TIME WARNER INC.
Form 10-Q
November 02, 2016
Table of Contents

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 September 30, 2016 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 October 25, 2016**
Common Stock $.01 par value	771,129,567

Table of Contents

TIME WARNER INC.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

AND OTHER FINANCIAL INFORMATION

Table of Contents

TIME WARNER INC.

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 and nine months ended September 30, 2016. 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 September 30, 2016 and cash flows for the nine months ended September 30, 2016.

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.

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, Adult Swim, Cartoon Network, CNN, HBO, Cinemax, Warner Bros. and New Line Cinema. During the nine months ended September 30, 2016, the Company generated Revenues of $21.427 billion (up 2% from $21.039 billion in 2015), Operating Income of $5.856 billion (up 7% from $5.479 billion in 2015), Income from continuing operations of $3.597 billion (up 22% from $2.938 billion in 2015), Net Income attributable to Time Warner shareholders of $3.633 billion (up 22% from $2.976 billion in 2015) and Cash provided by operations of $3.534 billion (up 18% from $2.997 billion in 2015).

Time Warner Businesses

Time Warner classifies its operations into three reportable segments: Turner, Home Box Office and Warner Bros. For additional information regarding Time Warner s segments, refer to Note 14, Segment Information, to the accompanying consolidated financial statements.

Turner. The Turner segment consists of businesses managed by Turner Broadcasting System, Inc. (Turner). During the nine months ended September 30, 2016, the Turner segment recorded Revenues of $8.526 billion (39% of the Company s total Revenues) and Operating Income of $3.531 billion.

Turner operates domestic and international television networks and related properties that offer entertainment, sports, kids and news programming on television and digital platforms for consumers around the world. The Turner networks and related properties include TNT, TBS, Adult Swim, truTV, Turner Classic Movies, Turner Sports, Cartoon Network, Boomerang, CNN and HLN. The Turner networks generate revenues principally from licensing programming to affiliates that have contracted to receive and distribute this programming to subscribers, from the sale of advertising and from licensing its original programming, including to over-the-top (OTT) services such as subscription-video-on-demand (SVOD) services, and its brands and characters for consumer products and other business ventures. Turner s programming is available to audiences for viewing live and on demand across television, mobile devices and other digital platforms through services provided by affiliates and on Turner s digital properties. Turner also owns and operates various digital media businesses, including *Bleacher Report*; the CNN digital properties, including *CNNgo*, *CNN.com* and *CNNMoney.com*; and other digital properties associated with its networks, all of which generate revenues principally from the sale of advertising and sponsorships. In addition, Turner manages and operates sports-related digital properties in conjunction with associated television rights, such as *NBA Digital* and *NCAA.com*, which also generate revenues primarily from the sale of advertising and sponsorships.

Table of Contents

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Home Box Office. The Home Box Office segment consists of businesses managed by Home Box Office, Inc. (Home Box Office). During the nine months ended September 30, 2016, the Home Box Office segment recorded Revenues of $4.399 billion (21% of the Company s total Revenues) and Operating Income of $1.488 billion.

Home Box Office operates the HBO and Cinemax multichannel premium pay television services, with the HBO service ranking as the most widely distributed multichannel premium pay television service. HBO- and Cinemax-branded premium pay, basic tier television or OTT services are distributed in over 60 countries in Latin America, Asia and Europe.

In the U.S., Home Box Office generates revenues principally from licensing programming to affiliates that have contracted to receive and distribute such programming to their customers who subscribe to the HBO or Cinemax services. HBO and Cinemax programming is available in the U.S. to subscribers of affiliates for viewing on Home Box Office s main HBO and Cinemax channels and its multiplex channels, through its on demand services, HBO On Demand and Cinemax On Demand, and through its broadband-delivered on demand services, HBO GO and MAX GO. HBO GO and MAX GO are available on a variety of digital platforms, including mobile devices, gaming consoles and internet-connected streaming devices and televisions. In April 2015, Home Box Office launched HBO NOW, an OTT service available to consumers in the U.S. Home Box Office s agreements with its domestic affiliates are typically long-term arrangements that provide for annual service fee increases and marketing support. While fees to Home Box Office under affiliate agreements are generally based on the number of subscribers served by the affiliates, the relationship between subscriber totals and the amount of revenues earned depends on the specific terms of the applicable agreement, which may include basic and/or pay television subscriber thresholds, volume discounts and other performance-based discounts. Marketing and promotional activities intended to retain existing subscribers and acquire new subscribers may also impact revenue earned.

Internationally, Home Box Office generates subscription revenues by providing country-specific HBO and Cinemax premium pay and basic tier television services to international affiliates that have contracted to receive and distribute such services to their local customers. In some countries, Home Box Office also generates subscription revenues from OTT services that are distributed to consumers either directly or through third parties. Additional sources of revenues for Home Box Office are the home entertainment sales of its original programming, including *Game of Thrones*, *True Detective*, *True Blood* and *Girls*, via physical and digital formats and the licensing of its original programming to OTT services, including SVOD services, and international television networks.

Warner Bros. The Warner Bros. segment consists of businesses managed by Warner Bros. Entertainment Inc. (Warner Bros.) that principally produce and distribute television shows, feature films and videogames. Warner Bros. television, film and videogame businesses benefit from a shared infrastructure, including shared production, distribution, marketing and administrative functions and resources. During the nine months ended September 30, 2016, the Warner Bros. segment recorded Revenues of $9.169 billion (40% of the Company s total Revenues) and Operating Income of $1.160 billion.

Warner Bros. is a leader in television production and distribution. For the 2016/2017 season, Warner Bros. is producing over 65 original series in the U.S., including (i) at least three series for each of the five broadcast networks (including *2 Broke Girls*, *Arrow*, *The Bachelor*, *The Big Bang Theory*, *Blindspot*, *DC s Legends of Tomorrow*, *The Flash*, *Gotham*, *Little Big Shots*, *Lucifer*, *The Middle*, *Mom*, *Supergirl*, *Supernatural*, *Vampire Diaries* and *The Voice*), (ii) series for basic cable networks (including *Animal Kingdom*, *People of Earth* and *Pretty Little Liars*), (iii) series for premium pay television services (including *The Leftovers*, *Shameless* and *Westworld*), (iv) series for SVOD services (including *Fuller House*, *Gilmore Girls: A Year in the Life* and *Longmire*), (v) series for first-run syndication (including *The Ellen DeGeneres Show*, *Extra*, *The Real* and *TMZ*) and (vi) animated series for Cartoon Network and Adult Swim (including *Be Cool, Scooby Doo!*, *Mike Tyson Mysteries*, *Teen Titans Go!* and *Wabbit*). Warner Bros. also licenses the rights to many of its U.S. original television series in international territories. Outside the U.S., Warner Bros. has a global network of production companies in many countries (located across Europe and South America and in Australia and New Zealand), which allows Warner Bros. to develop programming specifically tailored for the audiences in these territories. These local production companies also focus on developing non-scripted programs and formats that can be adapted and sold internationally and in the U.S. Warner Bros. generates television product revenues principally from the licensing of programs to broadcast and cable television networks and premium pay television and OTT services, including SVOD services.

Warner Bros. is a leader in the feature film industry and produces feature films under its Warner Bros. and New Line Cinema banners. The Warner Bros. segment s theatrical product revenues are generated principally through rental fees from theatrical

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

exhibition of feature films, including the following recently released films: *The Accountant*, *Barbershop: The Next Cut*, *Batman v Superman: Dawn of Justice*, *Central Intelligence*, *The Conjuring 2*, *The Legend of Tarzan, Lights Out*, *Me Before You*, *Storks, Suicide Squad* and *Sully* and subsequently through licensing fees received from the distribution of films on premium pay television, broadcast and cable television networks and OTT services, including SVOD services.

Warner Bros. is a leader in the home entertainment and videogame industries. The segment generates television and theatrical product revenues from the distribution of television and theatrical product in various physical and digital formats (e.g., electronic sell-through (EST) and video-on-demand). In addition, the segment generates revenues through the development and distribution of videogames, including the following recently released videogames: *LEGO Marvel s Avengers*, *LEGO Star Wars: The Force Awakens* and *Mortal Kombat XL.*

The distribution and sale of home entertainment product in physical formats is a large contributor to the segment s revenues and profits. For the past several years, sales of home entertainment product in physical formats have declined as the home entertainment industry has been undergoing significant changes as it transitions from the physical distribution of film and television content via physical discs to the electronic delivery of such content. Several factors have contributed to this decline, including consumers shifting to OTT services, which generate significantly less revenue per transaction for the Company than sales of home entertainment product in physical formats; changing retailer initiatives and strategies (e.g., reduction of floor space devoted to home entertainment product in physical formats); retail store closures; increasing competition for consumer discretionary time and spending; and piracy. During the first nine months of 2016, across the home entertainment industry, consumer spending on home entertainment product in physical formats continued to decline and consumer spending on electronic delivery continued to increase. The electronic delivery of film and television content is growing and becoming more important to the Warner Bros. segment, which has helped to offset some of the decline in sales of home entertainment product in physical formats.

Television Industry

The television industry is continuing to evolve, with changes in technology, rapid growth in new video services, and a corresponding increase in overall video content consumption and shift in consumer viewing patterns. Consumers are watching an increasing amount of programming on-demand and across a wide variety of services and devices, including smartphones, tablets, PCs and internet-connected televisions. Over the past few years, the number of multichannel video service (MVPD) subscribers in the U.S. declined slightly, and the Company expects further modest declines. To counteract this trend, some MVPD providers are placing greater emphasis on selling smaller bundles of cable networks, resulting in higher subscriber declines for most individual networks than for MVPDs in total.

At the same time, the penetration of broadband and internet-connected devices has grown, which has led to a growing number and variety of internet-delivered video services that do not require a traditional MVPD subscription or MVPD provider set-top box hardware. These include SVOD services such as Amazon Prime, Hulu and Netflix, which have continued to increase their number of subscribers and have been, and are expected to continue, making significant investments in acquired and original programming. Some television networks have launched OTT services, such as HBO NOW. In addition, MVPD providers as well as media and technology companies have launched, or have announced that they will launch, virtual MVPDs, which offer bundles of networks delivered via the internet. Ad-supported broadband video services, such as those offered through YouTube and Facebook, also have continued to gain in popularity.

As a result of these changes, consumers have more options for obtaining video content, including lower-cost alternatives. At the same time, however, the combination of new competitors, changes in viewing habits and declines in MVPD subscribers has negatively affected overall television ratings and, as a result, television advertising revenues for the industry and certain of the Company s networks. There also has been a corresponding shift of advertising dollars to non-traditional video outlets.

To address these changes, the Company s strategy over the past few years has focused on strengthening its position within the traditional TV ecosystem, enhancing the value of traditional pay television subscriptions for consumers, and pursuing new opportunities outside the traditional TV ecosystem. As part of this strategy, the Company plans to continue increasing its investment in high-quality distinctive programming to enhance the value of its networks. The Company is also working to enhance the value to consumers of the traditional MVPD bundle and capitalize on the shift in consumption habits in a number of ways, including by expanding the amount of its content that is available on demand and supporting the development of better user interfaces for on-demand multiplatform viewing. The Company is also pursuing a number of initiatives to capitalize on the new opportunities presented by these changes, including launching, investing in, and obtaining distribution through OTT services, including through

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

virtual MVPDs, as well as investing in short-form content production and digital-first news and entertainment networks. In addition, Turner has introduced new advertising products that provide greater data analytic tools and targeting capabilities to advertisers in order to compete more effectively with non-traditional outlets.

Recent Developments

AT&T and Time Warner Merger Agreement

On October 22, 2016, Time Warner entered into an Agreement and Plan of Merger (the Merger Agreement) with AT&T Inc. (AT&T), pursuant to which Time Warner will combine with AT&T in a stock-and-cash transaction. The Merger Agreement has been approved unanimously by the boards of directors of both companies. Subject to the conditions in the Merger Agreement, at the effective time of the merger, Time Warner s stockholders will receive $107.50 per share under the terms of the Merger Agreement, consisting of $53.75 per share in cash and $53.75 per share in AT&T stock. The stock portion will be subject to a collar such that Time Warner stockholders will receive 1.437 AT&T shares if AT&T s stock price is below $37.411 at closing and 1.300 AT&T shares if AT&T s stock price is above $41.349 at closing. If AT&T s stock price at closing is between $37.411 and $41.349, Time Warner stockholders will receive a number of shares between 1.300 and 1.437, equal to $53.75 in value. The merger is subject to approval by Time Warner stockholders and the receipt of certain antitrust and other regulatory consents. The transaction is expected to close before year-end 2017. Should Time Warner terminate the Merger Agreement in specified circumstances, including in order to consummate a competing transaction, Time Warner will be required to pay AT&T a termination fee equal to $1.725 billion.

In connection with entering into the Merger Agreement, the Company granted a total of 4.8 million special retention restricted stock units (Special Retention RSUs) to certain employees of Time Warner and its divisions, including all executive officers of Time Warner other than its Chairman and CEO, on October 24, 2016. Half of the Special Retention RSUs will vest 25% per year on each of the first four anniversaries of February 15, 2017, and the remaining half will vest 25% per year on each of the first four anniversaries of February 15, 2018. Pursuant to the Special Retention RSU agreements, vesting as a result of retirement is not permitted unless the employee retires after the merger has closed. In addition, the awards do not accelerate automatically following the closing of the merger. Instead, the employee must remain employed following the closing, and the awards will vest only upon the scheduled vesting date or upon termination of employment under certain circumstances, such as termination without cause, for good reason or due to retirement.

In addition, certain employees of Time Warner and its divisions, including executive officers other than the Chairman and CEO, have received or will receive a cash retention award. Half of the award will become payable upon the closing of the merger, and the remaining half will become payable six months thereafter, in both cases, subject to continued employment on the relevant payment date. Payment will also be made upon termination without cause or for good reason.

Strategic Review

As part of its long-range planning process, the Company routinely reviews opportunities to streamline its operations and optimize its programming. In connection with that review, the Company will evaluate its future use of certain owned and licensed programming rights and could incur charges of approximately $60 million to $80 million in the fourth quarter of 2016.

Time Warner Pension Plan Amendment

On August 1, 2016, the Time Warner Pension Plan (the Pension Plan) was amended to provide for a one-time lump sum window program for eligible vested participants who (i) had terminated employment as of May 31, 2016, (ii) had not yet commenced payment of their benefits as of May 31, 2016, (iii) are not otherwise eligible for an immediate lump sum payment of their benefits and (iv) have benefits with a present value of less than $50,000. Eligible participants had the opportunity to elect, during the period beginning on August 16, 2016 and ending on October 7, 2016, to receive their benefits in the form of an immediate lump sum payment. Certain annuity options were also available. Payments to those eligible participants who elected to receive their benefit under the window program will be made or commence as of December 2016. During the three months ended December 31, 2016, the Company expects to recognize settlement losses of approximately $55 million to $70 million in connection with this amendment to the Pension Plan, the majority of which will be related to businesses the Company has previously disposed of.

Hulu

On August 2, 2016, Time Warner purchased a 10% ownership interest in Hulu, LLC, a company that provides OTT video services, for $590 million in cash, including transaction costs. Time Warner accounts for this investment under the equity method of accounting.

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

2016 Debt Offering

On May 10, 2016, Time Warner issued $800 million aggregate principal amount of 2.95% Notes due 2026 under a shelf registration statement. See Financial Condition and Liquidity Outstanding Debt and Other Financing Arrangements for further information.

NCAA

On March 14, 2016, Turner and CBS entered into an agreement with the National Collegiate Athletic Association (the NCAA) to license the television, digital and marketing rights to the NCAA Division I Men s Basketball Championship Tournament (the NCAA Tournament) from 2025 through 2032 for an aggregate rights fee of $8.8 billion. While the aggregate rights fee will be paid by Turner to the NCAA, the rights fee, production costs, advertising revenues and sponsorship revenues related to the NCAA Tournament and related programming will continue to be shared by Turner and CBS. Annually, for 2025 through 2032, Turner will be allocated the first $90 million of revenue subject to the arrangement. However, if the amount paid for the rights fee and production costs in any year during that period exceeds advertising and sponsorship revenues for that year, including the $90 million of revenue allocated to Turner, CBS share of such shortfall will be limited to $45 million. Under the existing agreement among Turner, CBS and the NCAA, Turner and CBS have licensed rights to the NCAA Tournament through 2024.

Fandango

In April 2016, Warner Bros. sold its Flixster business to Fandango Media, LLC (Fandango), a subsidiary of NBCUniversal Media LLC, in exchange for a 25% interest in Fandango. For the nine months ended September 30, 2016, Warner Bros. recorded a pre-tax gain of $90 million in connection with this transaction.

Central European Media Enterprises Ltd.

On February 19, 2016, CME Media Enterprises B.V. (CME BV), a subsidiary of Central European Media Enterprises Ltd. (CME), entered into a credit agreement (the 2016 Credit Agreement) with third-party financial institutions for an approximate 470 million senior unsecured term loan (the 2016 Term Loan) that was funded in April 2016 and matures on February 19, 2021. Time Warner has guaranteed CME BV s obligations under the 2016 Credit Agreement for a fee equal to a rate based on CME s net leverage, which initially was 10.5%, less the interest rate on the 2016 Term Loan, which initially was approximately 1.78%, to be paid to Time Warner semi-annually. CME BV must pay a portion of the fee in cash and may, at CME BV s option, pay the remainder in cash or in kind. In April 2016, CME used cash on hand and the proceeds of the 2016 Term Loan to repay in their entirety both its Senior Secured Notes due 2017 (the Senior Secured Notes) and the term loan Time Warner provided CME in 2014 (the TW Term Loan), which also was due in 2017. Time Warner received approximately $485 million in connection with CME s repayment of the Senior Secured Notes and the TW Term Loan. As consideration for assisting CME in refinancing its debt due in 2017, Time Warner earned a fee equal to 1% of the aggregate principal amount of the 2016 Term Loan borrowed at funding. Prior to the funding, CME BV entered into unsecured interest rate hedge arrangements to protect against changes in the interest rate on the 2016 Term Loan during its term, and Time Warner has guaranteed CME BV s obligations under such arrangements.

In addition, on February 19, 2016, CME entered into an amendment to extend the maturity of its 251 million senior unsecured term loan obtained in 2014 from third-party financial institutions (the 2014 Term Loan) from November 1, 2017 to November 1, 2018. Time Warner continues to guarantee CME s obligations under the 2014 Term Loan.

Time Warner and CME also agreed on February 19, 2016 to amend and restate the $115 million revolving credit facility Time Warner provided CME in 2014 to reduce the size of the facility to $50 million as of January 1, 2018 and to extend its term from December 2017 to February 2021. Amounts outstanding under the revolving credit facility bear interest at a rate based on CME s net leverage. Beginning in April 2016, CME must pay a portion of the interest for each applicable quarterly interest period in cash and may, at CME s option, pay the remainder in kind by adding such amount to the outstanding principal amount of the revolving credit facility. As of September 30, 2016, there were no amounts outstanding under the revolving credit facility.

The Company recorded a pretax gain of $95 million in Investment gains (losses), net in the accompanying Consolidated Statement of Operations in the second quarter of 2016 in connection with these transactions. Additionally, when recognizing CME s results in the second quarter of 2016 under the equity method of accounting, the Company recorded a pretax charge of $150 million in Other loss, net in the accompanying Consolidated Statement of Operations related to these transactions.

Table of Contents

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

RESULTS OF OPERATIONS

Recent Accounting Guidance

See Note 1, Description of Business and Basis of Presentation, to the accompanying consolidated financial statements for a discussion of recent accounting guidance.

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 from continuing operations has been affected by transactions and certain other items in each period as follows (millions):

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Nine Months Ended September 30, 2016	Nine Months Ended September 30, 2015
Asset impairments	$ (30)	$ (7)	$ (35)	$ (8)
Gain (loss) on operating assets, net	(12)	2	77	(1)
Venezuelan foreign currency loss				(22)
Other	(14)	(3)	(28)	(8)
Impact on Operating Income	(56)	(8)	14	(39)
Investment gains (losses), net	57	15	93	(70)
Amounts related to the separation of Time Warner Cable Inc.		(4)		(8)
Amounts related to the disposition of Warner Music Group	(3)		(4)	
Amounts related to the separation of Time Inc.	(5)	(2)	(13)	(7)
Premiums paid and costs incurred on debt redemption		(21)		(72)
Items affecting comparability relating to equity method investments	1	17	(139)	(4)
Pretax impact	(6)	(3)	(49)	(200)
Income tax impact of above items	35	9	(18)	55
Impact of items affecting comparability on income from continuing operations	$ 29	$ 6	$ (67)	$ (145)

In addition to the items affecting comparability described above, the Company incurred Restructuring and severance costs of $11 million and $64 million for the three and nine months ended September 30, 2016, respectively, and $9 million and $31 million for the three and nine months ended September 30, 2015, respectively. For further discussion of Restructuring and severance costs, see Consolidated Results and Business Segment Results.

Asset Impairments

During the three and nine months ended September 30, 2016, the Company recognized asset impairments of $30 million and $35 million, respectively, which consisted of $25 million at Turner for both periods relating to an international broadcast license, $5 million and $6 million, respectively, at Warner Bros. relating to certain internally developed software and, for the nine months ended September 30, 2016, $4 million at Corporate relating to miscellaneous assets. During the three and nine months ended September 30, 2015, the Company recognized asset impairments of $7 million and $8 million, respectively, which consisted of $5 million and $6 million, respectively, at Corporate primarily related to certain internally developed software, and $1 million for both the three and nine months ended September 30, 2015 at both the Turner and Warner Bros. segments relating to miscellaneous assets.

Table of Contents

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Gain (Loss) on Operating Assets, Net

For the three months ended September 30, 2016, the Company recognized $12 million of loss on operating assets, primarily relating to the pending disposition of a business at the Turner segment. For the nine months ended September 30, 2016, the Company recognized $77 million of net gain on operating assets, consisting of $92 million of gains at the Warner Bros. segment, principally relating to the gain on the sale of Flixster s net assets to Fandango, and $15 million of losses at the Turner segment, principally relating to the pending disposition of a business. For the three and nine months ended September 30, 2015, the Company recognized $2 million of net gains on operating assets at the Turner segment, reflecting a $3 million gain upon its acquisition of the controlling interest of iStreamPlanet and a $1 million loss on the sale of a business. For the nine months ended September 30, 2015, the Company also recognized $2 million of net losses at the Turner segment related to the remeasurement of certain previously held investments upon the Turner segment s acquisition of controlling interests in those investments as well as a $1 million loss at the Warner Bros. segment.

Venezuelan Foreign Currency Loss

For the nine months ended September 30, 2015, the Company recognized a pretax foreign exchange loss of $22 million, consisting of $17 million at the Turner segment and $5 million at the Warner Bros. segment, related to a change in the foreign currency exchange rate used by the Company for remeasuring its Venezuelan net monetary assets from the SICAD 2 rate to the Simadi rate. The Venezuelan foreign currency loss is included in Selling, general and administrative expenses in the accompanying Consolidated Statement of Operations.

Other

For the three and nine months ended September 30, 2016, Other includes external costs related to mergers, acquisitions or dispositions of $4 million and $9 million, respectively, consisting of $3 million and $4 million, respectively, at the Turner segment and $1 million and $2 million, respectively, at the Warner Bros. segment and, for the nine months ended September 30, 2016, $3 million at Corporate. For the three and nine months ended September 30, 2016, Other also includes $10 million of pension settlement charges at Corporate, and for the nine months ended September 30, 2016, $9 million of expenses at the Home Box Office segment related to Home Box Office s withdrawal from a multiemployer benefit plan. For the three and nine months ended September 30, 2015, Other reflects external costs related to mergers, acquisitions or dispositions of $3 million and $8 million, respectively, consisting of $0 and $1 million, respectively, at the Turner segment, $2 million and $5 million, respectively, at the Warner Bros. segment and $1 million and $2 million, respectively, at Corporate. External costs related to mergers, acquisitions or dispositions, the pension settlement charges and the accrued pension withdrawal expenses are included in Selling, general and administrative expenses in the accompanying Consolidated Statement of Operations.

Investment Gains (Losses), Net

For the three and nine months ended September 30, 2016, the Company recognized $57 million and $93 million, respectively, of investment gains, net, consisting of a $41 million gain for both periods associated with an agreement to dissolve a Home Box Office joint venture in the Netherlands, $18 million of gains and $44 million of losses, respectively, relating to fair value adjustments on warrants to purchase common stock of CME held by the Company, $2 million of miscellaneous investment losses and $1 million of miscellaneous investment gains, respectively, and, for the nine months ended September 30, 2016, a $95 million gain in connection with the 2016 CME financing transactions. For the three and nine months ended September 30, 2015, the Company recognized $15 million of net investment gains and $70 million of net investment losses, respectively, consisting of $5 million and $110 million, respectively, of losses related to fair value adjustments on warrants to purchase common stock of CME held by the Company and $20 million and $40 million, respectively, of net miscellaneous investment gains. Investment losses, net are included in Other loss, net in the accompanying Consolidated Statement of Operations.

Amounts Related to the Separation of Time Warner Cable Inc.

For the three and nine months ended September 30, 2015, the Company recognized $4 million of losses related to payments made to Time Warner Cable Inc. (TWC) in accordance with a tax sharing agreement with TWC and, for the nine months ended September 30, 2015, the Company also recognized $4 million of losses related to changes in the value of a TWC tax indemnification receivable. These amounts have been reflected in Other loss, net in the accompanying Consolidated Statement of Operations.

Table of Contents

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Amounts Related to the Disposition of Warner Music Group

For the three and nine months ended September 30, 2016, the Company recognized $3 million and $4 million, respectively, of losses related to the disposition of Warner Music Group (WMG), primarily related to a legal settlement. These amounts have been reflected in Other loss, net in the accompanying Consolidated Statement of Operations.

Amounts Related to the Separation of Time Inc.

The Company recognized expenses of $5 million and $13 million for the three and nine months ended September 30, 2016, respectively, and $2 million and $7 million for the three and nine months ended September 30, 2015, respectively, primarily reflecting pension and other retirement benefit costs related to employees and former employees of Time Inc. These amounts have been reflected in Other loss, net in the accompanying Consolidated Statement of Operations.

Premiums Paid and Costs Incurred on Debt Redemption

For the three and nine months ended September 30, 2015, the Company recognized $21 million of premiums paid and costs incurred principally on the redemption of $313 million aggregate principal amount of its 5.875% Notes due 2016. For the nine months ended September 30, 2015, the Company also recognized $51 million of premiums paid and costs incurred on the purchase of $687 million aggregate principal amount of its 5.875% Notes due 2016 through a tender offer. The premiums paid and costs incurred on the debt redemptions were recorded in Other loss, net in the accompanying Consolidated Statement of Operations.

Items Affecting Comparability Relating to Equity Method Investments

For the three and nine months ended September 30, 2016, the Company recognized $1 million and $11 million of income, respectively, primarily related to net investment gains recorded by equity method investees and, for the nine months ended September 30, 2016, $150 million of losses related to the financing transactions with CME in 2016. For the three and nine months ended September 30, 2015, the Company recognized a $3 million asset impairment recorded by an equity method investee for both periods and $2 million of income and $1 million of losses, respectively, from discontinued operations recorded by an equity method investee. In addition, for the three months ended September 30, 2015, the Company recognized an $18 million reversal of an accrual related to government investigations recorded by an equity method investee. These amounts have 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 using the effective tax rate for the item. The estimated tax provision or tax benefit can vary based on certain factors, including the taxability or deductibility of the item and the applicable tax jurisdiction for the item. Also included in the income tax impact for the three and nine months ended September 30, 2016 is a tax benefit of approximately $19 million related to the settlement of Netherlands tax liabilities associated with the repayment of the CME Senior Secured Notes and TW Term Loan.

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.

Table of Contents

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

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

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2016	2015	% Change	2016	2015	% Change
Turner	$ 2,610	$ 2,398	9%	$ 8,526	$ 7,935	7%
Home Box Office	1,426	1,367	4%	4,399	4,203	5%
Warner Bros.	3,402	3,190	7%	9,169	9,687	(5)%
Intersegment eliminations	(271)	(391)	(31)%	(667)	(786)	(15)%
Total revenues	$ 7,167	$ 6,564	9%	$ 21,427	$ 21,039	2%

For the three and nine months ended September 30, 2016, Revenues at the Turner segment increased primarily driven by higher Subscription and Advertising revenues. Revenues at the Home Box Office segment increased for the three and nine months ended September 30, 2016 due to higher Subscription revenues. For the three months ended September 30, 2016, Revenues increased at the Warner Bros. segment driven by higher Theatrical product revenues, partially offset by lower Videogames and other revenues. For the nine months ended September 30, 2016, Revenues at the Warner Bros. segment decreased primarily due to lower Videogames and other revenues. Changes in exchange rates associated with the foreign currencies to which the Company is exposed negatively impacted the Company s Revenues by approximately $55 million and $230 million for the three and nine months ended September 30, 2016, respectively, as compared to the three and nine months ended September 30, 2015, with negative impacts of approximately $25 million and $120 million, respectively, at the Turner segment, $30 million and $100 million, respectively, at the Warner Bros. segment and $0 and $10 million, respectively, at the Home Box Office segment. If the foreign exchange rates relative to the U.S. Dollar remain at the levels they were at as of September 30, 2016 or if the U.S. Dollar strengthens further in 2016 relative to the foreign currencies to which the Company is exposed, the Company s Revenues in 2016 will be negatively affected as compared to its Revenues in 2015. Each of the revenue categories is discussed in greater detail by segment in Business Segment Results.

Costs of Revenues. For the three and nine months ended September 30, 2016, Costs of revenues were $3.873 billion and $11.718 billion, respectively, as compared to $3.526 billion and $11.802 billion for the three and nine months ended September 30, 2015, respectively. The increase in Costs of revenues for the three months ended September 30, 2016 reflected increases across all of the segments. The decrease in Costs of revenues for the nine months ended September 30, 2016 reflected a decrease at the Warner Bros. segment, partially offset by increases at the Turner and Home Box Office segments. The segment variations are discussed in Business Segment Results.

Selling, General and Administrative Expenses. For the three months ended September 30, 2016, Selling, general and administrative expenses increased 3% to $1.179 billion from $1.143 billion for the three months ended September 30, 2015, primarily reflecting an increase at Corporate. For the nine months ended September 30, 2016, Selling, general and administrative expenses increased 3% to $3.688 billion from $3.580 billion for the nine months ended September 30, 2015, primarily reflecting increases at the Turner segment and Corporate, partially offset by a decline at the Warner Bros. segment. For the nine months ended September 30, 2015, Selling, general and administrative expenses included a $22 million foreign currency charge related to a change in the foreign currency exchange rate used by the Company for remeasuring its Venezuelan net monetary assets from the SICAD 2 rate to the Simadi rate. The segment variations are discussed in Business Segment Results.

Included in Costs of revenues and Selling, general and administrative expenses is depreciation expense of $118 million and $359 million for the three and nine months ended September 30, 2016, respectively, and $120 million and $363 million for the three and nine months ended September 30, 2015, respectively.

Amortization Expense. Amortization expense was $48 million and $143 million for the three and nine months ended September 30, 2016, respectively, and $47 million and $138 million for the three and nine months ended September 30, 2015, respectively.

Table of Contents

TIME WARNER INC.

MANAGEMENT S DISCUSSION AND ANALYSIS

OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Restructuring and Severance Costs. For the three and nine months ended September 30, 2016 and 2015, the Company incurred Restructuring and severance costs primarily related to employee terminations and other exit activities. Restructuring and severance costs are as follows (millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Turner	$ 8	$ 5	$ 15	$ 23
Home Box Office			41	5
Warner Bros.	1	1	6	3
Corporate	2	3	2	
Total restructuring and severance costs	$ 11	$ 9	$ 64	$ 31

Operating Income. Operating Income increased to $2.014 billion for the three months ended September 30, 2016 from $1.834 billion for the three months ended September 30, 2015. Excluding the items noted under Transactions and Other Items Affecting Comparability totaling $56 million and $8 million of expense for the three months ended September 30, 2016 and 2015, respectively, Operating Income increased $228 million, primarily reflecting an increase at the Turner segment.

Operating Income increased to $5.856 billion for the nine months ended September 30, 2016 from $5.479 billion for the nine months ended September 30, 2015. Excluding the items noted under Transactions and Other Items Affecting Comparability totaling $14 million of income and $39 million of expense for the nine months ended September 30, 2016 and 2015, respectively, Operating Income increased $324 million, primarily reflecting an increase at the Turner segment.

Interest Expense, Net. Interest expense, net detail is shown in the table below (millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Interest expense	$			