GRAY TELEVISION INC
Form 10-Q
August 07, 2014
**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-Q**

**(Mark one)**

**[X] Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**For the quarterly period ended June 30, 2014 or**

**[ ] Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**For the transition period from _________ to _________ .**

**Commission file number 1-13796**

**Gray Television, Inc.**
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Georgia**<br>(State or other jurisdiction of incorporation or organization) | **58-0285030**<br>(I.R.S. Employer Identification Number) |
| **4370 Peachtree Road, NE, Atlanta, Georgia**<br>(Address of principal executive offices) | **30319**<br>(Zip code) |

**(404) 504-9828**
(Registrant's telephone number, including area code)

**Not Applicable**
(Former name, former address and former fiscal year, if changed since last report.)

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 periods 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 website, 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 “small 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 _____

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

| | |
|---|---|
| **Common Stock (No Par Value)** | **Class A Common Stock (No Par Value)** |
| **52,533,586 shares outstanding as of July 31, 2014** | **5,989,314 shares outstanding as of July 31, 2014** |

## INDEX

**GRAY TELEVISION, INC.**

**PART I. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**GRAY TELEVISION, INC.**

**CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)**

(in thousands)

| | June 30, 2014 | December 31, 2013 |
|---|---|---|
| **Assets:** | | |
| Current assets: | | |
| Cash | $66,070 | $13,478 |
| Accounts receivable, less allowance for doubtful accounts of $915 and $730, respectively | 84,149 | 70,047 |
| Current portion of program broadcast rights, net | 2,900 | 7,656 |
| Deferred tax asset | 34,112 | 34,113 |
| Prepaid and other current assets | 11,744 | 5,293 |
| Total current assets | 198,975 | 130,587 |
| | | |
| Property and equipment, net | 191,448 | 143,621 |
| Deferred loan costs, net | 18,269 | 17,293 |
| Broadcast licenses | 936,806 | 838,982 |
| Goodwill | 320,127 | 184,409 |
| Other intangible assets, net | 40,972 | 2,644 |
| Investment in broadcasting company | 13,599 | 13,599 |
| Other | 2,943 | 3,289 |
| Total assets (1) | $1,723,139 | $1,334,424 |

**See notes to condensed consolidated financial statements.**

**GRAY TELEVISION, INC.**

**CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)**

(in thousands except for share data)

| | June 30, 2014 | December 31, 2013 |
|---|---|---|
| **Liabilities and stockholders' equity:** | | |
| Current liabilities: | | |
| Accounts payable | $2,778 | $2,256 |
| Employee compensation and benefits | 17,240 | 16,759 |
| Accrued interest | 13,649 | 12,703 |
| Accrued network programming fees | 3,895 | 2,467 |
| Other accrued expenses | 5,831 | 5,158 |
| Federal and state income taxes | 1,232 | 1,550 |
| Current portion of program broadcast obligations | 3,148 | 9,707 |
| Deferred revenue | 6,461 | 2,522 |
| Acquisition related liabilities | 9,913 | 9,739 |
| Current portion of long-term debt | 5,453 | 224 |
| Total current liabilities | 69,600 | 63,085 |
| | | |
| Long-term debt, less current portion | 1,202,845 | 842,650 |
| Program broadcast obligations, less current portion | 1,383 | 1,520 |
| Deferred income taxes | 241,592 | 225,407 |
| Accrued pension costs | 27,300 | 26,925 |
| Other | 768 | 827 |
| Total liabilities (1) | 1,543,488 | 1,160,414 |
| | | |
| Commitments and contingencies (Note 7) | | |
| | | |
| Stockholders' equity: | | |
| Common stock, no par value; authorized 100,000,000 shares, issued 57,324,919 shares and 57,010,878 shares, respectively | 485,118 | 483,055 |
| Class A common stock, no par value; authorized 15,000,000 shares, issued 7,567,868 shares and 7,331,574 shares, respectively | 16,322 | 15,321 |
| Accumulated deficit | (248,132) | (251,000) |
| Accumulated other comprehensive loss, net of income tax benefit | (10,409) | (10,409) |
| | 242,899 | 236,967 |
| Treasury stock at cost, common stock, 4,791,481 shares and 4,768,925 shares, respectively | (40,850) | (40,559) |
| Treasury stock at cost, Class A common stock, 1,578,554 shares | (22,398) | (22,398) |
| Total stockholders' equity | 179,651 | 174,010 |
| Total liabilities and stockholders' equity | $1,723,139 | $1,334,424 |

**See notes to condensed consolidated financial statements.**

(1) Our consolidated total assets as of June 30, 2014 and December 31, 2013 included total assets of $6.4 million and $6.8 million, respectively, of a variable interest entity ("VIE"). These assets can only be used to settle the obligations of the VIE. Our consolidated total liabilities as of June 30, 2014 and December 31, 2013 included total liabilities of $3.0 million and $3.1 million, respectively, of the VIE. As of June 30, 2014 and December 31, 2013, the creditors of the VIE had recourse against Gray for $2.9 million and $3.0 million of these liabilities, respectively.

**GRAY TELEVISION, INC.**

**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)**

(in thousands except for per share data)

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | June 30, | | June 30, | |
| | 2014 | 2013 | 2014 | 2013 |
| Revenue (less agency commissions) | $107,249 | $84,285 | $198,546 | $162,454 |
| Operating expenses before depreciation, amortization and loss (gain) on disposal of assets, net: | | | | |
| Broadcast | 66,002 | 51,807 | 126,386 | 105,301 |
| Corporate and administrative | 9,848 | 5,293 | 16,347 | 9,117 |
| Depreciation | 6,986 | 5,938 | 13,370 | 11,738 |
| Amortization of intangible assets | 1,179 | 12 | 1,468 | 31 |
| Loss (gain) on disposals of assets, net | 48 | (77) | 379 | (105) |
| Operating expenses | 84,063 | 62,973 | 157,950 | 126,082 |
| Operating income | 23,186 | 21,312 | 40,596 | 36,372 |
| Other income (expense): | | | | |
| Miscellaneous income (expense), net | 3 | (1) | 3 | - |
| Interest expense | (15,825) | (12,594) | (31,099) | (25,134) |
| Loss from early extinguishment of debt | (4,897) | - | (4,897) | - |
| Income before income taxes | 2,467 | 8,717 | 4,603 | 11,238 |
| Income tax expense | 876 | 3,573 | 1,735 | 5,224 |
| Net income | 1,591 | 5,144 | 2,868 | 6,014 |
| | | | | |
| Basic per share information: | | | | |
| Net income | $0.03 | $0.09 | $0.05 | $0.10 |
| Weighted-average shares outstanding | 57,862 | 57,561 | 57,855 | 57,542 |
| | | | | |
| Diluted per share information: | | | | |
| Net income | $0.03 | $0.09 | $0.05 | $0.10 |
| Weighted-average shares outstanding | 58,311 | 57,939 | 58,298 | 57,820 |
| | | | | |
| Dividends declared per common share | $- | $- | $- | $- |

**See notes to condensed consolidated financial statements.**

**GRAY TELEVISION, INC.**

**CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY (Unaudited)**

(in thousands, except for number of shares)

| | **Class A Common Stock** | | **Common Stock** | | **Accumulated** | **Class A Treasury Stock** | | **Common Treasury Stock** | |
|---|---|---|---|---|---|---|---|---|---|
| | **Shares** | **Amount** | **Shares** | **Amount** | **Deficit** | **Shares** | **Amount** | **Shares** | **Amount** |
| Balance at December 31, 2013 | 7,331,574 | $15,321 | 57,010,878 | $483,055 | $(251,000) | (1,578,554) | $(22,398) | (4,768,925) | $(40,559) |
| Net income | - | - | - | - | 2,868 | - | - | - | - |
| Issuance of common stock: | | | | | | | | | |
| 401(k) plan | - | - | 1,080 | 13 | - | - | - | - | - |
| 2007 Long Term Incentive Plan - restricted stock | 236,294 | - | 312,961 | - | - | - | - | (22,556) | (291) |
| Share-based compensation | - | 1,001 | - | 2,050 | - | - | - | - | - |
| Balance at June 30, 2014 | 7,567,868 | $16,322 | 57,324,919 | $485,118 | $(248,132) | (1,578,554) | $(22,398) | (4,791,481) | $(40,850) |

**See notes to condensed consolidated financial statements.**

**GRAY TELEVISION, INC.**

**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)**

(in thousands)

| | Six Months Ended June 30, 2014 | Six Months Ended June 30, 2013 |
|---|---|---|
| **Operating activities** | | |
| Net income | $2,868 | $6,014 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 13,370 | 11,738 |
| Amortization of intangible assets | 1,468 | 31 |
| Amortization of deferred loan costs | 1,394 | 823 |
| Amortization of original issue discount related to long-term debt | (432) | 138 |
| Amortization of restricted stock and stock option awards | 3,052 | 1,464 |
| Amortization of program broadcast rights | 5,918 | 5,663 |
| Payments on program broadcast obligations | (7,692) | (5,700) |
| Deferred income taxes | 1,735 | 5,185 |
| Loss (gain) on disposals of assets, net | 379 | (105) |
| Loss from early extinguishment of debt | 4,897 | - |
| Other | 97 | 1,321 |
| Changes in operating assets and liabilities: | | |
| Receivables | (2,804) | 533 |
| Other current assets | 418 | (446) |
| Accounts payable | 362 | (418) |
| Other current liabilities | 3,363 | (1,495) |
| Accrued interest | 946 | 1,173 |
| Net cash provided by operating activities | 29,339 | 25,919 |
| | | |
| **Investing activities** | | |
| Purchases of property and equipment | (10,456) | (12,488) |
| Acquisitions of television businesses and broadcast licenses | (325,862) | (1,329) |
| Proceeds from asset sales | 997 | 138 |
| Other | (2) | 10 |
| Net cash used in investing activities | (335,323) | (13,669) |
| | | |
| **Financing activities** | | |
| Proceeds from borrowings on long-term debt | 544,000 | - |
| Repayments of borrowings on long-term debt | (178,157) | - |
| Deferred and other loan costs | (7,267) | (14) |
| Proceeds from issuance of common stock | - | 101 |
| Net cash provided by financing activities | 358,576 | 87 |
| Net increase in cash | 52,592 | 12,337 |
| Cash at beginning of period | 13,478 | 11,067 |

| | | |
|---|---|---|
| Cash at end of period | $66,070 | $23,404 |

**See notes to condensed consolidated financial statements.**

**GRAY TELEVISION, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

**1. Basis of Presentation**

The accompanying condensed consolidated balance sheet of Gray Television, Inc. (and its consolidated subsidiaries, except as the context otherwise provides,"Gray," the "Company," "we," "us," and "our") as of December 31, 2013, which was derived from the Company's audited financial statements as of December 31, 2013, and our accompanying unaudited condensed consolidated financial statements as of June 30, 2014 and for the periods ended June 30, 2014 and 2013 have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain information and note disclosures normally included in annual financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to those rules and regulations, although we believe that the disclosures made are adequate to make the information not misleading. In our opinion, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair statement have been included. Our operations consist of one reportable segment. For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013 (the "2013 Form 10-K"). Our financial condition as of, and operating results for the six-month period ended, June 30, 2014 are not necessarily indicative of the financial condition or results that may be expected for any future interim period or for the year ending December 31, 2014.

*Seasonality and Cyclicality*

Broadcast advertising revenues are generally highest in the second and fourth quarters each year. This seasonality results partly from increases in consumer advertising in the spring and retail advertising in the period leading up to and including the holiday season. Broadcast advertising revenues are also typically higher in even-numbered years due to increased spending by political candidates, political parties and special interest groups in advance of elections. This political spending typically is heaviest during the fourth quarter.

*Use of Estimates*

The preparation of financial statements in conformity with U.S. GAAP requires our management to make estimates and assumptions that affect the amounts reported in the unaudited condensed consolidated financial statements and the notes to the unaudited condensed consolidated financial statements. Our actual results could differ materially from these estimates. The most significant estimates we make relate to our allowance for doubtful accounts in receivables, valuation of goodwill and intangible assets, amortization of program broadcast rights and intangible assets, stock-based compensation, pension costs, income taxes, employee medical insurance claims, useful lives of property and equipment and contingencies.

*Variable Interest Entity*

During the year ended December 31, 2013, we entered into a series of transactions with the News-Press Gazette Company and Excalibur Broadcasting, LLC (collectively with its subsidiaries, “Excalibur”), pursuant to which we acquired the non-license assets, and Excalibur acquired the license assets, of KJCT-TV and associated low power stations (collectively, “KJCT-TV”), in the Grand Junction, Colorado market. In connection therewith, we entered into a shared services agreement, pursuant to which we provide certain services, including back-office, engineering and sales support, and a lease agreement, pursuant to which we provide studio and office space, to Excalibur. We have also entered into a put and call option agreement with Excalibur, pursuant to which we have the right to purchase, and Excalibur has the right to require us to purchase, the license assets of KJCT-TV, upon receipt of Federal Communications Commission (“FCC”) approval (the “KJCT-TV Option”). In connection with the consummation of Excalibur’s acquisition of KJCT-TV’s license assets, Excalibur incurred debt which Gray has guaranteed. The assets of Excalibur can only be used to settle the obligations of Excalibur. In compliance with FCC regulations, Excalibur maintains complete responsibility for and control over programming, finances, personnel and operations of KJCT-TV. See Note 3 “Long-term Debt” for more information.

We consolidate a VIE when we are determined to be the primary beneficiary. In accordance with U.S. GAAP, in determining whether we are the primary beneficiary of a VIE for financial reporting purposes, we consider whether we have the power to direct the activities of the VIE that most significantly impact the economic performance of the VIE and whether we have the obligation to absorb losses or the right to receive returns that would be significant to the VIE.

Based on the terms of our agreements with, the significance of our investment in, and our guarantee of the debt of, Excalibur, we have determined that Excalibur is a VIE of Gray. We believe we are the primary beneficiary of Excalibur because, subject to the ultimate control of the licensees, we have the power to direct the activities which significantly impact the economic performance of Excalibur through the services we provide, and our obligation to absorb losses and earn returns that would be considered significant to Excalibur. Included in our condensed consolidated statements of operations for the six months ended June 30, 2014 and 2013 is revenue of $0.9 million and $0.0 million, respectively, attributable to Excalibur.

The carrying amounts and classification of the assets and liabilities of Excalibur described above have been included in our consolidated balance sheets as of June 30, 2014 and December 31, 2013 as follows (in thousands):

| | **June 30, 2014** | **December 31, 2013** |
|---|---|---|
| **Assets:** | | |
| Current assets: | | |
| Cash | $473 | $ 473 |
| Accounts receivable, net | 292 | 524 |
| Current portion of program broadcast rights, net | 11 | 42 |
| Prepaid and other current assets | 6 | 7 |
| Total current assets | 782 | 1,046 |
| | | |
| Property and equipment, net | 790 | 883 |
| Deferred loan costs, net | 225 | 174 |
| Broadcast licenses | 4,161 | 4,161 |
| Other intangible assets, net | 459 | 575 |
| Total assets | $6,417 | $ 6,839 |
| | | |
| **Liabilities:** | | |
| Current liabilities: | | |
| Accounts payable | $32 | $ 14 |
| Employee compensation and benefits | 56 | 8 |
| Accrued interest | - | 2 |
| Other accrued expenses | 18 | 13 |
| Accrued expenses due to Gray | 1,276 | 651 |
| Current portion of program broadcast obligations | 11 | 45 |
| Current portion of long-term debt | 200 | 200 |
| Total current liabilities | 1,593 | 933 |
| | | |
| Long-term debt, less current portion | 2,700 | 2,800 |
| Other long-term liabilities | 2,124 | 3,106 |
| Total liabilities | $6,417 | $ 6,839 |

The assets of Excalibur can only be used to settle the obligations of Excalibur and may not be sold, or otherwise disposed of, except for assets sold or replaced with others of like kind or value. Other long-term liabilities of $2.1 million and $3.1 million, representing the fair value of the KJCT-TV Option as of June 30, 2014 and December 31, 2013, respectively, and accrued expenses due to Gray of $1.3 million and $0.7 million as of June 30, 2014 and December 31, 2013, respectively, were eliminated in our consolidated financial statements. The terms of the KJCT-TV Option provide for the acquisition of the license assets of KJCT-TV at an exercise price that was less than the carrying value of such assets as of June 30, 2014.

*Earnings Per Share*

We compute basic earnings per share by dividing net income attributable to common stockholders by the weighted-average number of common shares outstanding during the relevant period. The weighted-average number of common shares outstanding does not include restricted shares. These shares, although classified as issued and outstanding, are considered contingently returnable until the restrictions lapse and, in accordance with U.S. GAAP, are not included in the basic earnings per share calculation until the shares vest. Diluted earnings per share is computed by including all potentially dilutive common shares, including restricted shares and shares underlying stock options, in the denominator of the diluted weighted-average shares outstanding calculation, unless their inclusion would be antidilutive.

The following table reconciles basic weighted-average shares outstanding to diluted weighted-average shares outstanding for the three-month and six-month periods ended June 30, 2014 and 2013 (in thousands):

| | **Three Months Ended June 30,** | | **Six Months Ended June 30,** | |
|---|---|---|---|---|
| | **2014** | **2013** | **2014** | **2013** |
| Weighted-average shares outstanding-basic | 57,862 | 57,561 | 57,855 | 57,542 |
| Common stock equivalents for stock options and restricted stock | 449 | 378 | 443 | 278 |
| Weighted-average shares outstanding-diluted | 58,311 | 57,939 | 58,298 | 57,820 |

*Accumulated Other Comprehensive Loss*

Our accumulated other comprehensive loss balances as of June 30, 2014 and December 31, 2013 consist of adjustments to our pension liability and income tax benefit as follows (in thousands):

| | **June 30, 2014** | **December 31, 2013** |
|---|---|---|
| Accumulated balances of items included in accumulated other comprehensive loss: | | |
| Increase in pension liability | $(17,064) | $(17,064) |
| Income tax benefit | (6,655) | (6,655) |
| Accumulated other comprehensive loss | $(10,409) | $(10,409) |

*Consolidated Statement of Comprehensive Income*

Our comprehensive income for the three-month and six-month periods ended June 30, 2014 and 2013 consists entirely of net income. Therefore, a consolidated statement of comprehensive income is not presented.

*Property and Equipment*

Property and equipment are carried at cost. Depreciation is computed principally by the straight-line method. Maintenance, repairs and minor replacements are charged to operations as incurred; major replacements and betterments are capitalized. The cost of any assets sold or retired and the related accumulated depreciation are removed from the accounts at the time of disposition, and any resulting profit or loss is reflected in income or expense for the period. The following table lists components of property and equipment by major category (in thousands):

| | **June 30, 2014** | **December 31, 2013** | **Estimated Useful Lives (in years)** |
|---|---|---|---|
| Property and equipment: | | | |
| Land | $30,821 | $25,656 | |
| Buildings and improvements | 65,154 | 59,021 | 7 to 40 |
| Equipment | 365,051 | 323,603 | 3 to 20 |
| | 461,026 | 408,280 | |
| Accumulated depreciation | (269,578) | (264,659) | |
| Total property and equipment, net | $191,448 | $143,621 | |

*Allowance for Doubtful Accounts*

Our allowance for doubtful accounts is equal to at least 85% of our receivable balances that are 120 days old or older. We may provide allowances for certain receivable balances that are less than 120 days old when warranted by specific facts and circumstances. We generally write-off accounts receivable balances when the customer files for bankruptcy or when all commonly used methods of collection have been exhausted.

*Recent Accounting Pronouncements*

We have reviewed all recently issued accounting pronouncements. Of those pronouncements that have been issued but are not yet effective, we do not anticipate a material impact upon our financial statements upon our adoption of those pronouncements. None of the pronouncements that became effective and were adopted by us during the six months ended June 30, 2014 had a material effect upon our results of operations or financial position.

**2. Acquisitions**

During the six-month period ended June 30, 2014, we completed the four acquisitions described below: the Hoak Acquisition, the KNDX Acquisition, the KEVN Acquisition and the WQCW Acquisition (collectively, the "2014 Acquisitions"). The 2014 Acquisitions are expected to, among other things, increase our revenues and cash flows from operating activities, and allow us to operate more efficiently and effectively, including by increasing our scale and providing us the ability to negotiate more favorable terms in our agreements with third parties.

*Hoak Acquisition*

On June 13, 2014, we completed the acquisition of 100% of the capital stock of certain wholly owned subsidiaries of Hoak Media, LLC ("Hoak") for total cash consideration of approximately $298.4 million, which included a base purchase price of $290.8 million and a working capital adjustment of $7.6 million (the "Hoak Acquisition"). The subsidiaries owned and operated twelve television stations as described in the table below. The Hoak Acquisition also included the assumption of Hoak's interest in certain operating agreements, and the acquisition of certain non-license assets, of KHAS-TV, which serves the Lincoln-Hastings, Nebraska market, from Hoak. On June 13, 2014, we transferred the programing of KHAS-TV to KSNB-TV, a station owned by Gray which also serves the Lincoln-Hastings, Nebraska, television market. We used borrowings under the 2014 Senior Credit Facility, as defined below, to fund the purchase price to complete the Hoak Acquisition.

The following stations were acquired in the Hoak Acquisition:

| Station | Network Affiliation | Market | Market Rank |
|---|---|---|---|
| KSFY-TV | ABC | Sioux Falls, SD | 111 |
| KABY-TV* | ABC | Sioux Falls, SD | 111 |
| KPRY-TV* | ABC | Sioux Falls, SD | 111 |
| KVLY-TV | NBC | Fargo-Valley City, ND | 116 |
| KNOE-TV | CBS | Monroe- El Dorado, LA | 137 |
| KFYR-TV | NBC | Minot-Bismarck-Dickinson, ND | 145 |
| KMOT-TV* | NBC | Minot-Bismarck-Dickinson, ND | 145 |
| KUMV-TV* | NBC | Minot-Bismarck-Dickinson, ND | 145 |
| KQCD-TV* | NBC | Minot-Bismarck-Dickinson, ND | 145 |
| KALB-TV | NBC/CBS | Alexandria, LA | 179 |
| KNOP-TV | NBC | North Platte, NE | 208 |
| KIIT-LP | FOX | North Platte, NE | 208 |

* satellite station

Parker Broadcasting, Inc. (“Parker”) owns KXJB-TV, which is affiliated with the CBS network and serves the Fargo, North Dakota market, and KAQY-TV, which is affiliated with the ABC network and serves the Monroe, Louisiana market. As a component of the Hoak Acquisition, Gray assumed Hoak’s rights under certain agreements with Parker to provide back-office services, sales support and limited programming to KXJB-TV and KAQY-TV (collectively the “Parker Agreements”). For additional information on Parker, see “Pending Parker Acquisitions” below.

*KNDX Acquisition*

On May 1, 2014, we acquired certain assets of KNDX-TV and its satellite station KXND-TV, as well as certain non-license assets of low power stations KNDX-LP and KXND-LP, from Prime Cities Broadcasting, Inc. (“Prime Cities”). These four stations served as the Fox network affiliates for the Minot-Bismarck, North Dakota television market. On June 13, 2014, we transferred the programing of KNDX-TV and KXND-TV to the television stations that we acquired from Hoak in the Minot-Bismarck, North Dakota, television market. On June 27, 2014, we acquired the low power FCC licenses of KNDX-LP and KXND-LP from Prime Cities. We refer to the acquisition of these assets from Prime Cities as the “KNDX Acquisition.” The total cash consideration to complete the KNDX Acquisition was $7.5 million, which was funded from a combination of cash from operations and borrowings under our 2012 Senior Credit Facility, as defined below.

*KEVN Acquisition*

On May 1, 2014, we acquired 100% of the equity interests in KEVN, Inc. from Mission TV, LLC (the “KEVN Acquisition”). KEVN, Inc. owned and operated KEVN-TV and its satellite station, KIVV-TV (collectively the “KEVN Stations”). The KEVN Stations are affiliated with the Fox network and serve the Rapid City, South Dakota market. The total purchase price to complete the KEVN Acquisition was approximately $8.8 million which included a base purchase price of $7.8 million and a working capital adjustment of $1.0 million. The cash consideration to complete the KEVN Acquisition was funded from a combination of cash from operations and borrowings under our 2012 Senior Credit Facility.

*WQCW Acquisition*

On April 1, 2014, we acquired the assets of WQCW-TV, Portsmouth, Ohio and WOCW-LP, Charleston, West Virginia from Lockwood Broadcast Group (collectively, the "WQCW Acquisition"). WQCW-TV and WOCW-LP serve as the CW affiliate for the Charleston/ Huntington, West Virginia television market, where we own and operate WSAZ-TV, the market's NBC affiliate. The consideration to complete the WQCW Acquisition was approximately $5.5 million, which was funded from cash from operations.

*Preliminary Fair Value Estimates:*

The preliminary fair value estimates of the acquired assets, assumed liabilities and resulting goodwill from the 2014 Acquisitions are summarized as follows (in thousands):

| | **Hoak Acquisition** | **KNDX Acquisition** | **KEVN Acquisition** | **WQCW Acquisition** |
|---|---|---|---|---|
| Cash | $ - | $ - | $ 615 | $ - |
| Accounts receivable | 10,732 | - | 565 | - |
| Other current assets | 511 | 39 | 96 | 45 |
| Property and equipment | 45,223 | 2,576 | 3,888 | 991 |
| Broadcast licenses | 91,958 | 500 | 1,675 | 3,691 |
| Goodwill | 130,342 | 1,839 | 2,767 | 802 |
| Other intangible assets | 35,411 | 2,584 | 1,786 | 15 |
| Other non-current assets | - | 15 | 29 | - |
| Current liabilities | (3,595) | (36) | (265) | (45) |
| Other long-term liabilities | - | (17) | (32) | - |
| Deferred income tax liabilities | (12,134) | - | (2,339) | - |
| Total | $ 298,448 | $ 7,500 | $ 8,785 | $ 5,499 |

The amounts in the table above are based upon management’s estimate of the fair values using valuation techniques including income, cost and market approaches. In estimating the fair value of the acquired assets and assumed liabilities, the fair value estimates are based on, but not limited to, expected future revenue and cash flows, expected future growth rates, and estimated discount rates.

Accounts receivables are recorded at their fair value which represents the amount that we expect to collect. Contractual amounts are approximately $0.2 million more than their recorded fair value.

The amount related to property and equipment will be depreciated over their estimated useful lives ranging from 3 years to 40 years.

The amount related to other intangible assets represents the estimated fair values of retransmission agreements of $23.0 million; advertising contracts of $1.4 million; advertising relationships of $11.5 million; and favorable leases of $3.9 million. These intangible assets are being amortized over their estimated useful lives of approximately 4.2 years for retransmission agreements; approximately 1.0 year for advertising contracts; approximately 5.1 years for advertising relationships; and approximately 8.2 years for leases.

Goodwill is calculated as the excess of the consideration transferred over the fair value of the identifiable net assets acquired and liabilities assumed, and represents the future economic benefits expected to arise from other intangible assets acquired that do not qualify for separate recognition, including assembled workforce, as well as future synergies that we expect to generate from the 2014 Acquisitions. We have preliminarily recorded $135.8 million of goodwill in connection with the 2014 Acquisitions. Of the goodwill recognized in connection with the 2014 Acquisitions, approximately $85.7 million is deductible for income tax purposes.

The fair values of assets acquired and liabilities assumed were based upon preliminary valuations and the estimates and assumptions are subject to change within the measurement period as additional information is obtained. Any such changes could be material and could result in significantly different fair values from those set out above.

*Preliminary Pro Forma Financial Information*

The following table sets forth certain unaudited pro forma results of operations of the Company for the six months ended June 30, 2014 and 2013 assuming that the Hoak Acquisition, along with transactions necessary to finance the Hoak Acquisition, occurred on January 1, 2013 (in thousands, except per share data):

| | **Six Months Ended June 30,** | |
|---|---|---|
| | **2014** | **2013** |
| Revenue (less agency commissions) | $232,123 | $195,138 |
| Net income | $10,581 | $2,348 |
| Basic and diluted net income per share | $0.18 | |