

Warner Music Group Corp.  
Form 10-Q  
August 07, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2014

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 (I.R.S. Employer  
incorporation or organization) Identification No.)

1633 Broadway

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

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  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  (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

There is no public market for the Registrant's common stock. As of August 7, 2014 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.

WARNER MUSIC GROUP CORP.

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## ITEM 1. FINANCIAL STATEMENTS

Warner Music Group Corp.

## Consolidated Balance Sheets (Unaudited)

	June 30, 2014	September 30, 2013
	(in millions)	
<b>Assets</b>		
Current assets:		
Cash and equivalents	\$ 142	\$ 155
Accounts receivable, less allowances of \$69 and \$55 million	449	511
Inventories	37	33
Royalty advances expected to be recouped within one year	101	93
Deferred tax assets	43	43
Prepaid and other current assets	72	59
Total current assets	844	894
Royalty advances expected to be recouped after one year	190	173
Property, plant and equipment, net	206	180
Goodwill	1,675	1,668
Intangible assets subject to amortization, net	2,978	3,107
Intangible assets not subject to amortization	121	120
Other assets	102	110
Total assets	\$6,116	\$ 6,252
<b>Liabilities and Equity</b>		
Current liabilities:		
Accounts payable	\$221	\$ 280
Accrued royalties	1,163	1,147
Accrued liabilities	261	308
Accrued interest	50	75
Deferred revenue	230	139
Current portion of long-term debt	13	13
Other current liabilities	8	25
Total current liabilities	1,946	1,987
Long-term debt	3,033	2,854
Deferred tax liabilities, net	396	439
Other noncurrent liabilities	281	229
Total liabilities	\$5,656	\$ 5,509
<b>Equity:</b>		
Common stock (\$0.001 par value; 10,000 shares authorized; 1,055 shares issued and outstanding)	\$—	\$ —
Additional paid-in capital	1,128	1,128
Accumulated deficit	(623 )	(341 )
Accumulated other comprehensive loss, net	(63 )	(61 )
Total Warner Music Group Corp. equity	442	726
Noncontrolling interest	18	17
Total equity	460	743

Total liabilities and equity	\$6,116	\$ 6,252
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See accompanying notes

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Warner Music Group Corp.

## Consolidated Statements of Operations (Unaudited)

	Three Months Ended June 30, 2014		Nine Months Ended June 30, 2013	
	2014	2013	2014	2013
	(in millions)			
Revenues	\$788	\$663	\$2,256	\$2,107
Costs and expenses:				
Cost of revenue	(417)	(369)	(1,177)	(1,103)
Selling, general and administrative expenses (a)	(319)	(238)	(885)	(745)
Amortization expense	(67)	(48)	(199)	(143)
Total costs and expenses	(803)	(655)	(2,261)	(1,991)
Operating (loss) income	(15)	8	(5)	116
Loss on extinguishment of debt	(141)	(2)	(141)	(85)
Interest expense, net	(48)	(47)	(157)	(149)
Other income (expense)	4	(2)	(3)	(11)
Loss before income taxes	(200)	(43)	(306)	(129)
Income tax benefit (expense)	16	(19)	27	(8)
Net loss	(184)	(62)	(279)	(137)
Less: Income attributable to noncontrolling interest	(1)	(1)	(3)	(4)
Net loss attributable to Warner Music Group Corp.	\$(185)	\$(63)	\$(282)	\$(141)
(a) Includes depreciation expense of:	\$(14)	\$(13)	\$(39)	\$(38)

See accompanying notes

Warner Music Group Corp.

## Consolidated Statement of Comprehensive Loss (Unaudited)

	Three Months Ended June 30, 2014		Nine Months Ended June 30, 2013	
	2014	2013	2014	2013
	(in millions)			
Net loss	\$(184)	\$(62)	\$(279)	\$(137)
Other comprehensive income (loss), net of tax:				
Foreign currency adjustment	4	4	(2 )	(8 )
Deferred losses on derivative financial instruments	—	(2 )	—	(2 )
Other comprehensive income (loss), net of tax:	4	2	(2 )	(10 )
Total comprehensive loss	(180)	(60)	(281)	(147)
Less: Income attributable to noncontrolling interest	(1 )	(1 )	(3 )	(4 )
Comprehensive loss attributable to Warner Music Group Corp.	\$(181)	\$(61)	\$(284)	\$(151)

See accompanying notes

Warner Music Group Corp.

## Consolidated Statements of Cash Flows (Unaudited)

	Nine Months Ended June 30, 2014 2013 (in millions)	
<b>Cash flows from operating activities</b>		
Net loss	\$(279)	\$(137 )
Adjustments to reconcile net loss to net cash provided by operating activities:		
Loss on extinguishment of debt	141	85
Depreciation and amortization	238	181
Deferred income taxes	(47 )	(13 )
Non-cash interest expense	11	8
Non-cash share-based compensation expense	5	8
Changes in operating assets and liabilities:		
Accounts receivable	67	81
Inventories	(4 )	2
Royalty advances	(24 )	(9 )
Accounts payable and accrued liabilities	(96 )	(80 )
Royalty Payables	11	41
Accrued interest	(25 )	(33 )
Deferred revenue	93	25
Other balance sheet changes	(50 )	(12 )
Net cash provided by operating activities	41	147
<b>Cash flows from investing activities</b>		
Acquisition of music publishing rights	(20 )	(35 )
Capital expenditures	(46 )	(23 )
Investments and acquisitions of businesses	(26 )	(18 )
Net cash used in investing activities	(92 )	(76 )
<b>Cash flows from financing activities</b>		
Proceeds from the Revolving Credit Facility	490	111
Repayment of the Revolving Credit Facility	(490)	(86 )
Proceeds from Acquisition Corp. Senior Term Loan Facility	—	594
Repayment of Acquisition Corp. Senior Term Loan Facility	(7 )	(110 )
Proceeds from issuance of Acquisition Corp. 5.625% Senior Secured Notes	275	—
Proceeds from issuance of Acquisition Corp. 6.00% Senior Secured Notes	—	500
Repayment of Acquisition Corp. 6.00% 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 issuance of Acquisition Corp. 6.750% Senior Notes	660	—
Repayment of Acquisition Corp. 9.5% Senior Secured Notes	—	(1,250)
Repayment of Acquisition Corp. 11.5% Senior Notes	(765)	—
Financing costs paid	(104)	(129 )
Deferred financing costs paid	(12 )	(42 )



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Distribution to noncontrolling interest holder	(2 )	(2 )
Repayment of capital lease obligations	(2 )	—
Net cash provided by (used in) financing activities	43	(260 )
Effect of exchange rate changes on cash and equivalents	(5 )	(11 )
Net decrease in cash and equivalents	(13 )	(200 )
Cash and equivalents at beginning of period	155	302
Cash and equivalents at end of period	\$142	\$102

See accompanying notes

Warner Music Group Corp.

## Consolidated Statement of Equity (Unaudited)

	Common Stock Shares	Value	Additional Paid-in Capital	Accumulated Deficit	Other Comprehensive Loss	Total Warner Music Group Corp. Equity	Noncontrolling Interest	Total Equity
(in millions, except per share amounts)								
Balance at September 30, 2013	1,055	\$0.001	\$ 1,128	\$ (341 )	\$ (61 )	\$ 726	\$ 17	\$ 743
Net loss	—	—	—	(282 )	—	(282 )	3	(279 )
Other comprehensive loss, net of tax	—	—	—	—	(2 )	(2 )	—	(2 )
Distribution to noncontrolling interest	—	—	—	—	—	—	(2 )	(2 )
Balance at June 30, 2014	1,055	\$0.001	\$ 1,128	\$ (623 )	\$ (63 )	\$ 442	\$ 18	\$ 460

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.

### Acquisition of Warner Music Group by Access Industries

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 (formerly Airplanes Music 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.

### Acquisition of Parlophone Label Group

On July 1, 2013, the Company completed its acquisition of Parlophone Label Group. See Note 4 for a further discussion.

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 United States, 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 reissues 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, Big Beat, East West, Elektra, Erato, Fueled by Ramen, Nonesuch, Parlophone, Reprise, Roadrunner, Rykodisc, Sire, Warner Classics, Warner Music Nashville and Word.

Outside the United States, 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 United States: 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 domestic record labels have international rights. In certain smaller markets, the Company licenses the right to distribute the Company's records to non-affiliated third-party record labels. The Company's international artist services operations also include a network of concert promoters through which it provides resources to coordinate tours for the Company's artists and other artists as well as management companies that partner with artists on other aspects of their career such as merchandising, fan clubs, endorsements, as well as appearances and sponsorship.

The Company's Recorded Music distribution operations include Warner-Elektra-Atlantic Corporation ("WEA Corp."), which markets and sells music and video 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 the Company's worldwide artist and label-services organization, including ADA Worldwide, which provides distribution services outside of the U.S. through a network of affiliated and non-affiliated distributors.

In addition to the Company's Recorded Music products being sold in physical retail outlets, 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 download services such as Apple's iTunes and Google Play, and are otherwise used by digital streaming services such as Beats Music, Deezer, Rhapsody and Spotify, and digital radio services such as Pandora, iTunes Radio and iHeart Radio.

The Company has integrated the sale of digital content into all aspects of its business, including Artist & Repertoire ("A&R"), marketing, promotion and distribution. The Company's business development executives work closely with A&R departments to ensure that while a record is being produced, digital assets are also created with all distribution channels in mind, including streaming services, social networking sites, online portals and music-centered destinations. The Company also works side-by-side with its online and mobile 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 proportions may change as the roll out of new technologies continues. As an owner of music 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 aspects of their careers. Under these agreements, the Company provides services to and participates in artists' activities outside the traditional recorded music business. The Company builds 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 artist services and 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, concert promotion 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

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

The Company's Music Publishing operations include Warner/Chappell, its global Music Publishing company, headquartered in Los Angeles with operations in over 50 countries through various subsidiaries, affiliates and non-affiliated licensees. The Company 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, classical, 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 augment 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,

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 United States ("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, 2014 are not necessarily indicative of the results that may be expected for the fiscal year ended September 30, 2014.

The consolidated balance sheet at September 30, 2013 has been derived from the audited consolidated financial statements at that date but does not include all of the information and notes required by U.S. GAAP for complete financial statements.

For further information, refer to the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2013 (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 required to be consolidated in accordance with U.S. GAAP. All intercompany balances and transactions have been eliminated.

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, 2014 and June 30, 2013 relate to the periods ended June 27, 2014 and June 28, 2013, respectively. For convenience purposes, the Company continues to date its financial statements as of June 30. All references to September 30, 2013 relate to the fiscal year ended on September 27, 2013. For convenience purposes, the Company continues to date its financial statements as of September 30.

The Company has performed a review of all subsequent events through the date the financial statements were issued, and has determined that no additional disclosures are necessary.

#### New Accounting Pronouncements

In May 2014, the FASB issued guidance codified in ASC 606, Revenue Recognition – Revenue from Contracts with Customers (“ASC 606”), which amends the guidance in former ASC 605, Revenue Recognition and ASC 928, Entertainment – Music. The amendment was the result of a joint effort by the FASB and the International Accounting Standards Board to improve financial reporting by creating common revenue recognition guidance for U.S. GAAP and international financial reporting standards (“IFRS”). The joint project clarifies the principles for recognizing revenue and develops a common revenue standard for U.S. GAAP and IFRS. ASC 606 is effective for annual periods beginning after December 15, 2016, and interim periods within those years. Early application is not permitted. The update may be applied using one of two methods: retrospective application to each prior reporting period presented, or retrospective application with the cumulative effect of initially applying the update recognized at the date of initial application. The Company is currently evaluating the transition method that will be elected and the impact of the update on its financial statements and disclosures.

In April 2014, the FASB issued Accounting Standards Updates (“ASU”) 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity (“ASU 2014-08”). This ASU increases the requirements for components to be classified as discontinued operations to require a strategic shift (major line of business, major geographical area) that has or will have a major effect on an entity's operations and financial results. ASU 2014-08 is effective prospectively for disposals that occur in annual periods beginning after December 15, 2014, and interim periods thereafter. The adoption of this standard is not expected to have a significant impact on the Company's financial statements.

In July 2013, the FASB issued ASU 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists (“ASU 2013-11”). ASU 2013-11 attempts to eliminate diversity in practice by requiring an unrecognized tax benefit, or a portion of an unrecognized tax benefit, to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss, or a tax credit carryforward. ASU 2013-11 is effective for annual and interim reporting periods for fiscal years beginning after December 15, 2013. The adoption of this standard is not expected to have a significant impact on the Company’s financial statements, other than presentation.

During the first quarter of fiscal 2014, the Company simultaneously adopted ASU 2011-11, Disclosures about Offsetting Assets and Liabilities (“ASU 2011-11”) and ASU 2013-01, Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities (“ASU 2013-01”). ASU 2011-11 and ASU 2013-01 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. The adoption of these standards did not have an impact on the Company’s financial statements, other than disclosure.

During the first quarter of fiscal 2014, the Company adopted ASU 2013-02, Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income (“ASU 2013-02”). ASU 2013-02 requires entities to disclose, in one place, information



about the amounts reclassified out of accumulated other comprehensive income by component. The adoption of this standard did not have an impact on the Company's financial statements, other than disclosure.

### 3. Comprehensive Income (Loss)

Comprehensive income (loss), which is reported in the accompanying consolidated statements of equity, consists of net income (loss) and other gains and losses affecting equity that, under U.S. GAAP, are excluded from net income (loss). For the Company, the components of other comprehensive loss primarily consist of foreign currency translation losses, minimum pension liabilities, 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 changes in the components of accumulated other comprehensive loss, net of related taxes:

	Foreign Currency Translation Loss (in millions)	Minimum Pension Liability Adjustment	Accumulated Other Comprehensive Loss, net
Balance at September 30, 2013	\$(57)	\$ (4 )	\$ (61 )
Other comprehensive loss (a)	(2 )	—	(2 )
Amounts reclassified from accumulated other comprehensive income	—	—	—
Balance at June 30, 2014	\$(59)	\$ (4 )	\$ (63 )

(a) Foreign currency translation loss is net of a gain on intra-entity foreign currency transactions that are of a long-term investment nature of \$21 million.

### 4. Acquisition of Parlophone Label Group

On July 1, 2013, the Company completed the acquisition of Parlophone Label Group ("PLG") from Universal for £487 million in an all-cash transaction (the "PLG Acquisition"). The PLG Acquisition was accounted for in accordance with FASB ASC Topic 805, Business Combination ("ASC 805"), using the acquisition method of accounting. The assets acquired and liabilities assumed in connection with the PLG Acquisition, including identifiable intangible assets, have been measured at their fair value primarily using Level 3 inputs (see Note 12 for additional information on fair value inputs). Determining the fair value of the assets acquired and liabilities assumed requires judgment and involved the use of significant estimates and assumptions, including assumptions with respect to future cash inflows and outflows, discount rates, asset useful lives and market multiples, among other items. The use of different estimates and judgments could yield materially different results.

In connection with the PLG Acquisition, the Company incurred \$15 million in professional fees and integration costs during the three months ended June 30, 2014, \$51 million during the nine months ended June 30, 2014 and \$38 million in professional fees and integration costs, as well as an \$11 million fee under the Management Agreement (defined below), during the fiscal year ended September 30, 2013.



The allocation of the purchase price was completed as of June 30, 2014 and any adjustments to goodwill made up to that date have been recorded in the Company's balance sheet as of June 30, 2014. The table below presents (i) the estimate of the PLG Acquisition consideration as it relates to the acquisition of PLG by the Buyers and (ii) the final allocation of the purchase price to the estimated fair values of the assets acquired and liabilities assumed on the closing date of July 1, 2013 (in millions):

Purchase Price	£487
Preliminary Working Capital Adjustment	13
Adjusted Purchase Price	£500
Foreign Exchange Rate at July 1, 2013	1.53
Adjusted Purchase Price in U.S. dollars	\$765
Fair Value of assets acquired and liabilities assumed:	
Cash	46
Accounts receivable*	83
Other current assets	8
Property, plant and equipment	39
Intangible assets	764
Accounts payable	(83 )
Royalties payable	(147)
Other current liabilities	(21 )
Deferred revenue	(25 )
Deferred tax liabilities*	(140)
Other noncurrent liabilities *	(27 )
Fair value of net assets acquired	497
Goodwill recorded *	268
Total purchase price allocated	\$765

\*Preliminary amounts were adjusted in the first and third quarters of fiscal 2014 based on new information obtained during the measurement period.

As of June 30, 2014 and as of the date this Quarterly Report on Form 10-Q was filed, the working capital adjustment had still not been determined. Any subsequent working capital adjustments will be reflected in the statement of operations as the measurement period for this acquisition has closed.

The excess of the purchase price, over the fair value of net assets acquired, including the amount assigned to identifiable intangible assets and deferred tax adjustments, has been recorded to goodwill. The goodwill recorded as part of the PLG Acquisition reflects the expected value to be generated from the continuing transition of the music industry and the expected resulting cost savings; cost and revenue synergies to be realized; as well as any intangible assets that do not qualify for separate recognition. The resulting goodwill has been allocated to our Recorded Music reportable segment. The Company does not expect the goodwill recognized to be deductible for income tax purposes. Any impairment charges made in future periods associated with goodwill will not be tax deductible.

The components of the intangible assets identified in the table above and the related useful lives, allocated to the Company's Recorded Music reportable segment, are as follows:

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	Value (in millions)	Useful Life
Trademark and trade name	\$ 17	Indefinite
Catalog	442	13 years
Artist contracts	305	10 years
Total intangible assets	\$ 764	

Pro Forma Financial Information (unaudited)

The following unaudited pro forma information has been presented as if the PLG Acquisition occurred on October 1, 2012. This information is based on historical results of operations, adjusted to give effect to pro forma events that are (i) directly attributable to the PLG Acquisition; (ii) factually supportable; and (iii) expected to have a continuing impact on the Company's combined results. Additionally, certain pro forma adjustments have been made to the historical results of PLG in order to (i) convert them to U.S. GAAP; (ii) conform their accounting policies to those applied by the Company; (iii) present them in U.S. dollars; (iv) align accounting

periods; and (v) eliminate revenue and expenses and related assets and liabilities for international licensing agreements to sell repertoire owned by non acquired entities that have been terminated as a result of the PLG Acquisition and (vi) excluded assets not acquired by the Company. The unaudited pro forma results do not reflect the realization of any cost savings as a result of restructuring activities and other cost savings initiatives planned subsequent to the PLG Acquisition or the related estimated restructuring charges contemplated in association with any such expected cost savings. Such charges will be expensed in the appropriate accounting periods. The unaudited pro forma results for the three and nine months ended June 30, 2013 includes the licensing income remitted to the repertoire owner by the selling territory, but does not reflect the licensing fee retained and related direct costs incurred by the selling territory. For the three and nine months ended June 30, 2014, where the Company is the selling territory, the licensing fee and direct costs are included in our consolidated results.

The pro forma information as presented below is for informational purposes only and is not indicative of the results of operations that would have been achieved if the PLG Acquisition had taken place at the beginning of fiscal 2013.

	Three Months Ended June 30, 2013	Nine Months Ended June 30, 2013
	(in millions)	
Revenue	\$ 738	\$ 2,371
Operating income	8	105
Net loss attributable to Warner Music Group Corp.	(64 )	(168 )

Actual results related to PLG included in the Consolidated Statements of Operations for the three and nine months ended June 30, 2014 consist of revenues of \$102 million and \$248 million, respectively and operating loss of \$24 million and \$82 million, respectively. Actual results for the three and nine months ended June 30, 2014 include professional fees and integration costs of \$15 million and \$51 million, respectively and restructuring costs of \$18 million and \$42 million, respectively, associated with the PLG Acquisition. The results related to PLG included in the above results for the three and nine months ended June 30, 2013 consist of revenues of \$75 million and \$264 million, respectively. There was no operating loss during the three months ended June 30, 2013 and operating loss was \$11 million during the nine months ended June 30, 2013.

## 5. Goodwill and Intangible Assets

### Goodwill

The following summary sets forth the changes in goodwill for each reportable segment during the nine months ended June 30, 2014:

	RecordedMusic Music Publishing (in millions)	Total
Balance at September 30, 2013	\$1,204 \$ 464	\$1,668

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Acquisitions	5	—	5
Dispositions	—	—	—
Other adjustments	2	—	2
Balance at June 30, 2014	\$1,211	\$ 464	\$1,675

Acquisitions during the nine months ended June 30, 2014 represent an adjustment to preliminary amounts recorded in the prior period as a result of the PLG Acquisition based on new information obtained during the measurement period. Other adjustments during the nine months ended June 30, 2014 represent foreign currency movements.

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 may 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 consisted of the following:

	Weighted	June	September
	Average	30,	30,
	Useful Life	2014	2013
		(in millions)	
<b>Intangible assets subject to amortization:</b>			
Recorded music catalog	10 years	\$1,031	\$ 1,006
Music publishing copyrights	28 years	1,579	1,546
Artist and songwriter contracts	13 years	998	983
Trademarks	7 years	7	7
Total gross intangible asset subject to amortization		3,615	3,542
Accumulated amortization		(637 )	(435 )
Total net intangible assets subject to amortization		2,978	3,107
<b>Intangible assets not subject to amortization:</b>			
Trademarks and tradenames	Indefinite	121	120
Total net other intangible assets		\$3,099	\$ 3,227

## 6. Debt

## Debt Capitalization

Long-term debt, including the current portion, consisted of the following:

	June	September
	30,	30,
	2014	2013
	(in millions)	
Revolving Credit Facility—Acquisition Corp. (a)	\$—	\$ —
Term Loan Facility due 2020—Acquisition Corp. (b)	1,297	1,303
5.625% Senior Secured Notes due 2022—Acquisition Corp.	275	—
6.00% Senior Secured Notes due 2021—Acquisition Corp.	450	450
6.25% Senior Secured Notes due 2021—Acquisition Corp. (c)	214	213
6.75% Senior Notes due 2022—Acquisition Corp.	660	—
11.5% Senior Notes due 2018—Acquisition Corp. (d)	—	751
13.75% Senior Notes due 2019—Holdings	150	150
Total debt	3,046	2,867
Less: current portion	13	13
Total long-term debt	\$3,033	\$ 2,854

- (a) Reflects \$150 million of commitments under the Revolving Credit Facility, less letters of credit outstanding of approximately \$11 million and \$1 million at June 30, 2014 and September 30, 2013, respectively. There were no loans outstanding under the Revolving Credit Facility at June 30, 2014 or September 30, 2013.
  - (b) Principal amount of \$1.303 billion less unamortized discount of \$6 million at June 30, 2014. Principal amount of \$1.310 billion less unamortized discount of \$7 million at September 30, 2013. Of this amount, \$13 million at both June 30, 2014 and September 30, 2013, representing the scheduled amortization, was included in the current portion of long term debt.
  - (c) Face amount of €158 million. Amounts above represent the dollar equivalent of such notes at June 30, 2014 and September 30, 2013.
  - (d) Face amount of \$765 million less unamortized discounts of \$14 million at September 30, 2013. The Company refinanced the \$765 million of 11.5% Senior Notes due 2018 as part of the 2014 Refinancing.
- 2012 Debt Refinancing

On November 1, 2012, the Company completed a refinancing (the “2012 Refinancing”) of its then outstanding senior secured notes due 2016. In connection with the 2012 Refinancing, the Company issued new senior secured notes consisting of \$500 million aggregate principal amount of 6.00% Senior Secured Notes due 2021 (“the Dollar Notes”) and €175 million aggregate principal amount of 6.25% Senior Secured Notes due 2021 (the “Euro Notes” and together with the Dollar Notes, the “Existing Senior Secured



Notes”) and entered into new senior secured credit facilities consisting of a \$600 million term loan facility (the “Senior Term Loan Facility”) and a \$150 million revolving credit facility (the “Revolving Credit Facility” and, together with the Senior Term Loan Facility, the “Senior Credit Facilities”). Acquisition Corp. is the borrower under the Revolving Credit Facility (the “Revolving Borrower”) and under the Senior 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 Revolving Credit Facility.

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 fiscal year ended September 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 Senior Term Loan Facility (the “Term Loan Repayment”). Also on May 9, 2013, the Term Loan Borrower entered into an amendment to the Senior Term Loan Facility among the Term Loan Borrower, Holdings, the subsidiaries of the Term Loan Borrower party thereto, Credit Suisse AG, as administrative agent, and the other financial institutions and lenders from time to time party thereto, providing for the refinancing of the then outstanding term loan and for a \$820 million senior secured incremental term loan facility (the “Incremental Term Loan Facility”). As part of the amendment to the Senior Term Loan Facility, the interest rate, maturity date, and scheduled amortization were changed. On July 1, 2013, Acquisition Corp. drew down the \$820 million Incremental Term Loan Facility to fund the PLG Acquisition, pay fees, costs and expenses related to the PLG Acquisition and for general corporate purposes of Acquisition Corp. and its subsidiaries. Currently, the Senior Term Loan Facility provides for term loans thereunder (the “Term Loans”) in an amount of up to \$1.310 billion.

#### 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 6.00% Senior Secured Notes due 2021 and €17.5 million in aggregate principal amount of its outstanding 6.25% Senior Secured Notes due 2021. The Company recorded a loss on extinguishment of debt of approximately \$2 million in the fiscal year ended September 30, 2013, which represents the premium paid on early redemption.

#### 2014 Debt Refinancing

On April 9, 2014, the Company completed a refinancing of part of its outstanding debt (the “2014 Refinancing”). In connection with the 2014 Refinancing, the Company issued \$275 million in aggregate principal amount of its 5.625% Senior Secured Notes due 2022 (the “New Senior Secured Notes”) and \$660 million in aggregate principal amount of its

6.750% Senior Notes due 2022 (the “New Unsecured Notes”).

In connection with the 2014 Refinancing, the Company used \$869 million, to redeem or repurchase the Company’s previously outstanding \$765 million 11.5% Senior Notes due 2018 and to pay tender/call premiums of \$85 million and consent fees of approximately \$19 million. The Company also paid approximately \$3 million in accrued interest with respect to the notes redeemed or repurchased.

The Company recorded a loss on extinguishment of debt of approximately \$141 million in the nine months ended June 30, 2014, which represents the difference between the redemption payment and the carrying value of the debt, which included the principal value of \$765 million, less unamortized discounts of \$13 million and unamortized debt issuance costs of \$24 million.

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## Interest Rates

The loans under the Revolving Credit Facility bear interest at Revolving Borrower's election at a rate equal to (i) the rate for deposits in the borrowing currency in the London interbank market (adjusted for maximum reserves) for the applicable interest period ("Revolving LIBOR"), plus 2.00% per annum, or (ii) the base rate, which is the highest of (x) the corporate base rate established by the administrative agent from time to time, (y) 0.50% in excess of the overnight federal funds rate and (z) the one-month Revolving LIBOR plus 1.0% per annum, plus, in each case, 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 loans under the Senior Term Loan Facility bear interest at Term Loan Borrower's election at a rate equal to (i) the rate for deposits in U.S. dollars in the London interbank market (adjusted for maximum reserves) for the applicable interest period ("Term Loan LIBOR"), plus 2.75% per annum, or (ii) the base rate, which is the highest of (x) the corporate base rate established by the administrative agent as its prime rate in effect at its principal office in New York City from time to time, (y) 0.50% in excess of the overnight federal funds rate and (z) one-month Term Loan LIBOR, plus 1.00% per annum, plus, in each case, 1.75% per annum. The loans under the Senior Term Loan Credit Agreement are subject to a Term Loan LIBOR "floor" of 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.

## Amortization and Maturity of Term Loan Facility

The loans under the Senior Term Loan Facility amortize in equal quarterly installments due December, March, June and September in aggregate annual amounts equal to 1.00% of the original principal amount of the amended Senior Term Loan Facility with the balance payable on maturity date of the Term Loans. The loans outstanding under the Senior Term Loan Facility mature on July 1, 2020.

## Maturity of Revolving Credit Facility

The Revolving Credit Facility matures on November 1, 2017. On March 25, 2014, Acquisition Corp. received lender consent to an amendment to the credit agreement for its Revolving Credit Facility. The amendment became effective on April 9, 2014 and extended the maturity date of the Revolving Credit Facility to April 1, 2019.

## Maturities of Senior Notes and Senior Secured Notes

As of June 30, 2014, there are no scheduled maturities of notes until 2019, when \$150 million is scheduled to mature. Thereafter, \$1.599 billion is scheduled to mature.

## Interest Expense, net

Total interest expense, net was \$48 million and \$47 million for the three months ended June 30, 2014 and June 30, 2013, respectively. Total interest expense, net was \$157 million and \$149 million for the nine months ended June 30, 2014 and June 30, 2013, respectively. The weighted-average interest rate of the Company's total debt was 5.6% at June 30, 2014 and 8.1% at June 30, 2013.

## 7. Restructuring

In conjunction with the PLG Acquisition, the Company undertook a plan to achieve cost savings (the “Restructuring Plan”), primarily through headcount reductions. The Restructuring Plan was approved by the CEO prior to the close of the PLG Acquisition. Under the Restructuring Plan, the Company currently expects to record an aggregate of approximately \$86 million in restructuring charges, currently estimated to be made up of employee-related costs of \$78 million, real estate costs of \$7 million and other costs of \$1 million. Total restructuring costs of \$18 million were incurred in the three months ended June 30, 2014 with respect to these actions, which consist of \$15 million of employee-related costs and \$3 million of real estate costs. Total restructuring costs of \$42 million were incurred in the nine months ended June 30, 2014 with respect to these actions, which consist of \$37 million of employee-related costs, \$4 million of real estate costs and \$1 million of other costs. Total restructuring costs of \$3 million were incurred in both the three and nine months ended June 30, 2013 with respect to these actions, which consist of \$3 million of employee-related costs. Total costs to date under the Restructuring Plan are \$64 million, including total cash payments of \$42 million. The remainder of the Restructuring Plan is expected to be completed by the end of fiscal 2015.

Total restructuring activity is as follows:

	Employee- Related Costs (in millions)	Real Estate Costs	Other	Total
Balance at September 30, 2013	\$ 10	\$ —	\$ —	\$ 10
Restructuring expense	37	4	1	42
Cash Payments	(27)	(2)	(1)	(30)
Balance at June 30, 2014	\$ 20	\$ 2	\$ —	\$ 22

The restructuring accrual is recorded in other current liabilities on the consolidated balance sheet. These balances reflect estimated future cash outlays.

A summary of the charges in the Consolidated Statement of Operations resulting from the Restructuring Plan is shown below:

	Three Months Ended June 30, 2014	2013	Nine Months Ended June 30, 2014	2013
	(in millions)			
Selling, general and administrative expenses	\$ 18	\$ 3	\$ 42	\$ 3
Total restructuring expense	\$ 18	\$ 3	\$ 42	\$ 3

All of the above expenses were recorded in the Recorded Music reportable segment.

## 8. 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 download purchasers. Plaintiffs filed an operative consolidated amended complaint on August 31, 2011. Pursuant to the terms of an August 15, 2011 stipulation and order, the case is currently in discovery. Disputes regarding the scope of discovery are ongoing. Plaintiffs filed a Class Certification brief on March 14, 2014. The Company's reply date has not yet been set. 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.

On December 31, 2013, Plaintiffs filed a Motion for Preliminary Approval of Class Action Settlement. On January 23, 2014, the Court granted preliminary approval of the settlement. As part of the settlement, the Company will make available \$11.5 million (less attorneys' fees, costs, and costs of claims administration and class notice) to compensate class members for past sales of downloads and ringtones. Plaintiffs will file their motion for final approval of the Settlement Agreement on or before November 26, 2014. The hearing on final approval of the settlement is scheduled for January 8, 2015. 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.

#### 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.

#### 9. Derivative Financial Instruments

The Company uses derivative financial instruments, primarily foreign currency forward exchange 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 foreign currency forward exchange contracts 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. The foreign currency forward exchange contracts related to royalties are designated and qualify as cash flow hedges under the criteria prescribed in ASC 815. The Company records these contracts at fair value on its balance sheet and 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.

The Company may at times choose to hedge foreign currency risk associated with financing transactions such as third-party and intercompany debt and other balance sheet items. The foreign currency forward exchange contracts related to balance sheet items denominated in foreign currency are reviewed on a contract-by-contract basis and are designated accordingly. If these foreign currency forward exchange contracts do not qualify for hedge accounting, then the Company records these contracts at fair value on its balance sheet and the related gains and losses are immediately recognized in the statement of operations where there is an equal and offsetting entry related to the underlying exposure.

The fair value of foreign currency forward exchange contracts is determined by using observable market transactions of spot and forward rates (i.e., Level 2 inputs) which is discussed further in Note 12. Additionally, netting provisions are provided for in existing



International Swap and Derivative Association Inc. 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.

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

As of June 30, 2014, the Company had outstanding hedge contracts for the sale of \$17 million of foreign currencies at fixed rates. As of June 30, 2014, the Company had no deferred gains or losses in comprehensive loss related to foreign exchange hedging. As of September 30, 2013, the Company had outstanding hedge contracts for the sale of \$1.044 billion and the purchase of \$249 million of foreign currencies at fixed rates. As of September 30, 2013, the Company had no deferred gains or losses in comprehensive loss related to foreign exchange hedging.

The following is a summary of amounts recorded in the Consolidated Balance Sheet pertaining to the Company's use of foreign currency derivatives at June 30, 2014 and September 30, 2013:

	June 30, 2014	September 30, 2013 <sup>(b)</sup>
	(in millions)	
Other current assets	\$—	\$ 1
Other current liabilities	—	(23 )

(a) Includes less than \$1 million of foreign exchange derivative contracts in asset and liability positions.

(b) Includes \$5 million and \$27 million of foreign exchange derivative contracts in asset and liability positions, respectively.

## 10. 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, which also represent the reportable segments of the Company. 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, 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, 2013. The Company accounts for intersegment sales at fair value as if the sales were to third parties. While intercompany 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, and therefore, do not themselves impact consolidated results. Segment information consisted of the following:

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Three Months Ended	Recorded Music	Music Publishing	Corporate expenses and eliminations	Total
	(in millions)			
<b>June 30, 2014</b>				
Revenues	\$656	\$ 137	\$ (5 )	\$788
OIBDA	71	24	(29 )	66
Depreciation of property, plant and equipment	(9 )	(2 )	(3 )	(14 )
Amortization of intangible assets	(51 )	(16 )	—	(67 )
Operating income (loss)	\$11	\$ 6	\$ (32 )	\$(15 )
<b>June 30, 2013</b>				
Revenues	\$534	\$ 134	\$ (5 )	\$663
OIBDA	62	28	(21 )	69
Depreciation of property, plant and equipment	(8 )	(1 )	(4 )	(13 )
Amortization of intangible assets	(32 )	(16 )	—	(48 )
Operating income (loss)	\$22	\$ 11	\$ (25 )	\$8

Nine Months Ended	Recorded Music		Corporate	Total
	Music	Publishing	expenses and eliminations	
	(in millions)			
<b>June 30, 2014</b>				
Revenues	\$1,882	\$ 387	\$ (13 )	\$2,256
OIBDA	203	98	(68 )	233
Depreciation of property, plant and equipment	(26 )	(4 )	(9 )	(39 )
Amortization of intangible assets	(150 )	(49 )	—	(199 )
Operating income (loss)	\$27	\$ 45	\$ (77 )	\$(5 )
<b>June 30, 2013</b>				
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

## 11. Additional Financial Information

### Cash Interest and Taxes

The Company made interest payments of approximately \$70 million and \$64 million during the three months ended June 30, 2014 and June 30, 2013, respectively. The Company made interest payments of approximately \$171 million and \$174 million during the nine months ended June 30, 2014 and June 30, 2013, respectively. The Company paid approximately \$6 million and \$10 million of income and withholding taxes, net of refunds, during the three months ended June 30, 2014 and June 30, 2013, respectively. The Company paid approximately \$14 and \$18 million of income and withholding taxes, net of refunds, during the nine months ended June 30, 2014 and June 30, 2013.

## 12. Fair Value Measurements

FASB ASC Topic 820, Fair Value Measurements and Disclosures (“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.

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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, 2014 and September 30, 2013.

	Fair Value Measurements as of June 30, 2014			
	(Level 1)	(Level 2)	(Level 3)	Total
(in millions)				
<b>Other Current Assets:</b>				
Foreign Currency Forward Exchange Contracts (a)	\$ —	\$ —	\$ —	\$ —
<b>Other Current Liabilities:</b>				
Foreign Currency Forward Exchange Contracts (a)	—	—	—	—
<b>Other Current Liabilities:</b>				
Contractual Obligations (b)	—	—	(2 )	(2 )
<b>Other Non-Current Liabilities:</b>				
Contractual Obligations (b)	—	—	(7 )	(7 )
<b>Total</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ (9 )</b>	<b>\$ (9 )</b>

	Fair Value Measurements as of September 30, 2013			
	(Level 1)	(Level 2)	(Level 3)	Total
(in millions)				
<b>Other Current Assets:</b>				
Foreign Currency Forward Exchange Contracts (a)	\$ —	\$ 1	\$ —	\$ 1
<b>Other Current Liabilities:</b>				
Foreign Currency Forward Exchange Contracts (a)	—	(23 )	—	(23 )
<b>Other Current Liabilities:</b>				
Contractual Obligations (b)	—	—	(13 )	(13 )
<b>Other Non-Current Liabilities:</b>				
Contractual Obligations (b)	—	—	(9 )	(9 )
<b>Total</b>	<b>\$ —</b>	<b>\$ (22 )</b>	<b>\$ (22 )</b>	<b>\$ (44 )</b>

(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 the Company's 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 the Company's various acquisitions and the expected timing of the payment.

The following table reconciles the beginning and ending balances of net liabilities classified as Level 3:

Total  
(in millions)

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Balance at September 30, 2013	\$	22
Additions		2
Reductions		(2 )
Payments		(13 )
Balance at June 30, 2014	\$	9

The decrease in net liabilities classified as Level 3 was primarily related to contingent consideration payments made during the period.

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 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.

#### Fair Value of Debt

The Company had \$3.052 billion of principal debt outstanding at June 30, 2014, of which \$1.303 billion was variable rate debt and \$1.749 billion was fixed rate debt. Based on the level of interest rates prevailing at June 30, 2014, the fair value of the Company's debt was approximately \$3.098 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.

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. had issued and outstanding, as of June 30, 2014, the 5.625% Senior Secured Notes due 2022, the 6.00% Senior Secured Notes due 2021, the 6.25% Senior Secured Notes due 2021 and the 6.75% Senior Notes due 2022 (together, the “Acquisition Corp. Notes”).

The Holdings Notes are guaranteed by the Company. This guarantee is full and unconditional. 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), which are not guarantors of the Holdings Notes, 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 Acquisition Corp. Notes are, or were, 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. The Company’s guarantee of the Acquisition Corp. Notes is full and unconditional. The guarantee of the Acquisition Corp. Notes by Acquisition Corp.’s domestic, wholly-owned subsidiaries 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 New Senior Secured Notes and the New Unsecured Notes are also guaranteed by the Company and, in addition, are guaranteed by all of Acquisition Corp.’s domestic wholly owned subsidiaries.

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.



## WARNER MUSIC GROUP CORP.

## Supplementary Information

## Consolidating Balance Sheet (Unaudited)

June 30, 2014

	WMG Acquisition Corp. (issuer) (in millions)	Non- Guarantor Subsidiaries	Guarantor Subsidiaries	Elimination	WMG Acquisition Corp. Consolidated	WMG Holding Corp. (issuer)	Warner Music Group Corp.	Elimination	Warner Music Group Corp. Consolidated
<b>Assets:</b>									
<b>Current assets:</b>									
Cash and equivalents	\$—	\$ 34	\$ 108	\$—	\$ 142	\$—	\$—	\$—	\$ 142
Accounts receivable, net	—	161	288	—	449	—	—	—	449
Inventories	—	10	27	—	37	—	—	—	37
Royalty advances expected to be recouped within one year	—	56	45	—	101	—	—	—	101
Deferred tax assets	—	20	23	—	43	—	—	—	43
Prepaid and other current assets	5	8	59	—	72	—	—	—	72
<b>Total current assets</b>	<b>5</b>	<b>289</b>	<b>550</b>	<b>—</b>	<b>844</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>844</b>
Due (to) from parent companies	973	(191 )	(782 )	—	—	—	—	—	—
Investments in and advances to (from) consolidated subsidiaries	2,523	1,196	—	(3,719 )	—	591	442	(1,033 )	—
Royalty advances expected to be recouped after one year	—	106	84	—	190	—	—	—	190
Property, plant and equipment, net	—	123	83	—	206	—	—	—	206
Goodwill	—	1,379	296	—	1,675	—	—	—	1,675
Intangible assets subject to amortization, net	—	935	2,043	—	2,978	—	—	—	2,978
Intangible assets not subject to amortization	—	75	46	—	121	—	—	—	121
Other assets	48	20	28	—	96	6	—	—	102
<b>Total assets</b>	<b>\$3,549</b>	<b>\$ 3,932</b>	<b>\$ 2,348</b>	<b>\$ (3,719 )</b>	<b>\$ 6,110</b>	<b>\$ 597</b>	<b>\$ 442</b>	<b>\$ (1,033 )</b>	<b>\$ 6,116</b>
<b>Liabilities and Deficit:</b>									
<b>Current liabilities:</b>									
Accounts payable	\$1	\$ 80	\$ 140	\$—	\$ 221	\$—	\$—	\$—	\$ 221
Accrued royalties	—	518	645	—	1,163	—	—	—	1,163
Accrued liabilities	—	54	207	—	261	—	—	—	261
Accrued interest	45	—	—	—	45	5	—	—	50

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Deferred revenue	—	143	87	—	230	—	—	—	230
Current portion of long-term debt	13	—	—	—	13	—	—	—	13
Other current liabilities	—	—	8	—	8	—	—	—	8
Total current liabilities	59	795	1,087	—	1,941	5	—	—	1,946
Long-term debt	2,883	—	—	—	2,883	150	—	—	3,033
Deferred tax liabilities, net	—	115	281	—	396	—	—	—	396
Other noncurrent liabilities	16	128	137	—	281	—	—	—	281
Total liabilities	2,958	1,038	1,505	—	5,501	155	—	—	5,656
Total Warner Music Group Corp. equity (deficit)	591	2,894	825	(3,719 )	591	442	442	(1,033 )	442
Noncontrolling interest	—	—	18	—	18	—	—	—	18
Total equity (deficit)	591	2,894	843	(3,719 )	609	442	442	(1,033 )	460
Total liabilities and equity (deficit)	\$3,549	\$ 3,932	\$ 2,348	\$ (3,719 )	\$ 6,110	\$ 597	\$ 442	\$ (1,033 )	\$ 6,116

## WARNER MUSIC GROUP CORP.

## Supplementary Information

## Consolidating Balance Sheet

September 30, 2013

	WMG Acquisition Corp. (issuer) (in millions)	Non- Guarantor Subsidiaries	Guarantor Subsidiaries	Elimination	WMG Acquisition Corp. Consolidated	WMG Holdings Corp. (issuer)	Warner Music Group Corp.	Elimination	Warner Music Group Corp. Consolidated
<b>Assets:</b>									
<b>Current assets:</b>									
Cash and equivalents	\$—	\$ 16	\$ 139	\$—	\$ 155	\$—	\$—	\$—	\$ 155
Accounts receivable, net	—	185	326	—	511	—	—	—	511
Inventories	—	10	23	—	33	—	—	—	33
Royalty advances expected to be recouped within one year	—	59	34	—	93	—	—	—	93
Deferred tax assets	—	21	22	—	43	—	—	—	43
Prepaid and other current assets	5	8	46	—	59	—	—	—	59
<b>Total current assets</b>	<b>5</b>	<b>299</b>	<b>590</b>	<b>—</b>	<b>894</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>894</b>
Due (to) from parent companies	799	(27 )	(772 )	—	—	—	—	—	—
Investments in and advances to (from) consolidated subsidiaries	2,811	930	—	(3,741 )	—	879	726	(1,605 )	—
Royalty advances expected to be recouped after one year	—	109	64	—	173	—	—	—	173
Property, plant and equipment, net	—	101	79	—	180	—	—	—	180
Goodwill	—	1,379	289	—	1,668	—	—	—	1,668
Intangible assets subject to amortization, net	—	1,007	2,100	—	3,107	—	—	—	3,107
Intangible assets not subject to amortization	—	75	45	—	120	—	—	—	120
Other assets	68	14	21	—	103	7	—	—	110
<b>Total assets</b>	<b>\$3,683</b>	<b>\$ 3,887</b>	<b>\$ 2,416</b>	<b>\$ (3,741 )</b>	<b>\$ 6,245</b>	<b>\$ 886</b>	<b>\$ 726</b>	<b>\$ (1,605 )</b>	<b>\$ 6,252</b>
<b>Liabilities and Deficit:</b>									
<b>Current liabilities:</b>									

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Accounts payable	\$—	\$ 96	\$ 184	\$ —	\$ 280	\$ —	\$ —	\$ —	\$ 280
Accrued royalties	—	570	577	—	1,147	—	—	—	1,147
Accrued liabilities	—	81	227	—	308	—	—	—	308
Accrued interest	65	—	—	—	65	10	—	—	75
Deferred revenue	—	56	83	—	139	—	—	—	139
Current portion of long-term debt	13	—	—	—	13	—	—	—	13
Other current liabilities	—	23	(4 )	6	25	—	—	—	25
Total current liabilities	78	826	1,067	6	1,977	10	—	—	1,987
Long-term debt	2,704	—	—	—	2,704	150	—	—	2,854
Deferred tax liabilities, net	—	128	311	—	439	—	—	—	439
Other noncurrent liabilities	22	81							