TIME WARNER INC.
Form 10-Q
May 02, 2012
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 for the quarterly period ended March 31, 2012 or**

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 for the transition period from ____________________ to ____________________**

Commission file number 001-15062

TIME WARNER INC.

(Exact name of Registrant as specified in its charter)

Delaware	**13-4099534**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

One Time Warner Center

New York, NY 10019-8016

(Address of Principal Executive Offices) (Zip Code)

(212) 484-8000

(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 þ No ¨

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ 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. (Check one):

Large accelerated filer þ	Accelerated filer ¨
Non-accelerated filer ¨ (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 þ

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

Description of Class	Shares Outstanding as of April 24, 2012
Common Stock $.01 par value	959,915,926

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MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

INTRODUCTION

Management s discussion and analysis of results of operations and financial condition (MD&A) is a supplement to the accompanying consolidated financial statements and provides additional information on Time Warner Inc. s (Time Warner or the Company) businesses, current developments, financial condition, cash flows and results of operations. MD&A is organized as follows:

Overview. This section provides a general description of Time Warner s business segments, as well as recent developments the Company believes are important in understanding the results of operations and financial condition or in understanding anticipated future trends.

Results of operations. This section provides an analysis of the Company s results of operations for the three months ended March 31, 2012. This analysis is presented on both a consolidated and a business segment basis. In addition, a brief description of transactions and other items that affect the comparability of the results being analyzed is included.

Financial condition and liquidity. This section provides an analysis of the Company s financial condition as of March 31, 2012 and cash flows for the three months ended March 31, 2012.

Caution concerning forward-looking statements. This section provides a description of the use of forward-looking information appearing in this report, including in MD&A and the consolidated financial statements.

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MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

OVERVIEW

Time Warner is a leading media and entertainment company whose major businesses encompass an array of the most respected and successful media brands. Among the Company s brands are TNT, TBS, CNN, HBO, Cinemax, Warner Bros., New Line Cinema, *People*, *Sports Illustrated* and *Time*. During the three months ended March 31, 2012, the Company generated Revenues of $6.979 billion (up 4% from $6.683 billion in 2011), Operating Income of $1.247 billion (down 2% from $1.270 billion in 2011), Net Income attributable to Time Warner shareholders of $583 million (down 11% from $653 million in 2011) and Cash Provided by Operations of $416 million (down 50% from $825 million in 2011).

Time Warner Businesses

Time Warner classifies its operations into three reportable segments: Networks, Film and TV Entertainment and Publishing. For additional information regarding Time Warner s segments, refer to Note 11, Segment Information, in the accompanying consolidated financial statements. Effective for the first quarter of 2012, the Company changed the name of its Filmed Entertainment reportable segment to Film and TV Entertainment. This change did not affect the composition of the segment; accordingly, all prior period financial information related to this reportable segment was unaffected.

Networks. Time Warner s Networks segment consists of Turner Broadcasting System, Inc. (Turner) and Home Box Office, Inc. (Home Box Office). During the three months ended March 31, 2012, the Networks segment generated Revenues of $3.602 billion (51% of the Company s total Revenues) and $1.143 billion in Operating Income.

Turner operates domestic and international networks, including such recognized brands as TNT, TBS, truTV, CNN and Cartoon Network, which are among the leaders in advertising-supported television networks. The Turner networks generate revenues principally from providing programming to affiliates that have contracted to receive and distribute this programming and from the sale of advertising. Turner also operates various websites, including *CNN.com*, *NCAA.com*, *NASCAR.com* and *CartoonNetwork.com*, that generate revenues principally from the sale of advertising. Turner also provides online and mobile offerings for on demand viewing of programs on its networks and live streaming of its CNN and HLN networks to authenticated subscribers. As of March 31, 2012, Turner s online and mobile offerings were available to approximately 77 million subscribers.

Home Box Office operates the HBO and Cinemax multi-channel premium pay television services, with the HBO service ranking as the most widely distributed domestic multi-channel premium pay television service. Home Box Office generates revenues principally from providing programming to affiliates that have contracted to receive and distribute such programming to their customers who subscribe to the HBO or Cinemax services. As of March 31, 2012, HBO GO and MAX GO, Home Box Office s authenticated online services were available to essentially all of HBO s and Cinemax s respective domestic subscribers. An additional source of revenues for Home Box Office is the sale and licensing of its original programming, including *Game of Thrones*, *Boardwalk Empire* and *True Blood*.

The Company s Networks segment has been pursuing international expansion in select areas for the past several years, and the Company anticipates that international expansion will continue to be an area of focus at the Networks segment for the foreseeable future.

Film and TV Entertainment. Time Warner s Film and TV Entertainment segment consists of businesses managed by the Warner Bros. Entertainment Group (Warner Bros.) that principally produce and distribute theatrical motion pictures, television shows and videogames. During the three months ended March 31, 2012, the Film and TV Entertainment segment generated Revenues of $2.784 billion (38% of the Company s total Revenues) and $214 million in Operating Income.

The Film and TV Entertainment segment s theatrical product revenues are generated principally through rentals from theatrical exhibition of films, including the following recently released films: *Journey 2: The Mysterious Island, Sherlock Holmes: A Game of Shadows*, *Wrath of the Titans* and *Project X*, and subsequently through licensing fees received for the distribution of films on television networks and pay television programming services. Television product revenues are generated principally from the licensing of programs to television networks and pay television programming services. The segment also generates revenues for both its theatrical and television product through home video distribution on DVD and Blu-ray Discs and in various digital formats (e.g., electronic sell through and video-on-demand). In addition, the segment

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generates revenues through the distribution of videogames.

Warner Bros. continues to be an industry leader in the television content business. For the 2011-2012 broadcast season, Warner Bros. produced more than 30 scripted primetime series, with at least three series for each of the five broadcast networks (including *The Big Bang Theory*, *2 Broke Girls*, *Fringe*, *The Mentalist*, *The Middle*, *Mike & Molly*, *Person of Interest*, *Suburgatory*, *Two and a Half Men* and *Vampire Diaries*) and original series for cable television networks (including *The Closer*, *Pretty Little Liars*, *Rizzoli & Isles* and *Southland*). Internationally, Warner Bros. operates a group of local television production companies in the U.K. and the Netherlands that focus on developing non-scripted programs and formats that can be sold internationally and adapted for sale in the U.S. Warner Bros. has also begun to create locally produced versions of programs owned by the studio and to develop original local television programming.

The distribution of DVDs has been one of the largest drivers of the segment s revenues and profits over the last several years. However, in recent years, home video revenues have declined as a result of several factors, including consumers shifting to subscription rental services and discount rental kiosks, which generate significantly less revenue per transaction for the Company than DVD sales; the general economic downturn in the U.S. and many regions around the world; increasing competition for consumer discretionary time and spending; piracy; and the maturation of the standard definition DVD format. Reduced consumer spending on DVDs is being partially offset by growing sales of high definition Blu-ray Discs and increased sales through electronic delivery (particularly video-on-demand), which have higher incremental gross margins than standard definition DVDs. The decline in consumer spending on DVDs is also being partially offset by the licensing of theatrical and television content to subscription video-on-demand providers.

Publishing. Time Warner s Publishing segment consists principally of Time Inc. s magazine publishing and related websites, book publishing businesses and marketing services businesses. During the three months ended March 31, 2012, the Publishing segment generated Revenues of $773 million (11% of the Company s total Revenues) and $4 million in Operating Loss.

As of March 31, 2012, Time Inc. published 21 magazines in the U.S., including *People*, *Sports Illustrated* and *Time*, and over 70 magazines outside the U.S. All 21 of Time Inc. s U.S. magazines are available as tablet editions. The Publishing segment generates revenues primarily from the sale of advertising, magazine subscriptions and newsstand sales.

Since the fourth quarter of 2010, Turner has managed the *SI.com* and *Golf.com* websites, including selling all advertising for the websites, and in exchange Time Inc. has received a license fee from Turner. Beginning in the second quarter of 2012, Time Inc. will assume management of these websites, sell all advertising and no longer receive a license fee from Turner. This change will not impact the Company s consolidated results of operations.

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RESULTS OF OPERATIONS

Transactions and Other Items Affecting Comparability

As more fully described herein and in the related notes to the accompanying consolidated financial statements, the comparability of Time Warner s results has been affected by transactions and certain other items in each period as follows (millions):

	88888888888888	88888888888888
	Three Months Ended March 31, 2012	2011
Asset impairments	$ (52)	$ -
Gain (loss) on operating assets	(42)	3
Other	(10)	(8)
Impact on Operating Income	(104)	(5)
Investment gains (losses), net	(9)	4
Amounts related to the separation of Time Warner Cable Inc.	(1)	4
Pretax impact	(114)	3
Income tax impact of above items	36	3
Impact of items on net income attributable to Time Warner Inc. shareholders	$ (78)	$ 6

In addition to the items affecting comparability described above, the Company incurred Restructuring and severance costs of $26 million and $30 million for the three months ended March 31, 2012 and 2011, respectively. For further discussion of Restructuring and severance costs, refer to Consolidated Results and Business Segment Results.

Asset Impairments

For the three months ended March 31, 2012, the Company recognized $52 million of noncash charges at the Networks segment primarily related to certain receivables, inventories and long-lived assets in connection with Turner s decision in the first quarter of 2012 to shut down its general entertainment network in India.

Gain (Loss) on Operating Assets

For the three months ended March 31, 2012, the Company recognized a loss on operating assets of $42 million at the Publishing segment in connection with the sale in the first quarter of 2012 of the school fundraising business, QSP (the QSP Business).

For the three months ended March 31, 2011, the Company recognized a $3 million gain at the Film and TV Entertainment segment related to contingent consideration for certain prior acquisitions.

Other

Other reflects legal and other professional fees related to the defense of securities litigation matters for former employees totaling $2 million for each of the three months ended March 31, 2012 and 2011. Other also reflects external costs related to mergers, acquisitions or dispositions of $8 million and $6 million for the three months ended March 31, 2012 and 2011, respectively.

Investment Gains (Losses), Net

For the three months ended March 31, 2012 and 2011, the Company recognized $9 million of miscellaneous investment losses and $4 million of miscellaneous investment gains, net, respectively.

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MANAGEMENT S DISCUSSION AND ANALYSIS

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Amounts Related to the Separation of Time Warner Cable Inc.

For the three months ended March 31, 2012 and 2011, the Company recognized $1 million of other loss and $4 million of other income, respectively, related to the expiration, exercise and net change in the estimated fair value of Time Warner equity awards held by Time Warner Cable Inc. (TWC) employees, which has been reflected in Other loss, net in the accompanying Consolidated Statement of Operations.

Income Tax Impact

The income tax impact reflects the estimated tax provision or tax benefit associated with each item affecting comparability. Such estimated tax provisions or tax benefits vary based on certain factors, including the taxability or deductibility of the items and foreign tax on certain transactions.

Consolidated Results

The following discussion provides an analysis of the Company s results of operations and should be read in conjunction with the accompanying Consolidated Statement of Operations.

Revenues. The components of Revenues are as follows (millions):

	888888888888	888888888888	888888888888
	Three Months Ended March 31,		
	2012	2011	% Change
Subscription	$ 2,471	$ 2,368	4%
Advertising	1,472	1,431	3%
Content	2,861	2,733	5%
Other	175	151	16%
Total revenues	$ 6,979	$ 6,683	4%

The increase in Subscription revenues primarily related to an increase at the Networks segment. The increase in Advertising revenues was primarily due to an increase at the Networks segment, partially offset by a decrease at the Publishing segment. The increase in Content revenues was due primarily to an increase at the Film and TV Entertainment segment, partially offset by a decrease at the Networks segment. Each of the revenue categories is discussed in greater detail by segment in Business Segment Results.

Costs of Revenues. For the three months ended March 31, 2012, Costs of revenues increased to $3.976 billion from $3.727 billion for the three months ended March 31, 2011 driven primarily by increases at the Film and TV Entertainment and Networks segments. The segment variations are discussed in Business Segment Results.

Selling, General and Administrative Expenses. For three months ended March 31, 2012, Selling, general and administrative expenses decreased 1% to $1.575 billion from $1.591 billion for the three months ended March 31, 2011, primarily related to a decrease at the Networks segment. The segment variations are discussed in Business Segment Results.

Included in Costs of revenues and Selling, general and administrative expenses is depreciation expense of $154 million and $163 million for the three months ended March 31, 2012 and 2011, respectively.

Amortization Expense. Amortization expense decreased to $61 million for the three months ended March 31, 2012 from $68 million for the three months ended March 31, 2011.

Restructuring and Severance Costs. For the three months ended March 31, 2012, the Company incurred Restructuring and severance costs of $26 million, primarily related to employee terminations and other exit activities, consisting of $14 million at the Networks segment, $6 million at the Film and TV Entertainment segment and $6 million at the Publishing segment.

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For the three months ended March 31, 2011, the Company incurred Restructuring and severance costs of $30 million, primarily related to employee terminations and other exit activities, consisting of $12 million at the Networks segment, $6 million at the Film and TV Entertainment segment and $12 million at the Publishing segment.

Operating Income. Operating Income decreased to $1.247 billion for the three months ended March 31, 2012 from $1.270 billion for the three months ended March 31, 2011. Excluding the items noted under Transactions and Other Items Affecting Comparability totaling $104 million and $5 million of expense for the three months ended March 31, 2012 and 2011, respectively, Operating Income increased $76 million, reflecting increases at the Film and TV Entertainment and Networks segments. The segment variations are discussed under Business Segment Results.

Interest Expense, Net. For the three months ended March 31, 2012, Interest expense, net, increased to $320 million from $274 million for the three months ended March 31, 2011 due to higher average debt in 2012 reflecting the issuance of $3 billion of debt securities in April and November 2011.

Other Loss, Net. Other loss, net detail is shown in the table below (millions):

	88888888888		88888888888	
	Three Months Ended March 31,			
	2012		**2011**	
Investment gains (losses), net	$	(9)	$	4
Amounts related to the separation of TWC		(1)		4
Loss from equity method investees		(8)		(18)
Other		18		(4)
Other loss, net	$	-	$	(14)

Investment gains (losses), net and amounts related to the separation of TWC are discussed under Transactions and Other Items Affecting Comparability. The remaining changes in Other loss, net for the three months ended March 31, 2012 were due to an adjustment to reduce liability for deferred compensation and lower losses from equity method investees.

Income Tax Provision. Income tax provision increased to $346 million for the three months ended March 31, 2012 from $331 million for the three months ended March 31, 2011. The Company s effective tax rate was 37% and 34% for the three months ended March 31, 2012 and 2011, respectively. This change was primarily due to an increase in tax reserves.

Net Income. Net income decreased to $581 million for the three months ended March 31, 2012 from $651 million for the three months ended March 31, 2011. Excluding the items noted under Transactions and Other Items Affecting Comparability totaling $78 million of expense and $6 million of income for the three months ended March 31, 2012 and 2011, respectively, Net income increased $14 million, primarily reflecting higher Operating Income, partially offset by higher interest expense.

Net Loss Attributable to Noncontrolling Interests. For each of the three months ended March 31, 2012 and 2011, Net loss attributable to noncontrolling interests was $2 million.

Net Income Attributable to Time Warner Inc. Shareholders. Net income attributable to Time Warner Inc. shareholders was $583 million and $653 million for the three months ended March 31, 2012 and 2011, respectively. Basic and Diluted net income per common share attributable to

Time Warner Inc. common shareholders were $0.60 and $0.59, respectively, for the three months ended March 31, 2012 and were $0.59 and $0.59, respectively, for the three months ended March 31, 2011.

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OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Business Segment Results

Networks. Revenues and Operating Income of the Networks segment for the three months ended March 31, 2012 and 2011 are as follows (millions):

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	Three Months Ended March 31,		
	2012	**2011**	**% Change**
Revenues:			
Subscription	$ 2,154	$ 2,055	5%
Advertising	1,096	1,032	6%
Content	306	372	(18%)
Other	46	37	24%
Total revenues	3,602	3,496	3%
Costs of revenues[(a)]	(1,739)	(1,647)	6%
Selling, general and administrative[(a)]	(567)	(582)	(3%)
Asset impairments	(52)	-	NM
Restructuring and severance costs	(14)	(12)	17%
Depreciation	(79)	(83)	(5%)
Amortization	(8)	(10)	(20%)
Operating Income	$ 1,143	$ 1,162	(2%)

[(a)] Costs of revenues and Selling, general and administrative expenses exclude depreciation.

Subscription revenues increased primarily due to a $93 million increase in domestic subscription revenues reflecting higher domestic subscription rates.

The increase in Advertising revenues reflected domestic growth of $58 million driven by strong pricing and The National Collegiate Athletic Association Division I Men s Basketball Championship (the NCAA Tournament) events, due in part to the timing of games.

The decrease in Content revenues was due primarily to lower licensing revenues from original programming.

The components of Costs of revenues for the Networks segment are as follows (millions):

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	Three Months Ended March 31, 2012	2011	% Change
Programming costs:			
Originals and sports	$ 939	$ 828	13%
Acquired films and syndicated series	426	454	(6%)
Total programming costs	1,365	1,282	6%
Other direct operating costs	374	365	2%
Costs of revenues[a]	$ 1,739	$ 1,647	6%

[a] Costs of revenues exclude depreciation.

The increase in Costs of revenues was driven by higher programming costs. The increase in programming costs reflected higher costs for originals and sports programming, which included a $35 million impairment related to the cancellation of an original series, as well as higher NCAA Tournament programming costs due in part to the timing of games. This increase was partially offset by lower programming costs for acquired programming.

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As previously noted under Transactions and Other Items Affecting Comparability, the results for the three months ended March 31, 2012 included a $58 million charge related to Turner s decision in the first quarter of 2012 to shut down its general entertainment network in India. This charge consisted of $52 million of noncash charges primarily related to certain receivables, inventories and long-lived assets and a $6 million charge related to exit costs. The Networks segment expects to incur an additional noncash charge of approximately $70 million to $80 million in the second quarter of 2012 following the completion of the shutdown.

Operating Income decreased primarily due to higher Costs of revenues and the $58 million charge related to the shutdown of Turner s general entertainment network in India, partially offset by higher Revenues.

Film and TV Entertainment. Revenues and Operating Income of the Film and TV Entertainment segment for the three months ended March 31, 2012 and 2011 are as follows (millions):

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	Three Months Ended March 31,		
	2012	**2011**	**% Change**
Revenues:			
Subscription	$ 28	$ 18	56%
Advertising	13	11	18%
Content	2,685	2,535	6%
Other	58	40	45%
Total revenues	2,784	2,604	7%
Costs of revenues[a]	(2,008)	(1,880)	7%
Selling, general and administrative[a]	(466)	(468)	-
Gain on operating assets	-	3	(100%)
Restructuring and severance costs	(6)	(6)	-
Depreciation	(46)	(48)	(4%)
Amortization	(44)	(47)	(6%)
Operating Income	$ 214	$ 158	