

Media Selling, 4th Edition

Part Three: Knowledge

Chapter 14 - Business and Finance

By William Redpath

Why Business and Finance in a Sales Book?

When you sell directly to a major advertiser, you should have some understanding of its financial condition as well as its marketing strategy, which you learned when you asked the Discovery Questions as outlined in Chapter 9. If you have a basic knowledge of financial terminology, you can talk to a company's CEO, CFO (chief financial officer), or CMO (chief marketing officer) more knowledgeably, which will give you an edge over the vast majority of competing salespeople.

On the other hand, when you sell to advertising agencies, it is important to talk their language – CPMs, CPPs, CPCs, reach, and frequency – not necessarily financial language.

Also, the majority of top managers in the media industry come from sales – general managers of radio and television stations and publishers of magazines and newspapers, for example. If you aspire to get into management, you should be familiar with accounting principles and financial statements outlined below.

Accounting Systems

Business systems such as accounting are important to understand because once a salesperson completes a sale, data from that sale are input into a medium's operations system. Data flows from this system into an organization's accounting system. The importance of the proper handling of insertion orders (IOs), scheduling of advertising, and monitoring the pace of sales and unsold inventory cannot be overstated, for a medium's financial health is at stake. All media organizations must comply with legal requirements such as reporting for tax purposes, financial reporting for publicly traded companies, and last, but not least, for the career health of sales managers and salespeople.

I know of a sales manager of a television station who was dismissed after the manager's station ran three Public Service Announcements (PSAs) during a Super Bowl telecast. Unsurprisingly, the station's general manager was watching and was less than amused.

Computers have revolutionized operations, production, and traffic systems. I remember working at radio stations during the 1970s at which traffic was done manually using long, thin cardboard-like strips that had advertisers' names and commercial lengths typed on them that were then inserted in chronological order into metal holders. Once the metal holder was filled, it was photocopied and the result was a program log listing the program to be aired and the commercials to be aired in those programs.

Today's systems and the reports they generate make that system look barbaric. Not only do current computerized systems manage data, they analyze it to help sales

management maximize revenue. Revenue management is the application of mathematical and analytical techniques, such as yield-management software, to determine prices in order to maximize revenue. Yield management is considered a branch of revenue management and has been used in the airline industry since the 1970s but is now used in many media industries, including broadcasting, cable, and Interactive.

Comprehensive data systems that interconnect traffic and operations to the accounting or business office are standard in media companies today. An accounting system supports all of the other departments of a media organization, including sales, and this accounting system manages accounts receivable, billing of advertising sold, and collections.

The importance of accounting should be obvious. While many people get involved in the media industries for reasons other than the bottom line, a media company, like any other business enterprise, must earn a profit in order to survive. The purpose of a sales department is to bring in the revenue that makes profitability possible. But, without accounting, one would not know if the quest for profitability were successful—profits come after subtracting expenses from revenue, and the accounting department keeps track of the revenue that salespeople generate.

Financial Reports

While some small media companies may report their historical financial performance using cash basis accounting, the vast majority of companies, including all that have to report their financial results to government agencies, such as public traded companies, or financial institutions to which these companies are indebted, use Generally Accepted Accounting Principles (or GAAP). While cash basis accounting is acceptable, but not mandatory, for tax reporting purposes, it is unacceptable for financial reporting purposes.

GAAP are set by the Financial Accounting Standards Board (FASB), a private organization based in Norwalk, Connecticut. GAAP change over time, as several new accounting principles are issued each year, on average.

GAAP mandates use of accrual accounting, which means that revenues must be recognized when actually earned – in the case of the media, when advertising runs – not when cash is collected. Expenses are recorded when services or goods are used, not when they are paid for.

The General Ledger, which lists all accounts in an accounting system, feeds into a company's financial statements. A complete set of financial statements will include the following:

1. A balance sheet, sometimes referred to as a Statement of Financial Position.
2. An income statement
3. A statement of cash flows
4. A statement of stockholders' equity.

Because of its relative unimportance to having a basic understanding of how businesses operate on the financial side, I will not address the statement of stockholders' equity.

Balance Sheet

Exhibit 14.1 shows an example of a balance sheet. This is the balance sheet for Ajax Communications, Inc., a fictitious publicly traded radio company.

Exhibit 14.1

AJAX COMMUNICATIONS, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except per share amounts)

	December 31,	
	2007	2006
ASSETS		
Current Assets:		
Cash and cash equivalents	\$1,765	\$778
Accounts receivable, net of allowance of \$719 and \$403 at December 31, 2001 and 2000, respectively	9,772	10,639
Other current assets	642	595
	<hr/>	<hr/>
Total current assets	12,179	12,012
Property and equipment, net	25,817	20,716
Intangible assets, net	266,420	217,897
Other assets, net	1,940	2,108
	<hr/>	<hr/>
Total assets	\$306,356	\$252,733
 LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$2,044	\$1,672
Accrued compensation	1,000	932
Other current liabilities	3,010	2,298
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Total current liabilities	6,054	4,902
Long-term debt, less current portion	87,019	45,010
Other long-term liabilities	75	84
Deferred taxes	4,870	4,317
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Total liabilities	98,018	54,313
 Stockholders' equity:		
Common stock	369	352

Treasury shares	(6,757)	(7,063)
Additional paid-in capital	270,694	259,386
Retained deficit	(55,968)	(54,255)
	<hr/>	<hr/>
Total stockholders' equity	208,338	198,420
	<hr/>	<hr/>
Total liabilities and stockholders' equity	\$306,356	\$252,733
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A balance sheet is always a financial snapshot at a single point in time. On a balance sheet, assets always equal the sum of liabilities and owners', or shareholders', equity. If that does not make sense offhand, think of it this way. If you have something – an asset – either someone else owns it, and thus, it is a liability, or you own it, and, thus, it becomes equity.

Assets are listed on the left side of the balance sheet in Exhibit 14.1 and liabilities and owners' equity are on the right side. Assets start with Current Assets, which include Cash and Cash Equivalents, which are stable value instruments with a maturity date less than 90 days into the future.

Accounts Receivable are current assets, as are Prepaid Expenses, assuming the service that was prepaid will be used within one year. Assets are also not supposed to be stated at more than their Net Realizable Value. Therefore, a reserve needs to be estimated for Accounts Receivable that are not likely to be collected.

While inventory is certainly a term used in media selling, it is not inventory in the usual sense of the term (i.e., merchandise currently owned by a retailer that is for sale) in the current assets section of a balance sheet. When inventory is accounted for on a balance sheet, it is usually accounted for using the FIFO (First In, First Out) or the LIFO (Last In, First Out) method in terms of recognizing which items to expense and which to retain in inventory. Inventory accounting is usually not an issue for businesses in non-inflationary times.

Long-term assets are those that are expected to be used over a period longer than one year, and they usually start with Property, Plant and Equipment (PP&E), also known as tangible assets. PP&E is stated at cost less depreciation and amortization over the course of its life. Over the lives of tangible assets, the depreciation and amortization systematically reduce the assets' net values. Land is not depreciated for either financial reporting or tax purposes because it is not a depreciating asset like printing presses are, for example, which wear out. Land does not wear out and need to be replaced.

Sometimes companies list intangible assets as long-term, non-current, assets. In the media industries, the most valuable intangible assets include FCC licenses, cable franchises, network affiliation agreements, and customer mailing and subscriber lists.

Program rights are a major intangible asset category for television companies. As with PP&E, program rights are booked when they are purchased and amortized as they are used, when the programs are aired.

Intangible assets are recognized, or booked, only if they are acquired alone or as part of a going concern business. Self-created intangible assets are not booked if they are developed internally. That is, if a salesperson develops a relationship with a particular advertiser or advertising agency that leads to revenue, that is not recognized as an asset

on the books of the station. There can be many valuable self-created intangible assets with a company, but they are never explicitly recognized on the balance sheet. This is part of the tenet of conservatism of financial statements, to be addressed later in this chapter.

After intangible assets are acquired, they are amortized, almost without exception, in a straight line over 15 years for tax purposes (assuming they are acquired as part of an ongoing business in an asset transaction). For financial reporting purposes, intangible assets that have a finite life are amortized (decreased in value), with that amount recognized as an expense on the income statement, year by year, over the useful lives of the assets. Intangible assets that have an indefinite life are not amortized but are reviewed each year to make sure that their values on the financial statements, also known as book value or carrying value, is not greater than their fair values. If an asset's fair value is less than its book value, its book value must be reduced to be equal to its fair value, with the difference recognized as an expense on the income statement in that year.

Other Assets are other long-term assets that may have significant value; sometimes well above their book value. I once heard a business appraiser at a valuation conference state that he just about signed a valuation report valuing the equity of a closely-held corporation when it dawned on him to inquire as to what was included in the Other Assets of that corporation. The book value of Other Assets was quite low and the assets, therefore, appeared minor in nature at first glance. What he learned was that it was Wal-Mart Stores stock that had been acquired many years earlier. In the interim, the stock had appreciated many times over, so his valuation would have been wrong if he had just assumed that the book value of Other Assets was the fair market value of Other Assets.

Historical cost and Net Realizable Value are used in financial statements because of the concept of conservatism in historical financial statements. With the exception of certain marketable securities, assets are booked at cost and never increased in book value, even if they increase in fair market value. Conservatism is supposed to be an essential tenet of financial statements, even though one might not know it from recent financial scandals involving major corporations. Conservatism brings greater credibility to financial statements so that people using financial statements can know that claims made on financial statements are reliable and not overstated.

Looking at the right side of the balance sheet in Exhibit 14.1, Current Liabilities are liabilities such as Accounts Payable or Accrued Expenses, goods or services used that have not been paid for yet and that are to be paid for in less than one year. That also includes the portion of long-term debt that is payable in less than one year, if any. Current Assets minus Current Liabilities equals Working Capital.

Long-term debt consists of loans, notes, and bonds that have maturity dates more than one year into the future. Program payments to be paid in the future are also listed as liabilities, with payments to be made within the next year listed as a current liability. Prepaid magazine and newspaper subscriptions are also considered a liability because subscribers are owed magazines or newspapers in the future.

The shareholders' equity section of the balance sheet is on the bottom right of Exhibit 14.1, and it lists the various types of equity including preferred stock, if any, and various classes of common stock. The book values of some of these items may not be

even close to the fair market value of those securities. The book value of shareholders' equity can be negative, but, of course, the market value of an equity security cannot go below zero.

In terms of order of interests to be paid off upon liquidation of a corporation, debt has priority over preferred stock, which has priority over common stock. That is why preferred stock is called preferred, even though returns for holders of common stock have been higher over time. Common stock is the residual, or last, claimant on a liquidated corporation and is, therefore, considered riskier than other securities of a corporation.

Income Statement

An income statement, which can be seen in Exhibit 14.2, covers a period of time such as one month or one year. Exhibit 14.2 is the publicly reported income statements for Ajax Communications, Inc. for fiscal years 2005, 2006 and 2007.

Exhibit 14.2

AJAX COMMUNICATIONS, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, except per share amounts)

	Year ended December		
	2007	31, 2006	2005
Gross broadcast revenues	\$59,339	\$48,324	\$25,613
Less agency commissions	5,594	4,217	1,759
Net broadcast revenues	<u>53,745</u>	<u>44,107</u>	<u>23,854</u>
Station operating expenses	38,530	30,173	18,325
Depreciation and amortization	13,436	8,602	3,368
Corporate general and administrative expenses	4,857	4,501	2,773
Operating (loss) income	<u>(3,078)</u>	<u>831</u>	<u>(612)</u>
Interest expense	(3,279)	(4,229)	(5,249)
Gain (loss) on exchange/sale of radio stations	4,444	17,504	(602)
Other (expense) income, net	(465)	860	163
(Loss) income before income taxes and extraordinary items	<u>(2,378)</u>	<u>14,966</u>	<u>(6,300)</u>
Income tax benefit	665	0	0
(Loss) income before extraordinary items	<u>(1,713)</u>	<u>14,966</u>	<u>(6,300)</u>
Extraordinary loss from debt extinguishment,			

net of taxes	0	(1,114)	(471)
Net (loss) income	<u>(1,713)</u>	<u>13,852</u>	<u>(6,771)</u>
Loss applicable to common shares			
Net (loss) income	(1,713)	13,852	(6,771)
Preferred stock dividend requirements	0	(629)	(5,205)
Preferred stock accretion	0	(26,611)	(17,221)
Loss applicable to common shares	<u>(1,713)</u>	<u>(13,388)</u>	<u>(29,197)</u>
Basic and diluted loss per common share:			
Loss before extraordinary items	(\$0.05)	(\$0.39)	(\$119.69)
Extraordinary items	0.00	(0.03)	(1.96)
Net loss per common share	(\$0.05)	(\$0.42)	<u>(\$121.65)</u>

In internal financial statements, the income statement style I prefer shows revenue and expense categories down the middle, with the past month's actual results, past month's budget, with plus or minus variance percentage, and past month for the previous year, with plus or minus variance percentage, on the left. On the right, there should be year-to-date actual results, a year-to-date budget, with plus or minus variance percentage, and year-to-date for the previous year with plus or minus variance percentage. This style is seen by going to www.mediaselling.us and clicking on "Chapter 14, Internal Income Statement."

With an income statement, revenues are, of course, listed at the top. Revenues are usually listed by category such Local, Regional, National, Network Compensation, Political, Trade, Production, Equipment Leasing.

Subtracted from gross revenues in media industry financial statements are advertising agency commissions and commissions paid to national sales representative firms. This reporting is somewhat incongruous, in my opinion, because advertising agencies are agents of advertisers, while national sales representative firms work for the media companies. Local salespeople also work for local media companies, but their commissions are included in sales department expense, which is an expense that is listed below net revenues. Nevertheless, this has been the standard industry accounting treatment of national sales representative expenses for a long time and there is little prospect of that changing.

Be careful when looking at reported or estimated market revenues in the media, and in radio and television in particular. You need to know if they include trade revenues or not; generally, they do not, but sometimes they do. It is particularly important to know when you are estimating the revenue share of a radio or television station within its market. As with anything else, you do not want to compare apples with oranges.

Expenses are best listed by functional departments in income statements, with a more detailed list of expenses by category within functional departments below the list of functional departments.

It is important to know exactly what someone means when they use the term Operating Income. In the media industries, that term is frequently used to mean either Operating Cash Flow (OCF), which is the case most of the time, or Earnings Before Interest Taxes, Depreciation, and Amortization (EBITDA). However, in financial statements among most non-media businesses, the term Operating Income is synonymous with Earnings Before Interest and Taxes (EBIT). Therefore, depreciation and amortization is treated as an operating expense in the financial statements. If depreciation and amortization expense is not given its own line in the income statement, it will have a separate line in the Statement of Cash Flows. It is a reconciling item between Net Income and Cash from Operating Activities, because it is a non-cash expense. Adding depreciation and amortization expense back to EBIT will give you EBITDA.

To get from EBITDA to OCF, corporate overhead expenses, sometimes called management fees, which are charged, for example, by a corporate headquarters office to each of its owned media properties, must be added back. The only expenses that should be deducted from revenues in arriving at OCF are operating expenses of an operating unit, such as a television station, excluding corporate management expense and depreciation and amortization expense. Historically, OCF has been the most recognized profitability measure in the media industry.

It is very important to know what OCF is not, however. It is not a measure of true cash flow in the literal sense of the term. OCF is not a profit measure that is recognized in Generally Accepted Accounting Principles (GAAP) and it is not equivalent to Cash Flow from Operations that is seen in the Statement of Cash Flows, which is part of a complete set of financial statements.

Operating Cash Flow may be defined differently by different people. I know someone whom I greatly respect who defines OCF without including trade revenues or trade expenses. Including them in calculating OCF may change OCF in a given year due to timing differences of revenue and expense recognition, but inclusion of trade revenues and trade expenses is part of GAAP.

There are other problems associated with OCF and EBITDA, so it should definitely not be used as the only measure of earnings of a business. Among the problems is that EBITDA and OCF never take into account either depreciation or amortization of a business' assets, capital expenditures for new equipment, or expenditures for purchases of other businesses. EBITDA and OCF also ignore additions to working capital and overstate cash flow in periods when growth of working capital is necessary to sustain a business and nurture its growth.

In analyzing media company financial statements, besides knowing whether they are cash or accrual basis financial statements, one should know how trade revenue is treated. In the media industries, advertising time is frequently traded not for cash, but for goods or services. In television, sometimes programs are purchased for a station with no cash outlay, but the program supplier gets to keep a certain number of commercial availabilities to sell to local advertisers within the program. Other radio or television

stations may trade the use of a new car for the general manager in return for commercials on the station, without any cash actually changing hands. Trade deals are also often referred to as barter deals. Financial Accounting Standard (FAS) 63 states that all trade and barter revenue should be recorded at the estimated value of the goods or services received. FAS 63 also states that, as with cash transactions, trade revenue is recognized when earned and trade expense is recognized when a good or service is used. If goods or services are received before commercials are aired, a liability for the advertising must be recognized until the commercial is aired. If the commercial is broadcast before the goods or services are received, an asset must be recognized until the goods or services are used by the station.

Frequently in these financial statements, trade revenues and expenses are listed separately, below the line--below the determination of OCF and EBITDA on the income statement. Some income statements will list trade revenues among the gross revenues and list trade expenses among the regular operating expenses. Still other income statements, although a small minority, will make no distinction between cash and trade revenues on the income statement, simply including trade revenues with cash revenues in the appropriate category of gross revenues. Some financial statements (although not GAAP compliant) do not recognize trade revenues and trade expenses at all. Because trade revenues and expenses can be much higher in the media industry than in other kinds of businesses, it is important to know how they are accounted for.

Even though it seems obvious that trade involves no exchange of cash, it is important that the terms of trade deals struck by stations with various advertisers are understood by station executives. I know of a program director of a television station that did not use all of a trade with a local department store. The trade was advertising time in exchange for clothing for news anchors and other on-air personnel. There was a time expiration on the clothing side of the trade. When asked why some of the trade credit went unused, the program director said, "I thought I was saving the station money." Instead, the station was shortchanged some clothing. If you're in charge of effecting either side of a trade deal, be sure you know all the parameters of the deal, as well as how the accounting for the trade is to be handled.

Because trade deals can be easily abused (e.g., merchandise received in a trade can be stolen, or services can be diverted to personal, rather than business, use), internal management controls must be in place in the approval process, and to make sure the trade deals are implemented and executed properly.

There is a lot of chatter and slang used about margins, profit margins, or cash flow margins, especially in the media industry. A margin is a percentage, or a ratio, with a numerator and denominator. If you do not know for sure what the numerator and denominator are, and I mean not what the numbers are specifically but what they represent, ask. Is the ratio Operating Cash Flow divided by gross revenues or something else? What you may find is that the person dispensing the margin information does not know what constitutes the ratio.

Statement of Cash Flows

The Statement of Cash Flows, as seen in Exhibit 14.3, is a very important financial statement, because this shows the actual cash flows of a business entity. Remember, the

term Operating Cash Flow is a misnomer and should not be relied upon for flows of actual cash.

Exhibit 14.3

AJAX COMMUNICATIONS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	2006	Year ended December 31, 2005	2004
Cash flows from operating activities:			
Net (loss) income	(\$1,713)	\$13,852	(\$6,771)
Adjustments to reconcile net (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	13,436	8,602	3,368
Provision for doubtful accounts	822	725	390
Non-cash interest expense	283	1,579	1,576
Non-cash charge for debt extinguishments	0	1,114	471
Non-cash charge for compensation	491	0	0
(Gain) loss on sale of radio stations	(4,444)	(17,504)	477
Loss on sale of fixed assets and other	160	0	0
Changes in operating assets and liabilities, net of acquisitions:			
Accounts receivable	(328)	(6,249)	(1,481)
Other assets	(107)	(358)	(36)
Current and long-term liabilities	(803)	(2,940)	(372)
Deferred taxes	553	4,317	0
	8,350	3,138	(2,378)
Cash flows from investing activities:			
Acquisitions of radio stations, net of cash acquired, and escrow deposits on pending acquisitions:	(63,450)	(148,940)	(27,533)
Capital expenditures	(3,161)	(1,719)	(1,978)
Net proceeds from sale of radio stations	13,393	2,000	13,999

Proceeds from sale of fixed assets	27	0	0
	<hr/>	<hr/>	<hr/>
	(53,191)	(148,659)	(15,512)
Cash flows from financing activities:			
Proceeds from issuance of redeemable convertible preferred stock	0	0	41,754
Proceeds from issuance of common stock	4,068	156,939	0
Proceeds from long-term debt	60,500	48,500	16,500
Principal payments on long-term debt	(18,491)	(28,824)	(26,704)
Payment of notes payable	0	0	(7,500)
Payment for deferred financing costs	0	(1,904)	(427)
Payment of issuance costs	(249)	(11,606)	(2,802)
Treasury stock purchases	0	(7,063)	0
Dividends paid on all series of preferred stock	0	(8,153)	0
Redemption of Series B preferred stock	0	(5,000)	0
	<hr/>	<hr/>	<hr/>
	45,828	142,889	20,821
Net increase (decrease) in cash and cash equivalents	987	(2,632)	2,931
Cash and cash equivalents at beginning of period	<hr/>	<hr/>	<hr/>
	778	3,410	479
	<hr/>	<hr/>	<hr/>
Cash and cash equivalents at end of period	\$1,765	\$778	\$3,410

The Statement of Cash Flows is divided into three sections: Cash Flows from Operating Activities, Cash Flows from Investing Activities, and Cash Flows from Financing Activities. Operating activities are the operation of the business; investing activities include things such as capital expenditures; financing activities include the raising of cash through the sale of debt and equity securities, or the buyback of those securities, interest payments and dividend payments. It is in the Statement of Cash Flows that one really sees the true cash flows in a business or an entity that owns a business. Cash, after all, is the true lifeblood of a business. Regardless of other assets, revenues, or profitability, if a business does not have cash, or cannot raise cash, it cannot function.

One of the most important parts of a full set of financial statements are the footnotes. You should be able to read and understand footnotes because they amplify and elucidate other portions of the financial statements. If you do not understand what you read in financial footnotes, ask the entity's management or their investor relations department. Do not be satisfied with vague explanations that do not make complete

sense. Any questions about the financial statements, including the footnotes, should be answered clearly and forthrightly for you, assuming you have a right to know or a need to know. If you are a salesperson looking at financial statements to see if a company is creditworthy or has enough money to be a good prospect, you can ask someone in your own business or accounting department, or ask your company's accounting or auditing firm to help you.

Financial Information

Historical financial information on all companies that file reports with the Securities and Exchange Commission (SEC) can be found through numerous online services, and through the SEC's website at www.sec.gov.

Many radio and television stations voluntarily participate in market revenue compilations. In many, but not all, radio and television markets, an accounting firm or some other entity is hired to survey all the radio or television stations in that market regarding the amounts of their respective revenues. The survey taker keeps each station's submission confidential, but adds the data for all stations together and then sends the market totals to every station, along with the overall rank number for that station, and its rank in various revenue categories. This information illuminates the market revenue situation for everyone and allows management to see objectively how their station(s) stack up versus intramarket competition. The National Association of Broadcasters (NAB) publishes an annual book on television market revenues for many surveyed television markets, and it can be purchased from the NAB.

Other historical broadcasting data, including radio and television market revenues, is estimated and published by several firms. BIA Financial Network, Inc. (website: www.bia.com) publishes several reference books on the radio and television industries, including a unique software reference source called *Media Access Pro*. BIA plans to publish reference books and software on other media and telecommunications industries in the future.

The Internet Advertising Bureau (IAB) publishes revenue information on its website, www.iab.net/resources/ad_revenue.asp. *Advertising Age* magazine every year publishes magazine revenue, number of advertising pages sold, and circulation for the top 300 magazines and the information can be found on www.adage.com.

Types of Financial Statements

Financial statements are always the product of management, but are compiled, reviewed, or audited by outside accountants. There are essentially four types of financial statements:

1. Internal financial statements. These are statements that are produced by management. These are usually done on an accrual basis but are sometimes done on a cash basis, particularly in smaller companies.
2. Compiled financial statements. These financial statements are developed by an outside accountant or accounting firm based on information supplied by a client. The data is accepted essentially without review or questioning by the outside accountant.
3. Reviewed financial statements. These are financial statements for which an accountant performs some analytical and review procedures trying to identify major problems that

need correction, if any. These procedures are far less than those employed in a full audit.

4. Audited financial statements. This is a full set of financial statements, including footnotes, that include an audit opinion from an outside, independent accounting firm as to whether the financial statements are stated in accordance with GAAP. Audits are performed in accordance with Generally Accepted Auditing Standards (GAAS). Audited financial statements are mandated by the SEC for any annual financial statements that are filed with it. Companies that have any publicly traded debt or equity must file with the SEC, except for certain very small companies. Also, it is a standard covenant in loan agreements that the debtor give annual audited financial statements to the creditor as long as the loan is outstanding. Business partners or shareholders in closely-held companies sometimes demand audited financial statements as a condition of their investment.

Test Yourself

1. What is the full name of the accounting rules in the United States?
2. Does GAAP mandate cash or accrual accounting?
3. What are the three types of financial statements reviewed in this chapter?
4. Assets always equal what plus what?
5. Gross revenues minus what two items equals net revenues?
6. Name some major intangible assets for media companies.
7. What is the difference between OCF and EBITDA?
8. What is the difference between EBITDA and EBIT?
9. What is the difference between Operating Income (as usually defined in the media industries) and Operating Income in most other industries?
10. Why is the term “Operating Cash Flow” a misnomer?
11. Is trade revenue and trade expense included in revenues and expenses in GAAP?
12. What are the three sections of the Statement of Cash Flows?
13. What are the four types of financial statements?

Project

Go to the Web site of Viacom at www.viacom.com. Click on the “Investors Relations” link and then on the “financial announcements” link. Look at the Earnings Releases and click on “4th Quarter ‘07.” Does Viacom report EBITDA? What does it report?

Resources

www.adage.com/datacenter. (*Advertising Age* magazine’s Web site and its Data Center contain a wealth of information)

www.bia.com. (Media industry data, including industry financial data)

<http://investing.businessweek.com/research/company/overview/overview.asp>.

(BusinessWeek’s Company Insight Center provides detailed stock information and trends for publicly traded companies)

www.iab.net/resources/ad_revenue.asp. (The IAB’s revenue reports)

www.kagan.com. (Information about the media industry)

www.nab.org. (The National Association of Broadcasters (NAB) produces some of the best industry financial data among all trade associations)

www.sec.gov. (Securities and Exchange Commission.)