Music Publishing | Corporate expenses and eliminations | Total |
|---|---|---|---|---|
| | | (in millions) | | |
| **June 30, 2013** | | | | |
| Revenues | $ 534 | $ 134 | $ (5) | $ 663 |
| OIBDA | 61 | 28 | (20) | 69 |
| Depreciation of property, plant and equipment | (8) | (1) | (4) | (13) |
| Amortization of intangible assets | (32) | (16) | | (48) |
| Operating income (loss) | $ 21 | $ 11 | $ (24) | $ 8 |
| **June 30, 2012** | | | | |
| Revenues | $ 517 | $ 138 | $ (4) | $ 651 |
| OIBDA | 58 | 24 | (16) | 66 |

| | | | | |
|---|---|---|---|---|
| Depreciation of property, plant and equipment | (7) | (1) | (4) | (12) |
| Amortization of intangible assets | (32) | (15) | | (47) |
| Operating income (loss) | $ 19 | $ 8 | $ (20) | $ 7 |

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| Nine Months Ended | Recorded Music | Music Publishing | Corporate expenses and eliminations | Total |
|---|---|---|---|---|
| | | (in millions) | | |
| **June 30, 2013** | | | | |
| Revenues | $ 1,745 | $ 377 | $ (15) | $ 2,107 |
| OIBDA | 262 | 97 | (62) | 297 |
| Depreciation of property, plant and equipment | (24) | (4) | (10) | (38) |
| Amortization of intangible assets | (97) | (46) | | (143) |
| Operating income (loss) | $ 141 | $ 47 | $ (72) | $ 116 |
| **June 30, 2012** | | | | |
| Revenues | $ 1,675 | $ 386 | $ (12) | $ 2,049 |
| OIBDA | 211 | 93 | (54) | 250 |
| Depreciation of property, plant and equipment | (22) | (4) | (11) | (37) |
| Amortization of intangible assets | (99) | (46) | | (145) |
| Operating income (loss) | $ 90 | $ 43 | $ (65) | $ 68 |

**10. Additional Financial Information**

**Cash Interest and Taxes**

The Company made interest payments of approximately $174 million and $193 million during the nine months ended June 30, 2013 and June 30, 2012, respectively. The decrease in cash interest is due to timing of interest payments resulting from the refinancing of debt in the current fiscal year, the financing at the time of the Merger and the decrease in the cost of debt. The Company paid approximately $18 million and $32 million of income and withholding taxes, net of refunds, during the nine months ended June 30, 2013 and June 30, 2012, respectively. The $32 million of cash tax payments during the nine months ended June 30, 2012 includes $15 million of a payment relating to the settlement of an income tax audit in Germany. This payment was fully reimbursed to the Company by Time Warner under the terms of the 2004 acquisition of substantially all of the interests of the Recorded Music and Music Publishing businesses of Time Warner Inc.

**11. Fair Value Measurements**

ASC 820 defines fair value as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity.

In addition to defining fair value, ASC 820 expands the disclosure requirements around fair value and establishes a fair value hierarchy for valuation inputs. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels which is determined by the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

Level 1 inputs are based upon unadjusted quoted prices for identical instruments traded in active markets.

Level 2 inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 inputs are generally unobservable and typically reflect management s estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques that include option pricing models, discounted cash flow models and similar techniques.

In accordance with the fair value hierarchy, described above, the following table shows the fair value of the Company s financial instruments that are required to be measured at fair value as of June 30, 2013 and September 30, 2012. Balances in other current and other non-current liabilities represent purchase obligations and contingent consideration related to our various acquisitions. Derivatives not designated as hedging instruments represent the balances in other current assets and other current liabilities below and the gains and losses on these financial instruments are included as a component of other (expense) income, net, in the statement of operations.

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| | Fair Value Measurements as of June 30, 2013 (Level 1) | (Level 2) | (Level 3) | Total |
|---|---|---|---|---|
| | | (in millions) | | |
| *Other Current Assets:* | | | | |
| Foreign Currency Forward Exchange Contracts (a) | $ | $ 5 | $ | $ 5 |
| *Other Current Liabilities:* | | | | |
| Foreign Currency Forward Exchange Contracts (a) | $ | $ (4) | $ | $ (4) |
| *Other Current Liabilities:* | | | | |
| Contractual Obligations (b) | $ | $ | $ (2) | $ (2) |
| *Other Non-Current Liabilities:* | | | | |
| Contractual Obligations (b) | $ | $ | $ (11) | $ (11) |
| **Total** | **$** | **$ 1** | **$ (13)** | **$ (12)** |

| | Fair Value Measurements as of September 30, 2012 (Level 1) | (Level 2) | (Level 3) | Total |
|---|---|---|---|---|
| | | (in millions) | | |
| *Other Current Assets:* | | | | |
| Foreign Currency Forward Exchange Contracts (a) | $ | $ | $ | $ |
| *Other Current Liabilities:* | | | | |
| Foreign Currency Forward Exchange Contracts (a) | $ | $ (5) | $ | $ (5) |
| *Other Non-Current Liabilities:* | | | | |
| Contractual Obligations (b) | $ | $ | $ (11) | $ (11) |
| **Total** | **$** | **$ (5)** | **$ (11)** | **$ (16)** |

(a) The fair value of the foreign currency forward exchange contracts is based on dealer quotes of market forward rates and reflects the amount that the Company would receive or pay at their maturity dates for contracts involving the same currencies and maturity dates.

(b) This represents purchase obligations and contingent consideration related to our various acquisitions. This is based on a discounted cash flow approach and it is adjusted to fair value on a recurring basis and any adjustments are included as a component of operating income in the statement of operations. These amounts were mainly calculated using unobservable inputs such as future earnings performance of our various acquisitions and the expected timing of the payment. The change represents the increase in contingent consideration on a previous acquisition.

The majority of the Company s non-financial instruments, which include goodwill, intangible assets, inventories, and property, plant, and equipment, are not required to be re-measured to fair value on a recurring basis. These assets are evaluated for impairment if certain triggering events occur. If such evaluation indicates that an impairment exists, the asset is written down to its fair value. In addition, an impairment analysis is performed at least annually for goodwill and indefinite-lived intangible assets.

**12. Subsequent Events**

*Acquisition of the Parlophone Label Group*

On February 6, 2013, the Company signed a definitive agreement to acquire the Parlophone Label Group from Universal Music Group, a division of Vivendi, for £487 million, subject to a closing working capital adjustment, in an all-cash transaction (the Transaction ) pursuant to a Share Sale and Purchase Agreement (the PLG Agreement ) by and among Warner Music Holdings Limited, an English company and wholly-owned subsidiary of the Company ( WM Holdings UK ), certain related entities identified in the PLG Agreement (such entities, together with WM Holdings UK, the Buyers ), Acquisition Corp., as Buyers Guarantor, and EGH1 BV, a Dutch company, EMI Group Holdings BV, a Dutch company, and Delta Holdings BV, a Dutch company, as Sellers (as defined therein) (collectively, the PLG Sellers ), and Universal International Music BV, a Dutch company, as Sellers Guarantor (as defined therein), pursuant to which the PLG Sellers have agreed to sell, and the Buyers have agreed to buy, the outstanding shares of capital stock of PLG Holdco Limited, an English company ( PLG Holdco ) and certain related entities identified in the PLG Agreement (such entities, together with PLG Holdco, PLG ).

On June 28, 2013, the parties to the PLG Agreement entered into a Deed of Variation, resulting in an Amended and Restated Share Sale and Purchase Agreement (the PLG Amended Agreement ). The PLG Amended Agreement provides for, among other amendments, a revision to the definition of Aggregate Payments to increase this amount from the consideration paid for the outstanding shares of capital stock in PLG Holdco and certain related entities identified in the PLG Amended Agreement to an amount that reflects the entire purchase price. The adjustment to this definition results in a greater potential cap on liability for the PLG Sellers in connection with certain claims that may be brought under the PLG Amended Agreement.

Pursuant to the PLG Amended Agreement, the Transaction was completed on July 1, 2013.

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*Drawdown of Incremental Term Loan Facility*

On July 1, 2013, Acquisition Corp. drew down the $820 million Incremental Term Loan Facility to fund the acquisition of PLG, pay fees, costs and expenses related to the acquisition and for general corporate purposes of Acquisition Corp. and its subsidiaries.

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**WARNER MUSIC GROUP CORP.**

**Supplementary Information**

**Consolidating Financial Statements**

The Company is the direct parent of Holdings, which is the direct parent of Acquisition Corp. Holdings has issued and outstanding the 13.75% Senior Notes due 2019 (the Holdings Notes ). In addition, Acquisition Corp. has issued and outstanding the 6.00% Senior Secured Notes due 2021, the 6.25% Senior Secured Notes due 2021, and the 11.50% Senior Notes due 2018 (together, the Acquisition Corp. Notes ).

The Holdings Notes are guaranteed by the Company. These guarantees are full, unconditional, joint and several. The following condensed consolidating financial statements are presented for the information of the holders of the Holdings Notes and present the results of operations, financial position and cash flows of (i) the Company, which is the guarantor of the Holdings Notes, (ii) Holdings, which is the issuer of the Holdings Notes, (iii) the subsidiaries of Holdings (Acquisition Corp. is the only direct subsidiary of Holdings) and (iv) the eliminations necessary to arrive at the information for the Company on a consolidated basis. Investments in consolidated or combined subsidiaries are presented under the equity method of accounting. The Company has revised its presentation for the Guarantor and Non-Guarantor Financial Information from what was filed in our Form 10-Q for June 30, 2012. The Company uses the equity method to account for its investment in its subsidiaries. The revised presentation reflects adjustments to certain equity, intercompany and investment balances primarily to properly reflect the impact of purchase accounting in the consolidating balance sheet. We have also revised the presentation of our statement of cash flows and reclassified the activity for our Parent Company from Operating Activities to Investing Activities and for our Guarantor subsidiaries from Operating Activities to Financing Activities. The principal elimination entries eliminate investments in subsidiaries and intercompany balances.

The Acquisition Corp. Notes are also guaranteed by the Company and, in addition, are guaranteed by all of Acquisition Corp. s domestic wholly owned subsidiaries. The secured notes are guaranteed on a senior secured basis and the unsecured notes are guaranteed on an unsecured senior basis. These guarantees are full, unconditional, joint and several. The following condensed consolidating financial statements are also presented for the information of the holders of the Acquisition Corp. Notes and present the results of operations, financial position and cash flows of (i) Acquisition Corp., which is the issuer of the Acquisition Corp. Notes, (ii) the guarantor subsidiaries of Acquisition Corp., (iii) the non-guarantor subsidiaries of Acquisition Corp. and (iv) the eliminations necessary to arrive at the information for Acquisition Corp. on a consolidated basis. Investments in consolidated subsidiaries are presented under the equity method of accounting. There are no restrictions on Acquisition Corp. s ability to obtain funds from any of its wholly owned subsidiaries through dividends, loans or advances.

The Company and Holdings are holding companies that conduct substantially all of their business operations through Acquisition Corp. Accordingly, the ability of the Company and Holdings to obtain funds from their subsidiaries is restricted by the indentures for the Acquisition Corp. Notes and the credit agreements for the Acquisition Corp. New Senior Credit Facilities, and, with respect to the Company, the indenture for the Holdings Notes.

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**WARNER MUSIC GROUP CORP.**

**Supplementary Information**

**Consolidating Balance Sheet (Unaudited)**

**June 30, 2013**

| | WMG Acquisition Corp. (issuer) | Guarantor Subsidiaries | Non-Guarantor Subsidiaries | Eliminations | WMG Acquisition Corp. Consolidated | WMG Holdings Corp. (issuer) | Warner Music Group Corp. | Eliminations | Warner Music Group Corp. Consolidated |
|---|---|---|---|---|---|---|---|---|---|
| | | | | | (in millions) | | | | |
| **Assets:** | | | | | | | | | |
| Current assets: | | | | | | | | | |
| Cash and equivalents | $ | $ 10 | $ 92 | $ | $ 102 | $ | $ | $ | $ 102 |
| Accounts receivable, net | | 144 | 165 | | 309 | | | | 309 |
| Inventories | | 10 | 15 | | 25 | | | | 25 |
| Royalty advances expected to be recouped within one year | | 73 | 46 | | 119 | | | | 119 |
| Deferred tax assets | | 36 | 15 | | 51 | | | | 51 |
| Other current assets | 2 | 15 | 44 | | 61 | | | | 61 |
| Total current assets | 2 | 288 | 377 | | 667 | | | | 667 |
| Royalty advances expected to be recouped after one year | | 89 | 56 | | 145 | | | | 145 |
| Investments in and advances to (from) consolidated subsidiaries | 2,839 | 1,021 | | (3,860) | | 923 | 776 | (1,699) | |
| Property, plant and equipment, net | | 97 | 38 | | 135 | | | | 135 |
| Goodwill | | 1,379 | 14 | | 1,393 | | | | 1,393 |
| Intangible assets subject to amortization, net | | 1,036 | 1,321 | | 2,357 | | | | 2,357 |
| Intangible assets not subject to amortization | | 75 | 27 | | 102 | | | | 102 |
| Due (to) from parent companies | | (50) | 50 | | | | | | |
| Other assets | 55 | 18 | 10 | | 83 | 8 | | | 91 |
| Total assets | $ 2,896 | $ 3,953 | $ 1,893 | $ (3,860) | $ 4,882 | $ 931 | $ 776 | $ (1,699) | $ 4,890 |
| **Liabilities and Deficit:** | | | | | | | | | |
| Current liabilities: | | | | | | | | | |
| Accounts payable | | $ 71 | $ 50 | $ | $ 121 | $ | $ | $ | $ 121 |
| Accrued royalties | | 588 | 429 | | 1,017 | | | | 1,017 |
| Accrued liabilities | 1 | 82 | 118 | | 201 | | | | 201 |
| Accrued interest | 51 | | | | 51 | 5 | | | 56 |
| Deferred revenue | | 64 | 62 | | 126 | | | | 126 |
| Current portion of long-term debt | 29 | | | | 29 | | | | 29 |
| Other current liabilities | | 14 | (8) | | 6 | | | | 6 |
| Total current liabilities | 81 | 819 | 651 | | 1,551 | 5 | | | 1,556 |
| Long-term debt | 1,887 | | | | 1,887 | 150 | | | 2,037 |
| Deferred tax liabilities, net | | 146 | 200 | | 346 | | | | |