JACUZZI BRANDS INC
Form 10-Q
August 12, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended July 3, 2004

or

o **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: **1-14557**

JACUZZI BRANDS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**22-3568449**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

777 S. Flagler Drive; Suite 1100W
West Palm Beach, FL 33401
(Address of principal executive offices)

(561) 514-3838
(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 x No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act):
Yes x No o

As of July 30, 2004 Jacuzzi Brands, Inc. had one class of common stock, of which 75,448,440 shares were outstanding.

JACUZZI BRANDS, INC.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

JACUZZI BRANDS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
(in millions, except per share data)
(unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2004	2003	2004	2003
Net sales	$366.8	$315.5	$1,003.5	$865.2
Operating costs and expenses:				
Cost of products sold	249.9	221.4	696.4	599.2
Selling, general and administrative expenses	77.9	65.0	224.7	189.2
Restructuring charges	2.9	5.2	8.6	8.3
Operating income	36.1	23.9	73.8	68.5
Interest expense	(12.9)	(14.3)	(38.4)	(46.9)
Interest income	0.3	0.4	3.8	1.3
Other expense, net	(0.9)	(1.0)	(0.5)	(3.5)
Earnings before income taxes	22.6	9.0	38.7	19.4
(Provision for) benefit from income taxes	(8.9)	(3.5)	(15.1)	6.1
Earnings from continuing operations	13.7	5.5	23.6	25.5
Discontinued operations:				
Loss from operations (net of tax benefit of $0.2 for the three and nine months ended June 30, 2003 and tax benefit of $0.2 for the nine months ended June 30, 2004)		(0.4)	(0.6)	(0.4)
Impairment loss (net of tax benefit of $6.5)				(39.9)
Loss from discontinued operations		(0.4)	(0.6)	(40.3)
Net earnings (loss)	$ 13.7	$ 5.1	$ 23.0	$ (14.8)

Basic earnings (loss) per share:				
Continuing operations	$ 0.18	$ 0.07	$ 0.31	$ 0.34
Discontinued operations			(0.01)	(0.54)
	$ 0.18	$ 0.07	$ 0.30	$ (0.20)
Diluted earnings (loss) per share:				
Continuing operations	$ 0.18	$ 0.07	$ 0.31	$ 0.34
Discontinued operations			(0.01)	(0.54)
	$ 0.18	$ 0.07	$ 0.30	$ (0.20)

The accompanying notes are an integral part of these statements.

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JACUZZI BRANDS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(in millions)

	June 30, 2004	September 30, 2003
	(unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 26.1	$ 31.2
Trade receivables, net	256.8	229.6
Inventories	194.2	165.0
Deferred income taxes	16.5	15.5
Assets held for sale	3.0	16.8
Other current assets	23.3	30.1
Total current assets	519.9	488.2
Property, plant and equipment, net	125.1	129.7
Pension assets	154.1	148.3
Insurance for asbestos claims	160.0	160.0
Goodwill	288.7	283.1
Other intangibles, net	60.0	60.8
Other non-current assets	46.7	66.7
TOTAL ASSETS	$1,354.5	$1,336.8
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Notes payable	$ 21.9	$ 23.5
Current maturities of long-term debt	29.2	25.2
Trade accounts payable	112.7	102.3
Income taxes payable	19.4	10.8
Liabilities associated with assets held for sale		8.7
Accrued expenses and other current liabilities	127.1	136.2
Total current liabilities	310.3	306.7
Long-term debt	446.8	451.4
Deferred income taxes	18.3	26.2
Asbestos claims	160.0	160.0
Other non-current liabilities	131.8	136.8

Total liabilities	1,067.2	1,081.1
Commitments and contingencies		
Stockholders equity	287.3	255.7
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$1,354.5	$1,336.8

The accompanying notes are an integral part of these statements.

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JACUZZI BRANDS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions)
(unaudited)

	Nine months ended June 30,	
	2004	**2003**
OPERATING ACTIVITIES:		
Net cash provided by operating activities of continuing operations	$ 8.1	$ 37.0
Net cash used in operating activities of discontinued operations	(1.8)	(9.2)
NET CASH PROVIDED BY OPERATING ACTIVITIES	6.3	27.8
INVESTING ACTIVITIES:		
Proceeds from sale of businesses, net	4.5	120.5
Purchases of property, plant and equipment	(12.1)	(11.4)
Proceeds from sale of real estate	3.2	11.0
Proceeds from sale of fixed assets	0.5	0.1
NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES	(3.9)	120.2
FINANCING ACTIVITIES:		
Proceeds from long-term debt	44.2	42.1
Repayment of long-term debt	(44.7)	(321.6)
Escrow deposits in restricted cash collateral accounts		(60.9)
Escrow withdrawals from restricted cash collateral accounts		178.1
Payment of financing fees	(1.6)	(8.9)
Proceeds from the issuance of common stock for option exercises	0.9	
(Decrease) increase in notes payable, net	(4.1)	5.5
NET CASH USED IN FINANCING ACTIVITIES	(5.3)	(165.7)
Effect of exchange rate changes on cash and cash equivalents	(2.2)	7.0
DECREASE IN CASH AND CASH EQUIVALENTS	(5.1)	(10.7)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	31.2	32.1
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 26.1	$ 21.4

The accompanying notes are an integral part of these statements.

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JACUZZI BRANDS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Tabular amounts in millions)
(unaudited)

Note 1-Basis of Presentation

We manufacture and distribute a broad range of consumer and industrial products through our three business segments Bath Products, Plumbing Products and Rexair. We serve residential markets through Jacuzzi, Inc.; Sundance Spas, Inc.; Eljer Plumbingware, Inc. and related subsidiaries (Jacuzzi), while we serve commercial/institutional markets through Zurn Industries, Inc. (Zurn). We also manufacture premium RAINBOW® vacuum cleaner systems through Rexair, Inc. (Rexair).

We operate on a 52- or 53-week fiscal year ending on the Saturday nearest to September 30. All three- and nine-month data contained in this Report on Form 10-Q reflects the results of operations for the 13-week and 39-week or 40-week periods ended on the Saturday nearest June 30 of the respective year, but are presented as of June 30 for convenience. Our condensed consolidated interim financial statements as of June 30, 2004 and for the 13-week and 40-week periods ended June 30, 2004 (also referred to as the third quarter of 2004 and nine months ended 2004 , respectively) and the 13-week and 39-week periods ended June 30, 2003 (also referred to as the third quarter of 2003 and nine months ended 2003 , respectively) are unaudited. However, in our opinion, these financial statements reflect all normal, recurring adjustments necessary to provide a fair presentation of our financial position, results of operations and cash flows for the periods presented. These interim financial statements are condensed, and thus, do not include all of the information and footnotes required by accounting principles generally accepted in the United States for presentation of a complete set of financial statements. The balance sheet as of September 27, 2003 (referred to as of September 30, 2003 for convenience) has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

These interim results are not necessarily indicative of the results that should be expected for the full year. For a better understanding of Jacuzzi Brands, Inc. and our financial statements, the condensed interim financial statements should be read in conjunction with our audited consolidated financial statements for the year ended September 27, 2003, which are included in our 2003 Annual Report on Form 10-K, filed on December 19, 2003.

Note 2- New Accounting Pronouncements

In December 2003, the Financial Accounting Standards Board (FASB) issued Statement No. 132 (revised 2003), *Employers Disclosures about Pensions and Other Postretirement Benefits, an amendment of FASB Statements No. 87, 88 and 106* (SFAS 132). This Statement revises employers disclosure requirements for pension plans and other post-retirement benefit plans. It does not change the measurement or recognition of those plans required by FASB Statement No. 87, *Employers Accounting for Pensions*; FASB Statement No. 88, *Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits*, or FASB Statement No. 106, *Employers Accounting for Post-retirement Benefits Other Than Pensions*. This Statement requires additional disclosures about the assets, obligations, cash flows, and net periodic benefit cost of defined benefit pension plans and other post-retirement benefit plans. The required information should be provided separately for pension plans and for other post-retirement benefit plans. SFAS 132 is effective for annual financial statements with fiscal years ending after December 15, 2003. The interim-period disclosures required by this Statement are effective for interim periods beginning after December 15, 2003 and, as such, are included in **Note 10.**

In December 2003, the FASB issued Interpretation No. 46, *Consolidation of Variable Interest Entities* (FIN 46). This Interpretation, and its subsequent revisions, of Accounting Research Bulletin No. 51, *Consolidated Financial Statements*, as amended, (ARB 51) addresses consolidation by business enterprises of variable interest entities. Under current practice, two enterprises generally have been included in consolidated financial statements because one enterprise controls the other through voting interests. FIN 46 defines the concept of   variable interests   and requires existing unconsolidated variable interest entities to be consolidated by their primary beneficiaries if the entities do not effectively disperse risks among the parties involved. It also requires the deconsolidation of consolidated variable interest entities in certain circumstances if it is determined that the consolidating equity holder is not the primary beneficiary. We have evaluated our interests in our wholly-owned subsidiaries and continue to consolidate them under

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JACUZZI BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Tabular amounts in millions)
(unaudited)

Note 2- New Accounting Pronouncements (continued)

the guidelines set forth in ARB 51. We have also completed an evaluation of all of our variable interests and have determined that we do not have any interests in variable interest entities, as defined by FIN 46.

On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Medicare Act) was enacted. In January 2004, the FASB issued FASB Staff Position No. FAS 106-1, *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* (FSP 106-1). Pursuant to FAS 106-1, in the second quarter of fiscal 2004, we elected to defer recognizing the effects of the Medicare Act in the accounting for our post-retirement plan under FASB Statement No. 106, *Employers Accounting for Postretirement Benefits Other Than Pensions,* until authoritative FASB guidance was issued. In May 2004, FSP No. FAS 106-2, *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003* (FSP 106-2) was issued. FSP 106-2 supersedes FSP 106-1 and provides guidance on accounting for the effects of the Medicare Act. Under FSP 106-2, companies eligible for federal subsidies under the Medicare Act should recognize the expected benefit as part of the measurement of accumulated post-retirement obligation. FSP 106-2 is effective for the first interim or annual period beginning after June 15, 2004. We are assessing the impact of the Medicare Act and FSP 106-2 on our post-retirement pension plan.

Note 3-Inventories

Inventories consist of the following:

	June 30, 2004	September 30, 2003
Finished products	$128.2	$103.3
In-process products	13.4	13.0
Raw materials	52.6	48.7
	$194.2	$165.0

Note 4-Goodwill and Other Intangible Assets

As of June 30, 2004, we had goodwill of $288.7 million compared to $283.1 million at September 30, 2003. The increase in the goodwill balance is due to exchange rate fluctuations.

Identifiable intangible assets, which are included in the Rexair segment, are comprised of:

		June 30, 2004		September 30, 2003	
	Estimated Life	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Patented technology	10 years	$ 2.6	$ 0.7	$ 2.6	$ 0.6
Distributor network	40 years	36.0	2.6	36.0	1.9
Trade name	Indefinite	24.7		24.7	
Total identifiable intangible assets		$63.3	$ 3.3	$63.3	$ 2.5

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JACUZZI BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Tabular amounts in millions)
(unaudited)

Note 5-Long-Term Debt

Long-term debt consists of the following:

	June 30, 2004	September 30, 2003
Senior Notes Payable:		
9.625% Senior Notes	$380.0	$ 380.0
Bank Facilities:		
Asset-based facility	27.8	23.9
Term loan	61.8	65.0
Other long-term debt	6.4	7.7
	476.0	476.6
Less: current maturities	(29.2)	(25.2)
Long-term debt	$446.8	$ 451.4

On June 30, 2004, we amended our asset-based revolving credit facility and term loan (collectively the Bank Facilities), which provides for:

- a reduction in the interest rate of our term loan from Prime plus 5% with a minimum rate of 9.25% to 500 basis points over LIBOR;
- the elimination of annual prepayments on the term loan of $10 million, which were scheduled to begin in August 2005;
- the elimination of annual prepayments on the term loan equal to 25% of our annual consolidated excess cash flow, as determined by the original loan agreement;
- the extension of the term loan s maturity date by one year to July 15, 2009; and
- the elimination of all debt covenants except the requirement to maintain a minimum consolidated fixed charge coverage ratio. This requirement is applicable only if our availability under the asset-based credit facility falls below $20 million.

This amendment was not considered a substantial modification of our debt under the guidance provided in EITF Issue

No. 96-19, *Debtor s Accounting for a Modification or Exchange of Debt Instruments*.

At June 30, 2004, we had approximately $153.0 million available to be borrowed under the asset-based facility, of which we had utilized approximately $69.8 million (including $42.0 million of letters of credit), leaving $83.2 million available for additional borrowings. In addition, we have outstanding bankers acceptances of $2.1 million which do not affect availability under the asset-based facility. The weighted average interest rate on borrowings under the asset-based credit facility was 3.6% for the nine months ended fiscal 2004.

The Bank Facilities contain a subjective acceleration clause and a requirement to maintain a lockbox associated with our asset-based facility. As required by EITF Issue No. 95-22, *Balance Sheet Classification of Borrowings Outstanding under Revolving Credit Agreements that Include both a Subjective Acceleration Clause and a Lockbox Arrangement*, the entire balance of the asset-based facility is included in current maturities of long-term debt.

The $380 million, 9.625% notes (the Senior Notes), which are due July 1, 2010 and require the payment of interest of $18.3 million on January 1 and July 1 of each year, were subject to registration with the Securities and Exchange Commission pursuant to a registration rights agreement. On February 17, 2004, we completed an offer to exchange new, registered Senior Notes for the then outstanding unregistered notes. The terms of the new, registered Senior Notes are identical, in all material respects, to the terms of the then outstanding unregistered notes, except that the new Senior Notes have been registered under the Securities Act, and the transfer restrictions and registration rights relating to the unregistered notes do not apply to the registered Senior Notes.

During the nine months ended fiscal 2004, we paid $42.4 million of interest on our borrowings. Additional information regarding our long-term debt structure can be found in our 2003 Annual Report on Form 10-K, filed on December 19, 2003.

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JACUZZI BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Tabular amounts in millions)
(unaudited)

Note 6-Commitments and Contingencies

Warranties

We record a reserve for future warranty costs based on current unit sales, historical experience and management s judgment regarding anticipated rates of warranty claims and cost per claim. The adequacy of the recorded warranty reserves is assessed each quarter and adjustments are made as necessary. The specific terms and conditions of the warranties vary depending on the products sold and the countries in which we do business. Changes in the warranty liability during the period are as follows:

Balance at September 30, 2003	$ 19.0
Warranty accrual	15.1
Cash payments	(10.5)
Balance at June 30, 2004	$ 23.6

Guarantees & Indemnifications

In connection with the sale of Ames True Temper in January 2002, we continue to guarantee the lease payments of their master distribution center. The lease obligation will expire in 2015. The lease payments totaled $3.7 million for fiscal 2003, and increase by 2.25% each year thereafter. We obtained a security interest and indemnification from Ames True Temper on the lease that would enable us to exercise remedies in the event of default. We have not been called upon to make any payments under this guarantee.

We have sold a number of assets and operating entities over the last several years and have, on occasion, provided indemnifications for liabilities relating to product liability, environmental and other claims. We have accrued approximately $9.1 million as of June 30, 2004 for asserted and potential unasserted claims related to these liabilities.

Litigation

We and our subsidiaries are parties to legal proceedings that we believe to be either ordinary, routine litigation incidental to the business of present and former operations or immaterial to our financial condition, results of operations or cash flows.

Certain of our subsidiaries are defendants or plaintiffs in lawsuits that have arisen in the normal course of business. While certain of these matters involve substantial amounts, it is management s opinion, based on the advice of counsel, that the ultimate resolution of such litigation and environmental matters will not have a material adverse effect on our financial condition, results of operations or cash flows.

Litigation resulting from a dispute with the former owners of the Sundance Spas business has resulted in a judgment of approximately $5.1 million in our favor. The gain of $3.9 million resulting from the judgment is not included in the results of our operations in the third quarter of fiscal 2004 as it is still subject to appeal.

In June 1998, we acquired Zurn, which itself owned various subsidiaries. Zurn is one of our wholly-owned subsidiaries. Zurn, along with many other unrelated companies, is a co-defendant in numerous asbestos related lawsuits pending in the U.S. Plaintiffs claims primarily allege personal injuries allegedly caused by exposure to asbestos used primarily in industrial boilers formerly manufactured by a segment of Zurn that has been presented as a discontinued operation. Zurn did not manufacture asbestos or asbestos components but purchased it from suppliers.

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JACUZZI BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Tabular amounts in millions)
(unaudited)

Note 6-Commitments and Contingencies (continued)

Legislation has been introduced in the Senate that would remove asbestos claims from the current tort system and place them in a trust fund system. This trust would be funded by the insurers and defendant companies. There can be no assurance as to when or if this or any other legislation will be passed and become law or what, if any, the financial impact it could have on Zurn.

New claims filed against Zurn were lower period over period. For the third quarter and nine months ended fiscal 2004, approximately 6,700 and 21,800, respectively, new asbestos claims were filed against Zurn. For the third quarter and nine months ended fiscal 2003, approximately 8,600 and 23,500, respectively, new asbestos claims were filed against Zurn.

During the third quarter and nine months ended fiscal 2004 and as of the end of such periods, approximately 15,357 and 24,126 claims, respectively, were paid and/or pending payment and approximately 2,278 and 3,247 claims, respectively, were dismissed and/or pending dismissal. During the third quarter and nine months ending fiscal 2003 and as of the end of such periods, approximately 31,300 and 39,500 claims, respectively, were paid and/or pending payment and approximately 1,100 and 2,800 claims, respectively, were dismissed and/or pending dismissal.

As of June 30, 2004, the number of asbestos claims pending against Zurn was approximately 74,700 compared to 59,000 as of September 30, 2003. The increase in pending claims is a result of new claims exceeding the number of claims newly resolved during the period. The claims are handled pursuant to a defense strategy funded by Zurn s insurers. Since Zurn received its first asbestos claim in the 1980s, Zurn has paid or dismissed or agreed to settle or dismiss approximately 97,000 asbestos claims including dismissals or agreements to dismiss of approximately 9,000 of such claims through June 30, 2004 compared to 84,000 and 6,400 claims, respectively, through September 30, 2003.

The pending claims against Zurn as of June 30, 2004 were included in approximately 5,500 lawsuits, in which Zurn and an average of 100 other companies are named as defendants, and which cumulatively allege damages of approximately $13.5 billion against all defendants. The pending claims against Zurn as of September 30, 2003 were included in approximately 5,600 lawsuits, in which Zurn and an average of 100 other companies are named as defendants, and which cumulatively allege damages of approximately $12 billion against all defendants. Defense costs currently do not erode the coverage amounts in the insurance policies, although a few policies that will be accessed in the future may count defense costs toward aggregate limits.

At September 30, 2003, Zurn and its actuarial consultant estimated that its potential liability for asbestos claims pending against it and for claims estimated to be filed through 2013 is approximately $160 million. This accrual comprises (i) approximately $8 million in claims that had been settled but unpaid as of September 30, 2003; (ii) approximately $36 million in proposed settlements of pending and future claims; and (iii) approximately $116 million for other future claims. This estimate is based on the current and anticipated number of future asbestos claims, the timing and amounts of asbestos payments, the status of ongoing litigation and the potential impact of defense strategies and settlement initiatives. However, there are inherent uncertainties involved in estimating both the number of future asbestos claims as well as future settlement costs, and the actual liability could exceed Zurn s estimate due to changes in law and other factors beyond their control.

Zurn s estimate of its asbestos liability assumes (i) its vigorous defense strategy will enable it to reduce both its claim frequency and claim severity in the future; (ii) approximately 178,000 other future asbestos claims; and (iii) its insurers will continue to pay defense costs without eroding the coverage amounts of its insurance policies. While Zurn believes there is evidence, in recent claims settlements, for such an impact of a successful defense strategy, if the defense strategy ultimately is not successful, to the extent assumed by Zurn, the severity and frequency of asbestos claims could increase substantially above Zurn s estimates. Further, while Zurn s current asbestos liability is based on an estimate of claims through 2013, such liability may continue beyond 2013, and such liability could be substantial.

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JACUZZI BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Tabular amounts in millions)
(unaudited)

Note 6-Commitments and Contingencies (continued)

Zurn estimates that its available insurance to cover its potential asbestos liability as of June 30, 2004 is approximately $303.5 million. The amount of available insurance reflects the payments made during the third quarter offset by a credit of approximately $1.5 million from the carriers relating to claims processed in prior periods. Zurn estimated that its available insurance to cover its potential asbestos liability as of September 30, 2003 was approximately $314.0 million. Zurn believes, based on its experience in defending and dismissing such claims and the coverage available, that it has sufficient insurance to cover the pending and reasonably estimable future claims. This conclusion was reached after considering Zurn s experience in asbestos litigation, the insurance payments made to date by Zurn s insurance carriers, existing insurance policies, the industry ratings of the insurers and the advice of insurance coverage counsel with respect to applicable insurance coverage law relating to the terms and conditions of those policies. However, there is no assurance that this amount of insurance will ultimately be available or that Zurn s asbestos liabilities will not ultimately exceed this amount. Factors that could cause a decrease in the amount of available coverage include changes in law governing the policies, potential disputes with the carriers on the scope of coverage and insolvencies of one or more of Zurn s carriers.

Principally as a result of the past insolvency of certain of Zurn s insurance carriers, certain gaps exist in Zurn s insurance coverage but only if and after Zurn uses approximately $231.5 million of its remaining approximate $303.5 million of insurance coverage, based on its coverage analysis. As noted above, the actuarial estimate of Zurn s potential liability for asbestos claims pending against it and for claims estimated to be filed through 2013 is $160 million. In order to use approximately $278.5 million of the $303.5 million of its insurance coverage from solvent carriers, Zurn estimates that it would need to satisfy approximately $14 million of asbestos claims, with additional gaps of $80 million layered within the final $25 million of the $303.5 million of coverage. We will pursue, if necessary, any available recoveries on our approximately $148 million of coverage with insolvent carriers, which includes approximately $83 million of coverage attributable to the gaps discussed above. These estimates are subject to the factors noted above.

After review of the foregoing with Zurn and its consultants, we believe that the resolution of Zurn s pending and reasonably estimable asbestos claims will not have a material adverse effect on Zurn s financial condition, results of operations or cash flows.

Note 7 - Comprehensive Income

The components of comprehensive income are as follows:

	Third Quarter		Nine Months Ended	
	2004	**2003**	**2004**	**2003**
Net earnings (loss)	$13.7	$ 5.1	$23.0	$(14.8)
Foreign currency translation:				
Adjustments arising during the period	(0.2)	14.3	15.1	22.1
Reclassification adjustment in earnings				2.1
Net unrealized loss on investments, net of tax	(0.9)		(9.7)	

Comprehensive income	$12.6	$19.4	$28.4	$ 9.4

Note 8 - Earnings Per Share

The basic and diluted weighted average number of common and common equivalent shares outstanding are as follows:

	Third Quarter		Nine Months Ended	
	2004	**2003**	**2004**	**2003**
Basic weighted average number of common shares outstanding	75.2	74.7	75.0	74.5
Effect of potentially dilutive securities:				
Stock options	0.5	0.2	0.5	0.1
Restricted stock	0.1		0.1	
Diluted weighted average number of common and common equivalent shares outstanding	75.8	74.9	75.6	74.6

JACUZZI BRANDS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Tabular amounts in millions)
(unaudited)

Note 8 - Earnings Per Share (continued)

Options to purchase 1.0 million and 1.1 million shares in the third quarter and nine months ended fiscal 2004, respectively, and options to purchase 3.9 million and 4.6 million shares in the third quarter and nine months ended fiscal 2003, respectively, were not included in the computation of diluted earnings (loss) per share because the exercise prices of these options exceeded the average market price of the common shares during the respective periods.

Note 9 - Employee Stock Options

We apply Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations in accounting for our stock-based compensation plans. Thus, we use the intrinsic value method to determine the compensation cost for our stock-based awards to employees. Had compensation cost for awards under our stock-based compensation plans been determined using the fair value method prescribed by FASB Statement No. 123, *Accounting for Stock-Based Compensation*, as revised, our net earnings and net earnings per share would have been reduced to the pro forma amounts presented below:

	Third Quarter		Nine Months Ended	
	2004	2003	2004	2003
Net earnings (loss), as reported:	$13.7	$ 5.1	$23.0	$(14.8)
Stock-based employee compensation expense, net of tax	0.9	0.3	1.6	1.0
Total stock-based employee compensation expense determined under the fair value method, net of tax	(1.1)	(0.6)	(2.2)	(2.1)
Pro forma net income (loss)	$13.5	$ 4.8	$22.4	$(15.9)
Earnings (loss) per share:				
Basic - as reported	$0.18	$0.07	$0.30	$(0.20)
Basic - pro forma	0.18	0.07	0.30	(0.22)
Diluted - as reported	$0.18	$0.07	$0.30	$(0.20)
Diluted - pro forma	0.18	0.07	0.30	(0.22)

The fair value of each stock option granted is established on the date of the grant using the Black-Scholes option pricing model with the following weighted average assumptions for grants for 2004 and 2003:

- expected volatility rates of 67% for 2004 and 65% for 2003;
- risk-free interest rates of 2.87% for 2004 and 2.67% for 2003;

- expected option lives of 4 years for both years; and

- expected dividend yield of 0% for both years.

On March 17, 2004, in connection with an option exchange offer, we accepted for cancellation options to purchase 1,903,337 shares of our common stock, and granted 435,730 restricted shares of our common stock (restricted stock awards) in exchange. Participants tendered 100% of the options eligible to be exchanged. In the third quarter of fiscal 2004, we cashed-out options to purchase 469,887 shares of our common stock held by former employees for $0.4 million.

In accordance with EITF No. 00-23, *Issues Related to the Accounting for Stock Compensation under APB Opinion No. 25, Accounting for Stock Issued to Employees,* and FASB Interpretation No. 44*, Accounting for Certain Transactions involving Stock Compensation*, employee stock options issued within six months of the option exchange are considered replacement awards and are subject to variable accounting until the award is exercised, forfeited or canceled. As of June 30, 2004, there are 91,250 employee stock options being accounted for under these provisions.

The restricted stock awards will vest in quarterly increments over the next four years. The restricted stock award s intrinsic value of $3.8 million at the grant date is being amortized over the vesting period in tranches consistent with our accounting policy of recognizing expense for awards with graded vesting under the expense attribution method described in FASB Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*. During the third quarter and nine months ended fiscal 2004, we recognized $0.6 million and $0.8 million, respectively, of amortization associated with these awards.

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Note 10 - Pension and Retirement Plans

We sponsor a number of non-contributory defined benefit pension plans and a number of defined contribution plans, including foreign defined benefit pension plans. Additionally, we provide other post-retirement benefits, such as health care and life insurance benefits, to certain groups of retirees with most retirees contributing a portion of our costs.

The components of net periodic benefits and costs for our pension and other post-retirement benefit plans are as follows:

	Pension Plans			
	Third Quarter		Nine Months Ended	
	2004	2003	2004	2003
Service cost	$(1.9)	$(2.0)	$ (6.0)	$ (5.9)
Interest cost	(5.3)	(5.0)	(15.8)	(15.0)
Expected return on plan assets	8.9	9.0	26.7	26.9
Amorization of prior service cost	(0.2)	(0.2)	(0.5)	(0.5)
Amortization of net actuarial loss	(0.6)		(1.8)	(0.1)
Curtailments/settlements			(0.4)	
Periodic benefit of defined benefit plans	0.9	1.8	2.2	5.4
Net reclassification adjustment for discontinued operations				(0.1)
Net periodic benefit (costs):				
Defined benefit plans	0.9	1.8	2.2	5.3
Defined contribution plans	(0.3)	(0.4)	(1.0)	(1.1)
Net periodic benefit	$ 0.6	$ 1.4	$ 1.2	$ 4.2

Other Post-retirement Benefit Plans			
Third Quarter		Nine Months Ended	
2004	2003	2004	2003

Service cost	$(0.1)	$(0.2)	$(0.4)	$(0.6)
Interest cost	(0.9)	(0.9)	(2.8)	(2.6)
Amortization of prior service cost	0.2		0.6	
Amortization of net actuarial loss	(0.5)	(0.1)	(1.5)	(0.4)
Curtailments/settlements			(0.6)	
Net periodic costs	$(1.3)	$(1.2)	$(4.7)	$(3.6)

We contributed $2.5 million to our defined benefit pension plans during the third quarter of fiscal 2004 and $3.9 million during the nine months ended fiscal 2004. We anticipate contributing an additional $1.1 million to the plans in the fourth quarter of 2004 bringing our total estimated contributions for the year to $5.0 million. On June 1, 2004, the Rexair Inc. Pension Plan was merged into the Jacuzzi Brands, Inc. Master Pension Plan.

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Note 11 - Accrued Restructuring Costs

As of June 30, 2004, we had accruals of $8.7 million for restructuring costs. The activity in the restructuring liability accounts by cost category is as follows:

	Lease and Contract Related Accruals	Severance and Related Accruals	Total Accruals
Balance at September 30, 2003	$ 5.5	$ 6.0	$ 11.5
Charges	0.3	8.3	8.6
Cash payments	(1.1)	(9.3)	(10.4)
Other		(1.0)	(1.0)
Balance at June 30, 2004	$ 4.7	$ 4.0	$ 8.7

During the third quarter and nine months ended fiscal 2004, we recorded restructuring charges of $3.2 million and $8.9 million, respectively, of which $0.3 million was included in cost of products sold. These charges include:

Plant shut down and restructuring charges associated with the closure of our Salem, OH manufacturing plant and the downsizing of our Ford City, PA manufacturing plant of $2.8 million for the third quarter and $7.5 million for the nine months ended fiscal 2004. Pension and post-retirement curtailment charges of $1.0 million included in these amounts reduced the balance of our pension asset;

Severance of $1.0 million for the third quarter and $2.0 million for the nine months ended fiscal 2004 associated with the consolidation of administrative functions, the majority of which were incurred in conjunction with the opening of our new shared services center in Dallas, TX; and

A reversal of our restructuring reserve for unused lease space of $0.6 million. The space will be used to accommodate the customer service functions of the domestic whirlpool bath and spa businesses, which will be consolidated and moved to our Dallas, TX shared services center.

Approximately $6.2 million of the accrued restructuring costs at June 30, 2004 are included in the balance sheet caption Accrued expenses and other current liabilities, while the remaining $2.5 million are recorded in the balance sheet caption Other non-current liabilities. We expect the remaining accruals to be paid with cash over the periods provided by the severance and lease agreements over the next four years.

Note 12-Income Taxes

During the first quarter of fiscal 2004, we had an initial meeting with the Internal Revenue Service (IRS) to begin their audit for the fiscal years 1998 through 2002. The IRS is currently at the information gathering stage of the audit process and has not communicated any areas of concern or proposed adjustments. The IRS anticipates completing their audit in June 2005. During the second quarter of fiscal 2004, we received a tax refund of $4.0 million and interest of $2.5 million relating to the examination of the federal income tax returns for the fiscal years 1995 through 1997. The tax refund was already included in our tax rates in prior periods. The interest was included in interest income in the second quarter of fiscal 2004. We provided for taxes on earnings from continuing operations at an effective tax rate of approximately 39% for the first, second and third quarters of fiscal 2004.

During the first quarter of fiscal 2003, the IRS completed its examination of the federal income tax returns for fiscal years 1995 through 1997. We recorded tax benefits of $13.6 million in the first quarter of fiscal 2003 from audit settlements resulting from these examinations. A substantial portion of the proposed adjustments derived from the spin-off of the Company from Hanson plc in 1995. Excluding this adjustment, we provided for taxes on earnings from continuing operations at an effective tax rate of approximately 39% for the first, second and third quarters of fiscal 2003.

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Note 13- Discontinued Operations

On December 28, 2001, the Board of Directors approved a formal disposal plan, which called for the sale of five businesses, including SiTeco Lighting which was sold in October 2002.

In March 2003, the Board of Directors approved the disposal of our swimming pool and equipment, hearth and water systems businesses. During the third quarter of fiscal 2003, we disposed of the swimming pool and equipment and hearth businesses in two separate transactions. The net cash proceeds from these transactions totaled $16.7 million. In October 2003, we sold our water systems business for $3.1 million in cash. In connection with the disposal plans, we recorded a charge of $39.9 million in March 2003, which represented the difference between the historical net carrying value (including goodwill) and the estimated net realizable value of the net assets of the businesses, less costs to sell. These discontinued businesses were previously included in our Bath Products segment.

The operating results of these businesses are included in loss from discontinued operations for all periods presented, in accordance with FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* (SFAS 144).

Summarized results of these businesses are as follows:

	Third Quarter		Nine Months Ended	
	2004	2003	2004	2003
Net sales	$	$10.5	$ 2.1	$60.7
Operating income (loss)		(0.5)	(0.9)	(0.3)

Included in assets held for sale at June 30, 2004 and September 30, 2003 are properties held for sale of $3.0 million and $5.4 million, respectively. These properties are currently being marketed for sale and meet all of the criteria for classification as held for sale as required by SFAS 144. The properties are recorded at the lower of their carrying value or fair value less costs to sell. Assets held for sale and liabilities associated with assets held for sale at September 30, 2003 include assets of $11.4 million and liabilities of $8.7 million associated with our water systems business, which was sold in October 2003.

Note 14-Segment Data

We currently operate in three reportable business segments Bath Products, Plumbing Products and Rexair. The following is a summary of the significant accounts and balances by segment, reconciled to the consolidated totals.

	Bath Products	Plumbing Products	Rexair	Corporate and Other	Consolidated Total

Net Sales						
Third Quarter	2004	$253.9	$ 86.2	$ 26.7	$	$ 366.8
	2003	217.2	73.2	25.1		315.5
Nine Months Ended	2004	$698.1	$224.7	$ 80.7	$	$1,003.5
	2003	584.5	203.1	77.6		865.2
Total Operating Income (Loss)						
Third Quarter	2004	$ 14.4	$ 18.8	$ 7.5	$ (4.6)	$ 36.1
	2003	9.5	15.2	7.2	(8.0)	23.9
Nine Months Ended	2004	$ 23.1	$ 43.1	$ 20.2	$ (12.6)	$ 73.8
	2003	17.2	45.8	19.4	(13.9)	68.5
Assets						
As of June 30, 2004		$654.0	$175.8	$159.5	$365.2	$1,354.5
As of September 30, 2003		612.5	163.9	156.6	403.8	1,336.8

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Note 15-Supplemental Joint Issuer and Guarantor Financial Information

The following represents the supplemental consolidating condensed financial statements of Jacuzzi Brands, Inc. (JBI), which is the issuer of our Senior Notes, the subsidiaries which are guarantors of the Senior Notes and our subsidiaries which are not guarantors of the Senior Notes as of June 30, 2004 and September 30, 2003 and for each of the three and nine months ended June 30, 2004 and 2003. Certain of our existing and future domestic restricted subsidiaries guarantee the Senior Notes, jointly and severally, on a senior basis. The Senior Notes are secured by a first-priority lien on and security interest in substantially all of our domestic real property, plant and equipment (referred to as Notes Collateral). The Senior Notes are also secured by a second-priority lien on and security interest in the Bank Collateral (see our 2003 Annual Report on Form 10-K, filed on December 19, 2003). Separate consolidated financial statements of each guarantor are not presented, as we have determined that they would not be material to investors.

	For the Three Months Ended June 30, 2004				
	JBI	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$	$ 273.2	$ 95.6	$ (2.0)	$ 366.8
Operating costs and expenses:					
Cost of products sold		186.3	65.6	(2.0)	249.9
Selling, general and administrative expenses	5.1	52.9	19.9		77.9
Restructuring charges		2.9			2.9
Operating (loss) income	(5.1)	31.1	10.1		36.1
Interest expense	(12.3)	(0.2)	(0.4)		(12.9)
Interest income		0.2	0.1		0.3
Intercompany interest (expense) income, net	(3.5)	3.1	0.4		
Equity in earnings (losses) of investees, net	27.3	5.6		(32.9)	
Other income (expense), net		(1.0)	0.1		(0.9)
Other intercompany income (expense), net		0.2	(0.2)		
Earnings before income taxes	6.4	39.0	10.1	(32.9)	22.6
Benefit from (provision for) income taxes	7.3	(11.7)	(4.5)		(8.9)

Net earnings	$ 13.7	$ 27.3	$ 5.6	$ (32.9)	$ 13.7

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Note 15-Supplemental Joint Issuer and Guarantor Financial Information (Continued)

	For the Three Months Ended June 30, 2003				
	JBI	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$	$ 235.5	$ 81.6	$ (1.6)	$ 315.5
Operating costs and expenses:					
Cost of products sold		167.0	56.0	(1.6)	221.4
Selling, general and administrative expenses	2.6	47.2	15.2		65.0
Restructuring charges	5.2				5.2
Operating (loss) income	(7.8)	21.3	10.4		23.9
Interest expense	(10.3)	(3.8)	(0.2)		(14.3)
Interest income	0.1	0.1	0.2		0.4
Intercompany interest (expense) income, net	(7.1)	8.4	(1.3)		
Equity in earnings (losses) of investees, net	37.1	2.6		(39.7)	
Minority interest (expense) income	(15.4)	15.4			
Other income (expense), net		(1.4)	0.4		(1.0)
Other intercompany income (expense), net	0.2	4.6	(4.8)		
(Loss) earnings before income taxes	(3.2)	47.2	4.7	(39.7)	9.0
Benefit from (provision for) income taxes	8.7	(10.1)	(2.1)		(3.5)
Income (loss) from continuing operations	5.5	37.1	2.6	(39.7)	5.5
(Loss) income from discontinued operations	(0.4)	(0.4)	1.0	(0.6)	(0.4)
Net earnings	$ 5.1	$ 36.7	$ 3.6	$ (40.3)	$ 5.1

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Note 15-Supplemental Joint Issuer and Guarantor Financial Information (Continued)

	For the Nine Months Ended June 30, 2004				
	JBI	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$	$ 733.7	$ 274.6	$ (4.8)	$ 1,003.5
Operating costs and expenses:					
Cost of products sold		511.3	189.9	(4.8)	696.4
Selling, general and administrative expenses	12.6	152.4	59.7		224.7
Restructuring charges		8.6			8.6
Operating (loss) income	(12.6)	61.4	25.0		73.8
Interest expense	(37.1)	(0.7)	(0.6)		(38.4)
Interest income	2.5	0.9	0.4		3.8
Intercompany interest (expense) income, net	(10.4)	11.5	(1.1)		
Equity in earnings (losses) of investees, net	61.0	12.6		(73.6)	
Other income (expense), net	0.1	(1.8)	1.2		(0.5)
Other intercompany income (expense), net		0.1	(0.1)		
Earnings before income taxes and discontinued operations	3.5	84.0	24.8	(73.6)	38.7
Benefit from (provision for) income taxes	20.1	(24.0)	(11.2)		(15.1)
Earnings from continuing operations	23.6	60.0	13.6	(73.6)	23.6
Loss from discontinued operations	(0.6)	(0.6)	(1.0)	1.6	(0.6)
Net earnings	$ 23.0	$ 59.4	$ 12.6	$ (72.0)	$ 23.0

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Note 15-Supplemental Joint Issuer and Guarantor Financial Information (Continued)

	For the Nine Months Ended June 30, 2003				
	JBI	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net sales	$	$ 645.4	$ 223.2	$ (3.4)	$ 865.2
Operating costs and expenses:					
Cost of products sold		449.0	153.6	(3.4)	599.2
Selling, general and administrative expenses	5.3	140.5	43.4		189.2
Restructuring charges	8.3				8.3
Operating (loss) income	(13.6)	55.9	26.2		68.5
Interest expense	(32.0)	(14.2)	(0.7)		(46.9)
Interest income	0.5	0.4	0.4		1.3
Intercompany interest (expense) income, net	(13.8)	20.6	(6.8)		
Equity in earnings (losses) of investees, net	110.9	4.7		(115.6)	
Minority interest (expense) income	(46.2)	46.2			
Other (expense) income, net	(1.8)	(1.7)			(3.5)
Other intercompany income (expense), net	0.4	10.2	(10.6)		
Earnings before income taxes and discontinued operations	4.4	122.1	8.5	(115.6)	19.4
Benefit from (provision for) income taxes	21.1	(11.2)	(3.8)		6.1
Earnings from continuing operations	25.5	110.9	4.7	(115.6)	25.5
Loss from discontinued operations	(40.3)	(40.3)	(26.2)	66.5	(40.3)
Net (loss) earnings	$ (14.8)	$ 70.6	$ (21.5)	$ (49.1)	$ (14.8)

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Note 15-Supplemental Joint Issuer and Guarantor Financial Information (Continued)

	At June 30, 2004				
	JBI	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Current assets:					
Cash and cash equivalents	$ (0.4)	$ (2.7)	$ 29.2	$	$ 26.1
Trade receivables, net		163.9	92.9		256.8
Inventories		149.0	45.2		194.2
Deferred income taxes	27.9	(12.4)	1.0		16.5
Assets held for sale		3.0			3.0
Other current assets	4.1	7.4	11.8		23.3
Total current assets	31.6	308.2	180.1		519.9
Property, plant and equipment, net	1.0	76.1	48.0		125.1
Pension assets	154.1				154.1
Insurance for asbestos claims		160.0			160.0
Goodwill		229.2	59.5		288.7
Other intangibles, net		60.0			60.0
Other non-current assets	27.0	19.0	0.7		46.7
Investment in subsidiaries/ Intercompany receivable (payable), net	586.5	790.8	169.4	(1,546.7)	
Total assets	$ 800.2	$ 1,643.3	$ 457.7	$ (1,546.7)	$ 1,354.5
LIABILITIES AND STOCKHOLDERS EQUITY					
Current liabilities:					
Notes payable	$	$	$ 21.9	$	$ 21.9
Current maturities of long-term debt	27.8	1.4			29.2
Trade accounts payable		55.7	57.0		112.7
Income taxes payable	(1.5)	16.3	4.6		19.4
Accrued expenses and other current liabilities	9.7	87.2	30.2		127.1

Total current liabilities	36.0	160.6	113.7		310.3
Long-term debt	441.8	5.0			446.8
Deferred income taxes	(6.2)	24.6	(0.1)		18.3
Asbestos claims		160.0			160.0
Other non-current liabilities	41.3	69.9	20.6		131.8
Total liabilities	512.9	420.1	134.2		1,067.2
Commitments and contingencies					
Stockholders equity	287.3	1,223.2	323.5	(1,546.7)	287.3
Total liabilities and stockholders equity	$800.2	$ 1,643.3	$ 457.7	$ (1,546.7)	$ 1,354.5

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Note 15-Supplemental Joint Issuer and Guarantor Financial Information (Continued)

	At September 30, 2003				
	JBI	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Current assets:					
Cash and cash equivalents	$ 0.2	$ 2.9	$ 28.1	$	$ 31.2
Trade receivables, net		143.9	85.7		229.6
Inventories		127.6	37.4		165.0
Deferred income taxes	27.9	(12.4)			15.5
Assets held for sale		11.9	4.9		16.8
Other current assets	3.2	12.0	14.9		30.1
Total current assets	31.3	285.9	171.0		488.2
Property, plant and equipment, net	0.5	84.3	44.9		129.7
Pension assets	148.3				148.3
Insurance for asbestos claims		160.0			160.0
Goodwill		229.2	53.9		283.1
Other intangibles, net		60.8			60.8
Other non-current assets	28.7	37.9	0.1		66.7
Investment in subsidiaries/Intercompany receivable (payable), net	568.7	829.1	160.6	(1,558.4)	
Total assets	$ 777.5	$ 1,687.2	$ 430.5	$ (1,558.4)	$ 1,336.8
LIABILITIES AND STOCKHOLDERS EQUITY					
Current liabilities:					
Notes payable	$	$	$ 23.5	$	$ 23.5
Current maturities of long-term debt	23.9	1.3			25.2
Trade accounts payable		56.0	46.3		102.3
Income taxes payable	2.2	8.0	0.6		10.8
Liabilities associated with assets held for sale		6.4	2.3		8.7
Accrued expenses and other current liabilities	27.9	79.7	28.6		136.2

Total current liabilities	54.0	151.4	101.3		306.7
Long-term debt	445.0	6.4			451.4
Minority interest		91.5		(91.5)	
Deferred income taxes	(6.2)	31.9	0.5		26.2
Asbestos claims		160.0			160.0
Other non-current liabilities	29.0	89.0	18.8		136.8
Total liabilities	521.8	530.2	120.6	(91.5)	1,081.1
Commitments and contingencies					
Stockholders equity	255.7	1,157.0	309.9	(1,466.9)	255.7
Total liabilities and stockholders equity	$777.5	$ 1,687.2	$ 430.5	$(1,558.4)	$ 1,336.8

JACUZZI BRANDS, INC.
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Note 15-Supplemental Joint Issuer and Guarantor Financial Information (Continued)

	For the Nine Months Ended June 30, 2004				
	JBI	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Consolidated
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	$ 11.4	$ (34.5)	$ 29.4	$	$ 6.3
INVESTING ACTIVITIES:					
Proceeds from sale of businesses, net		2.4	2.1		4.5
Purchases of property, plant and equipment	(0.6)	(7.3)	(4.2)		(12.1)
Proceeds from sale of real estate			3.2		3.2
Proceeds from the sale of fixed assets		0.3	0.2		0.5
Net transfers with subsidiaries	(11.2)	12.5		(1.3)	
NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES	(11.8)	7.9	1.3	(1.3)	(3.9)
FINANCING ACTIVITIES:					
Proceeds from long-term debt	44.1	0.1			44.2
Repayment of long-term debt	(43.4)	(1.3)			(44.7)
Payment of financing fees	(1.6)				(1.6)
Proceeds from the issuance of common stock for option exercises	0.9				0.9
Decrease in notes payable, net			(4.1)		(4.1)
Net transfers with parent		11.2	(12.5)	1.3	
NET CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES	0.0	10.0	(16.6)	1.3	(5.3)
Effect of exchange rate changes on cash and cash equivalents	(0.2)	11.0	(13.0)		(2.2)
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(0.6)	(5.6)	1.1		(5.1)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	0.2	2.9	28.1		31.2
	$ (0.4)	$ (2.7)	$ 29.2	$	$ 26.1

CASH AND CASH EQUIVALENTS AT END OF PERIOD	—	—	—	—	—

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(Tabular amounts in millions)
(unaudited)

Note 15-Supplemental Joint Issuer and Guarantor Financial Information (Continued)

	For the Nine Months Ended June 30, 2003				
	JBI	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Consolidated
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	$ (52.5)	$ (9.0)	$ 89.3	$	$ 27.8
INVESTING ACTIVITIES:					
Proceeds from sale of businesses, net		107.1	13.4		120.5
Purchases of property, plant and equipment		(9.0)	(2.4)		(11.4)
Proceeds from sale of real estate		11.0			11.0
Proceeds from the sale of fixed assets		0.1			0.1
Net transfers with subsidiaries	13.9	105.3		(119.2)	
NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES	13.9	214.5	11.0	(119.2)	120.2
FINANCING ACTIVITIES:					
Proceeds from long-term debt	42.1				42.1
Repayment of long-term debt	(136.5)	(185.1)			(321.6)
Escrow deposits in restricted cash collateral accounts	(60.9)				(60.9)
Escrow withdrawals in restricted cash collateral accounts	178.1				178.1
Payment of financing fees	(7.9)	(1.0)			(8.9)
Increase in notes payable, net			5.5		5.5
Net transfers with parent		(13.9)	(105.3)	119.2	
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	14.9	(200.0)	(99.8)	119.2	(165.7)
Effect of exchange rate changes on cash and cash equivalents	24.1	(12.6)	(4.5)		7.0
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	0.4	(7.1)	(4.0)		(10.7)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	0.3	11.0	20.8		32.1
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 0.7	$ 3.9	$ 16.8	$	$ 21.4

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Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

(Tabular amounts in millions)

Disclosure Concerning Forward-Looking Statements

In December 1995, the Private Securities Litigation Reform Act of 1995 (the Reform Act) was enacted by the United States Congress. The Reform Act, as amended, contains certain amendments to the Securities Act of 1933 and the Securities Exchange Act of 1934. These amendments provide protection from liability in private lawsuits for forward-looking statements made by public companies. We choose to take advantage of the safe harbor provisions of the Reform Act.

This Quarterly Report on Form 10-Q contains both historical information and other information. While we have specifically identified certain information as being forward-looking in the context of its presentation, we caution the reader that, with the exception of information that is clearly historical, all the information contained in this Quarterly Report on Form 10-Q should be considered to be forward-looking statements as referred to in the Reform Act. Without limitation, when we use the words believe, estimate, plan, expect, intend, anticipate, continue, p probably, should, will and similar expressions, we intend to clearly express that the information deals with possible future events and is forward-looking in nature.

Forward-looking information involves risks and uncertainties. This information is based on various factors and assumptions about future events that may or may not actually come true. As a result, our operations and financial results in the future could differ substantially from those we have discussed in the forward-looking statements in this Quarterly Report and other documents that have been filed or furnished with the Securities and Exchange Commission. In particular, various economic and competitive factors, including those outside our control, such as interest rates, foreign currency exchange rates, inflation rates, instability in domestic and foreign financial markets, acts of war, terrorist acts, outbreak of new diseases, consumer spending patterns, energy costs and availability, freight costs, availability of consumer and commercial credit, adverse weather, levels of residential and commercial construction, changes in raw material and component costs and the creditworthiness of our customers, insurers and investees, could cause our actual results during the remainder of 2004 and in future years to differ materially from those expressed in any forward-looking statement made in this Quarterly Report on Form 10-Q. In addition, under the heading Critical Accounting Policies and Estimates in the Management s Discussion and Analysis of Financial Condition and Results of Operations section of our Annual Report on Form 10-K, we describe various estimates and assumptions that we make that affect the reported amounts of assets, liabilities, sales and expenses as well as the disclosure of contingent assets and liabilities. Future revisions to these estimates and assumptions may cause these amounts, when reported, to differ materially from those expressed in any forward-looking statement made in this Quarterly Report on Form 10-Q, particularly with respect to statements relating to pension and other post-retirement benefits, asbestos liabilities, self-insurance reserves, inventories and trade receivables. All subsequent written and oral forward-looking statements attributable to Jacuzzi Brands, Inc. and our subsidiaries are expressly qualified in their entirety by the foregoing factors.

Results of Operations

Overview

Jacuzzi Brands, Inc., through our subsidiaries, is a leading global producer of branded bath and plumbing products for the residential, commercial and institutional markets. We currently operate under three segments Bath Products, Plumbing Products and Rexair.

Our Bath Products segment manufactures and distributes whirlpool baths, spas, showers, sanitary ware, including sinks and toilets, and bathtubs for the residential construction and remodeling markets. The residential construction and remodeling markets have been strong for the last several years primarily as a result of lower interest rates and overall strong demand. We believe that interest rates will remain a primary driver of these markets in the short-term, and that macro-economic and demographic factors such as population growth will drive demand for residential construction and remodeling over the long-term.

Our Plumbing Products segment manufactures professional grade drainage, water control, commercial brass and PEX piping products for the commercial and institutional construction, renovation and facilities maintenance markets. Growth in the commercial and institutional markets has started to rebound after contracting over the past couple of years. We believe that macro-economic and demographic factors such as population and infrastructure growth will drive growth in these markets over the long-term.

Our Rexair segment manufactures premium vacuum cleaner systems sold through independent distributors in the direct sales retail channel.

In December 2001, we approved a formal disposal plan for the sale of five businesses, and in February 2003, we approved a formal disposal plan for the sale of three businesses. We completed the sale of these businesses during the

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period from January 2002 through October 2003, transforming us from a diversified industrial conglomerate into a focused operating company. The results of these discontinued businesses are excluded from our results from continuing operations for all periods presented and from any discussions of our continuing operating results. They are, however, included in our results from discontinued operations and are discussed separately in **Note 13** to our Condensed Consolidated Financial Statements included in this Report on Form 10-Q.

Overall

	Third Quarter		Nine Months Ended	
	2004	**2003**	**2004**	**2003**
Net sales				
Bath Products	$253.9	$217.2	$ 698.1	$584.5
Plumbing Products	86.2	73.2	224.7	203.1
Rexair	26.7	25.1	80.7	77.6
Total net sales	$366.8	$315.5	$1,003.5	$865.2
Operating income				
Bath Products	$ 14.4	$ 9.5	$ 23.1	$ 17.2
Plumbing Products	18.8	15.2	43.1	45.8
Rexair	7.5	7.2	20.2	19.4
	40.7	31.9	86.4	82.4
Corporate expenses	(4.6)	(8.0)	(12.6)	(13.9)
Total operating income	$ 36.1	$ 23.9	$ 73.8	$ 68.5

Net sales for the third quarter of fiscal 2004 increased 16.3% to $366.8 million from $315.5 million in the same period last year as a result of increased sales in each of our three segments. Net sales in the third quarter of fiscal 2004 also benefited from favorable fluctuations in currency exchange rates of $8.5 million.

Net sales for the nine months ended fiscal 2004 rose 16.0% to $1,003.5 million from $865.2 million in the same period last year. The increase in net sales was the result of improved sales in all segments, with the most significant increase achieved in our Bath Products segment. Net sales for the nine months ended fiscal 2004 also benefited from favorable fluctuations in currency exchange rates of $30.1 million and an additional week of sales as 2004 is a 53-week year. Net sales for the nine months ended fiscal 2003 included the technology license sale of $8.6 million.

Operating income increased 51.0%, to $36.1 million in the third quarter of fiscal 2004 as a result of sales growth in all segments. We incurred $3.2 million of restructuring charges associated with the shut down of our Salem, OH cast iron plant, the downsizing of our Ford City, PA ceramic plant and the continued consolidation of administrative functions

in the Dallas, TX shared services center in the third quarter of fiscal 2004. Operating income in the third quarter of fiscal 2003 included $5.2 million in restructuring charges related to the reorganization and consolidation of our corporate headquarters, reflecting our operating company organization. The reorganization resulted in a number of management changes and the relocation and consolidation of the Jacuzzi headquarters in Walnut Creek, CA into our principal offices in West Palm Beach, FL.

Operating income in the nine months ended fiscal 2004 increased $5.3 million compared to the same period of the prior year. Increased operating income from strong sales growth was partially offset by restructuring charges of $8.9 million related to the Salem, OH plant closure, Ford City, PA downsizing and the shared services margin improvement projects. Operating income for the nine months ended fiscal 2004 also included $4.1 million in charges related to non-performing customer notes incurred as a result of financial difficulties encountered by several of our Brazilian bath product distributors. Operating income in the nine months ended fiscal 2003 included $8.6 million for the sale of a technology license and $8.3 million of restructuring charges associated with the reorganization and consolidation of our corporate headquarters.

Operating income in the third quarter and nine months ended fiscal 2004 benefited from favorable fluctuations in currency exchange rates of $1.0 million and $2.8 million, respectively.

On March 17, 2004, in connection with an option exchange offer, we accepted for cancellation options to purchase 1,903,337 shares of our common stock, and granted 435,730 restricted shares of our common stock (restricted stock awards) in exchange. Participants tendered 100% of the options eligible to be exchanged. We subsequently cashed-out

options to purchase 469,887 shares of our common stock held by former employees for $0.4 million. The charges related to the cash-out offer were recorded entirely in the third quarter of fiscal 2004.

The restricted stock awards will vest in quarterly increments over the next four years. The restricted stock award s intrinsic value of $3.8 million at the grant date will be amortized over the vesting period in tranches consistent with our accounting policy of recognizing expense for awards with graded vesting under the expense attribution method described in FASB Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*. We recognized $0.6 million and $0.8 million of amortization associated with these restricted stock awards in the third quarter and nine months ended fiscal 2004, respectively, and expect to recognize an additional $0.5 million of amortization in the fourth quarter of fiscal 2004.

Bath Products

Sales in the Bath Products segment increased $36.7 million and $113.6 million for the third quarter and nine months ended fiscal 2004, respectively, in comparison with the same periods in fiscal 2003. The sales increases were led by increased sales of our domestic spas, reflecting improved volume and increases in our average selling prices, and increased sales of our domestic whirlpool baths, reflecting strong performance in both jetted and non-jetted baths. The U.K. also contributed to the sales increase mainly due to growth in the home sector. Favorable currency exchange rates contributed $8.5 million and $30.1 million to the sales increases for the third quarter and nine months ended fiscal 2004, respectively.

Operating income for the third quarter of fiscal 2004 increased 51.6% to $14.4 million compared to the third quarter of the prior year. Operating income increased on a year-to-date basis by 34.3% to $23.1 million compared to the nine months ended fiscal 2003. The increase for both periods was primarily the result of strong sales and margin growth in the domestic spa and whirlpool bath businesses. Gross margin increased as a percentage of sales mainly due to increased volume over fixed overhead and improved manufacturing efficiencies. Strong earnings growth was accomplished despite restructuring charges incurred during the third quarter and nine months ended fiscal 2004 of $3.8 million and $9.5 million, respectively. The year-to-date period was also impacted by a $1.0 million write off of accounts receivable associated with the bankruptcy of a domestic distributor, a $4.1 million increase in our bad debt reserves associated with financial difficulties encountered by several Brazilian bath product distributors and $1.0 million in severance related to staffing reductions in Brazil. We have since taken over sales responsibility for the Brazilian home center channel, and expect this action to result in improved sales, margins and customer service for this segment as we are now directly in control of sales into this channel. Operating results for the nine months ended fiscal 2003 included start-up costs associated with the move to a new whirlpool bath manufacturing facility in Chino, CA; costs incurred to implement process improvements designed to improve quality and efficiency at the new plant; and costs associated with the initial stocking of the Lowe s home centers.

The restructuring charges incurred in the third quarter of fiscal 2004 related to the closure of the Salem, OH plant ($2.2 million), the downsizing of the Ford City, PA plant ($0.6 million) and the continued consolidation of administrative functions, the majority of which were incurred in conjunction with the opening of our new shared services center in Dallas, TX ($1.0 million). On a year-to-date basis, restructuring charges for these initiatives were $5.9 million for the Salem plant, $1.6 million for the Ford City plant and $2.0 million for the shared services center.

The Salem, OH plant ceased production in May 2004. In the second quarter of fiscal 2004, we announced a plan to downsize our Ford City, PA ceramic plant and eliminate approximately 200 positions at the plant. We recorded a $1.0 million restructuring charge in the second quarter for pension and post-retirement benefit curtailments associated with the elimination of these positions. We expect the Ford City downsizing to be substantially complete by the end of fiscal 2004. The consolidation and relocation of the customer service functions of our domestic whirlpool bath and spa businesses to our shared services center was initiated in the third quarter of fiscal 2004 and is expected to decrease

costs and improve customer satisfaction. We expect to incur approximately $4.0 million in additional restructuring charges related to the Salem ($0.7 million), Ford City ($2.0 million) and shared services initiatives ($1.3 million) over the next quarter. Fiscal 2004 restructuring costs to be recorded in the Bath Products segment for these initiatives are expected to total approximately $13.5 million, with the benefits of these actions taking effect in fiscal 2005. Including a reversal of a restructuring reserve for unused lease space of $0.6 million recorded in corporate expenses, total net restructuring costs for these initiatives are expected to be $12.9 million for the year.

Each of these actions are part of our previously announced plans to improve margins in the Bath Products segment in general and the sanitary ware business specifically by eliminating high-cost manufacturing through lower-cost sourcing and improved customer service.

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Litigation with the former owners of the Sundance Spas business has resulted in a judgment of approximately $5.1 million in our favor. The favorable financial impact of the judgment of $3.9 million has not been included in our results of operations as it is subject to a potential appeal. We incurred litigation expense as a result of this legal action of $0.1 million and $1.1 million in the third quarter and the nine months ended fiscal 2004, respectively.

Operating income in fiscal 2004 was positively impacted by $1.0 million in the third quarter and $2.8 million in the nine months ended fiscal 2004 as a result of foreign currency exchange rate fluctuations.

Plumbing Products

Sales in the Plumbing Products segment increased $13.0 million and $21.6 million in the third quarter and the nine months ended fiscal 2004, respectively, as compared to the same periods last year. Sales increased across all product lines due to effective marketing and product innovation efforts as well as a slight rebound in the U.S. commercial and institutional construction markets. Included in year-to-date fiscal 2003 results was $8.6 million in sales recognized upon the granting of a license for certain technology that had been the subject of patent litigation.

Operating income increased $3.6 million in the third quarter of fiscal 2004 and decreased $2.7 million in the nine months ended fiscal 2004 in comparison with the same periods of fiscal 2003. The year-to-date decrease was a result of the $8.6 million technology license sale in the second quarter of fiscal 2003. Excluding this sale, operating income increased for the nine months ended fiscal 2004. The increase for both periods was the result of improved sales, which more than offset higher scrap iron and steel costs. We have implemented initiatives targeting procurement and finished product pricing to offset these margin pressures. The third quarter results include benefits realized from these procurement and pricing initiatives, some of which are not expected to reach full effect until next quarter.

Rexair

Rexair sales increased $1.6 million and $3.1 million in the third quarter and the nine months ended fiscal 2004, respectively, as compared with the same periods of the previous year. The sales increases were primarily due to higher volume and the higher price points of the new ***e***2 RAINBOW™ vacuum cleaner system, which was launched earlier this year. The rollout of the new ***e***2 model was completed during the second quarter of fiscal 2004.

Operating income in the third quarter and the nine months ended fiscal 2004 increased by $0.3 million and $0.8 million, respectively, as compared with the same periods of fiscal 2003. The increase in operating income in the third quarter of fiscal 2004 is primarily the result of higher sales. During fiscal 2003, an inventory reduction program was in place that negatively impacted operating income by approximately $1.0 million in the first nine months of that year.

Corporate Expenses

Corporate expenses decreased $3.4 million and $1.3 million in the third quarter and the nine months ended fiscal 2004, respectively, as compared to the same periods last year. The third quarter of fiscal 2004 includes a reversal of the restructuring reserve for unused lease space in Dallas, TX of $0.6 million. The space will be used by the customer service function of the shared services operations center. Corporate expenses in the third quarter and nine months ended fiscal 2004 also reflect reductions in pension income due to a lower discount rate, costs associated with Sarbanes-Oxley compliance, an increase in consulting fees and an increase in personnel costs reflecting our new operating company organization. The third quarter and first nine months of fiscal 2004 include charges totaling $0.8 million and $0.9 million, respectively, associated with our previously announced employee stock option buy back and exchange offer. We recorded $5.2 million and $8.3 million of restructuring charges in the third quarter and nine months ended fiscal 2003 related to the reorganization and consolidation of our corporate headquarters.

Interest Income and Expense

Interest expense for the third quarter and nine months ended fiscal 2004 declined by $1.4 million and $8.5 million, respectively, from the comparable prior year periods. The lower interest expense reflects the reduction in debt balances resulting from our restructuring and refinancing in the fourth quarter of fiscal 2003, as well as lower interest rates.

The increase in interest income of $2.5 million for the nine months ended fiscal 2004 as compared to the prior year was due entirely to interest received from the IRS related to a prior year audit settlement (see **Taxes**).

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Other Expense, net

Included in other expense, net for both years are expenses associated with retained liabilities of our ladder operations which were sold in October 1999. The nine months ended fiscal 2004 includes a $2.4 million gain on the settlement and collection of a portion of a note we held from the owners of a power plant constructed by one of our former subsidiaries. In addition, the nine months ended fiscal 2004 includes a gain of $3.2 million resulting from the resolution of litigation that was under appeal and a $0.9 million gain on the sale of real estate. The third quarter and nine months ended fiscal 2003 include $0.2 million and $2.3 million, respectively, of professional fees associated with the restructuring of our debt. In addition, the nine months ended fiscal 2003 includes a gain of $3.4 million on the sale of real estate.

Taxes

During the first quarter of fiscal 2004, we had an initial meeting with the Internal Revenue Service (IRS) to begin their audit for the fiscal years 1998 through 2002. The IRS is currently at the information gathering stage of the audit process and has not communicated any areas of concern or proposed adjustments. The IRS anticipates completing their audit in June 2005. During the second quarter of fiscal 2004, we received a tax refund of $4.0 million and interest of $2.5 million relating to the examination of the federal income tax returns for the fiscal years 1995 through 1997. The tax refund was already included in our tax rates in prior periods. The interest was included in interest income in the second quarter of fiscal 2004. We provided for taxes on earnings from continuing operations at an effective tax rate of approximately 39% for the first, second and third quarters of fiscal 2004.

During the first quarter of fiscal 2003, the IRS completed its examination of the federal income tax returns for fiscal years 1995 through 1997. We recorded tax benefits of $13.6 million in the first quarter of fiscal 2003 from audit settlements resulting from these examinations. A substantial portion of the proposed adjustments derived from the spin-off of the Company from Hanson plc in 1995. Excluding this adjustment, we provided for taxes on earnings from continuing operations at an effective tax rate of approximately 39% for the first, second and third quarters of fiscal 2003.

Accrued Restructuring Costs

As of June 30, 2004, we had accruals of $8.7 million for restructuring costs. The activity in the restructuring liability accounts by cost category is as follows:

	Lease and Contract Related Accruals	Severance and Related Accruals	Total Accruals
Balance at September 30, 2003	$ 5.5	$ 6.0	$ 11.5
Charges	0.3	8.3	8.6
Cash payments	(1.1)	(9.3)	(10.4)
Other		(1.0)	(1.0)
Balance at June 30, 2004	$ 4.7	$ 4.0	$ 8.7

During the third quarter and nine months ended fiscal 2004, we recorded restructuring charges of $3.2 million and $8.9 million, respectively, of which $0.3 million was included in cost of products sold. These charges include:

- Plant shut down and restructuring charges associated with the closure of our Salem, OH manufacturing plant and the downsizing of our Ford City, PA manufacturing plant of $2.8 million for the third quarter and $7.5 million for the nine months ended fiscal 2004. Pension and post-retirement curtailment charges of $1.0 million included in these amounts reduced the balance of our pension asset;

- Severance of $1.0 million for the third quarter and $2.0 million for the nine months ended fiscal 2004 associated with the consolidation of administrative functions, the majority of which were incurred in conjunction with the opening of our new shared services center in Dallas, TX; and

- A reversal of our restructuring reserve for unused lease space of $0.6 million. The space will be used to accommodate the customer service functions of the domestic whirlpool bath and spa businesses, which will be consolidated and moved to our Dallas, TX shared services center.

Approximately $6.2 million of the accrued restructuring costs at June 30, 2004 are included in the balance sheet caption Accrued expenses and other current liabilities, while the remaining $2.5 million are recorded in the balance sheet caption Other non-current liabilities. We expect the remaining accruals to be paid with cash over the periods provided by the severance and lease agreements over the next four years.

Liquidity and Capital Resources

Our primary sources of liquidity and capital resources are cash and cash equivalents, cash provided from operations and available borrowings. We expect to satisfy operating needs and the cash requirements related to our capital expenditures and restructurings through operating cash flows and borrowings under our existing bank facilities.

Net cash provided by operating activities of continuing operations was $8.1 million for the nine months ended fiscal 2004, compared to net cash provided by operating activities of $37.0 million for the same period of fiscal 2003. In fiscal 2003, we received $53.9 million of income tax refunds and $8.6 million as a result of a technology sale, offset by payments of liabilities we had previously accrued related to retained liabilities for operations we had sold during that year. We typically use cash in the first half of the fiscal year and generate cash in the second half of the fiscal year due to the seasonality of most of our businesses. Weather can significantly influence both residential and non-residential construction and installation, which ultimately affects sales in our Bath Products and Plumbing Products segments. Sales of outdoor jetted spas and other products are also sensitive to weather conditions and tend to decrease during the fall and winter months (predominantly the first and second fiscal quarters).

Trade receivables, net increased $27.2 million, or 11.8%, predominately due to seasonality and increased sales in the Bath Products segment. The increase in inventories of $29.2 million, or 17.7%, was caused by a build-up of inventory levels in anticipation of higher sales volume in the second half of fiscal 2004, which we typically experience due to the aforementioned seasonality conditions. Inventory levels have also increased in the transition to sourced inventory products as a result of closing the Salem, OH plant and downsizing the Ford City, PA facility. Over the next quarter, we expect to use additional cash of $0.9 million related to the Salem, OH plant closure, $1.6 million related to the downsizing of our Ford City, PA facility and $0.8 million associated with our shared services center.

During the nine months ended June 30, 2004, we paid approximately $10.4 million, and expect to pay approximately $6.2 million over the next twelve months, related to our restructuring plans.

Our discontinued operations used cash of $1.8 million during the nine months ended fiscal 2004 as compared to $9.2 million used in the same period of fiscal 2003. The net cash used in the nine months ended fiscal 2004 pertained to the operations of our water systems business, which was sold in October 2003. In the nine months ended fiscal 2003, our swimming pool and equipment business experienced increased cash requirements as was typical for this business in the winter months. We sold this business in May 2003.

We received $4.5 million from sold businesses in the nine months ended fiscal 2004. Approximately $2.4 million related to the sale of our water systems business in October 2003 and $2.1 million related to payments received in connection with the sale of our swimming pool and equipment business in May 2003. We also received $3.2 million from the sale of excess real estate and $0.5 million from the sale of fixed assets and paid $12.1 million for capital expenditures. In the nine months ended fiscal 2003, we received net proceeds of $103.8 million from the sale of SiTeco Lighting, $16.0 million for the pool and pool equipment businesses and $0.7 million from the sale of the hearth business. Additionally, we received net proceeds of $11.0 million from the sale of real estate, partially offset by $11.4 million of capital expenditures.

Upon the sale of Spear & Jackson in September 2002, we retained 3,543,281 common shares of the buyer who subsequently changed its name to Spear & Jackson. We are subject to restrictions on the voting and disposition of these shares and have no involvement in the management or operation of Spear & Jackson. The investment was recorded at its fair value of $1.0 million at the date of acquisition based on an independent valuation. The carrying value of the investment was adjusted to $22.0 million at September 30, 2003 in accordance with FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. FASB Statement No. 115 requires that investments such as this be adjusted to fair market value at the end of each reporting period. Fluctuations in the value

of this investment are recorded in other comprehensive income as unrealized gains and losses, net of tax. The carrying value of the investment has been adjusted to its market value of $5.5 million as of June 30, 2004. This represents a reduction in value of $16.5 million since September 30, 2003. On April 16, 2004, the Securities and Exchange Commission filed a complaint and obtained a temporary restraining order against the CEO and major shareholder of Spear & Jackson for, among other things, illegally acquiring shares of Spear & Jackson. We are restricted from disposing of our investment in the common shares of Spear & Jackson until September 2004.

On June 30, 2004, we amended our asset-based revolving credit facility and term loan (collectively the Bank Facilities), which provides for:

a reduction in the interest rate of our term loan from Prime plus 5% with a minimum rate of 9.25% to 500 basis points over LIBOR;

the elimination of annual prepayments on the term loan of $10 million, which were scheduled to begin in August 2005;

- the elimination of annual prepayments on the term loan equal to 25% of our annual consolidated excess cash flow, as determined by the original loan agreement;
- the extension of the term loan s maturity date by one year to July 15, 2009; and
- the elimination of all debt covenants except the requirement to maintain a minimum consolidated fixed charge coverage ratio. This requirement is applicable only if our availability under the asset-based credit facility falls below $20 million.

This amendment was not considered a substantial modification of our debt under the guidance provided in EITF Issue No. 96-19, *Debtor s Accounting for a Modification or Exchange of Debt Instruments*.

Under the five-year asset-based revolving credit facility, we can borrow up to $200.0 million subject to a borrowing base consisting of eligible accounts receivable and eligible inventory, plus eligible trademarks. The initial amount of eligible trademarks of $20.0 million is being amortized monthly over the first two years of the facility as a reduction of the borrowing base. At June 30, 2004, we had approximately $153.0 million available to be borrowed under the asset-based facility, of which we had utilized approximately $69.8 million (including $42.0 million of letters of credit), leaving $83.2 million available for additional borrowings. In addition, we have outstanding bankers acceptances of $2.1 million which does not affect availability under the asset-based facility.

The weighted average interest rate on borrowings under the asset-based credit facility was 3.6% for the nine months ended fiscal 2004. We were not subject to the debt covenant at June 30, 2004 because our availability exceeded $20.0 million. We expect to maintain availability in excess of $20.0 million for the foreseeable future. There are several fees associated with the asset-based credit facility including an unused commitment fee of 0.5%, a letter of credit fee equal to the applicable LIBOR margin and a fronting fee of 0.125% on all outstanding letters of credit.

The Bank Facilities contain a subjective acceleration clause and a requirement to maintain a lockbox associated with our asset-based facility. As required by EITF Issue No. 95-22, *Balance Sheet Classification of Borrowings Outstanding under Revolving Credit Agreements that Include both a Subjective Acceleration Clause and a Lockbox Arrangement*, the entire balance of the asset-based facility is included in current maturities of long-term debt.

The $380 million, 9.625% notes (the Senior Notes), which are due July 1, 2010 and require the payment of interest of $18.3 million on January 1 and July 1 of each year, were subject to registration with the Securities and Exchange Commission pursuant to a registration rights agreement. On February 17, 2004, we completed an offer to exchange new, registered Senior Notes for the then outstanding unregistered notes. The terms of the new, registered Senior Notes are identical, in all material respects, to the terms of the then outstanding unregistered notes, except that the new Senior Notes have been registered under the Securities Act, and the transfer restrictions and registration rights relating to the unregistered notes do not apply to the registered Senior Notes.

During the nine months ended fiscal 2004, we repaid $4.6 million of our debt, including a $3.2 million permanent reduction of our term loan. We also paid $1.6 million of financing fees related to our Bank Facilities and Senior Notes. In the nine months ended fiscal 2003, we reduced our debt borrowings by $274.0 million and paid $8.9 million in financing fees. In fiscal 2003, we also withdrew $117.2 million from our restricted cash collateral accounts, the establishment and depletion of which was prescribed by the terms of our then outstanding bank facilities. Cash withdrawn from these accounts was used for the payment of previously outstanding debt.

Certain of our existing and future domestic restricted subsidiaries guarantee the Senior Notes, jointly and severally, on a senior basis. The Senior Notes are secured by a first-priority lien on and security interest in substantially all our domestic real property, plant and equipment (referred to as Notes Collateral). The Senior Notes are also secured by a second-priority lien on and security interests in the Bank Collateral which consists of existing and future domestic

subsidiaries and 65% of the capital stock of, or other equity interest in, existing and future first-tier foreign subsidiaries and substantially all of the other assets (other than the assets that constitute Notes Collateral), in each case that are held by Jacuzzi Brands, Inc. or any of our subsidiary guarantors. Obligations under the Bank Facilities are secured by a first priority lien on the Bank Collateral and a second priority lien on the Notes Collateral.

The outstanding debt balances and the maximum availability under these debt instruments at June 30, 2004 were as follows:

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	Maximum Availability	Amount Outstanding	Applicable Interest Rate
Senior Notes	$ 380.0	$ 380.0	9.625%
Asset-based credit facility	153.0	27.8	2.25% over LIBOR or 0.25% over Prime
Term Loan	61.8	61.8	500 basis points over LIBOR
US Brass Note	6.4	6.4	Interest imputed at 9.5%
Total	$ 601.2	$ 476.0	

In the nine months ended fiscal 2004, we paid $42.4 million of interest on our borrowings. Below is a summary of our significant contractual obligations, which reflects the amendment to our Bank Facilities, discussed above:

	Payments Due in Fiscal						Payments Due Thereafter
	Total	2004	2005	2006	2007	2008	
Long-term debt	$476.0	$27.8	$1.4	$1.5	$1.7	$1.8	$441.8
Notes payable	21.9	21.9					
Lease obligations	27.0	2.4	7.8	6.2	4.4	2.5	3.7
Total contractual cash obligations	$524.9	$52.1	$9.2	$7.7	$6.1	$4.3	$445.5

Additional information regarding our long-term debt structure can be found in our 2003 Annual Report on Form 10-K, filed on December 19, 2003.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

In the normal course of doing business, we are exposed to the risks associated with changes in interest rates and currency exchange rates. To limit the risks from such fluctuations, we have in the past, and may in the future, enter into various hedging transactions that have been authorized pursuant to our policies, but do not engage in such transactions for trading purposes.

To manage exposure to interest rate movements, we have used interest rate protection agreements. However, as of June 30, 2004, we do not have any such agreements outstanding. Based on our overall exposure to interest rate changes under our existing debt structure (see **Note 5** to our Condensed Consolidated Financial Statements), a hypothetical increase of 100 basis points across all maturities of our floating rate debt obligations, would decrease our estimated pre-tax earnings in the twelve month period by approximately $0.8 million. There were no swap agreements

outstanding during any portion of the nine months ended fiscal 2004.

We are also exposed to foreign currency exchange risk related to our international operations as well as our U.S. businesses, which import or export goods. We have made limited use of financial instruments to manage this risk and have no such instruments outstanding as of June 30, 2004. A hypothetical unfavorable movement of 10% across each of the foreign exchange rates that we have exposure would have decreased our estimated income from continuing operations by approximately $3.6 million in fiscal 2003. This calculation assumes that each exchange rate would change in the same direction relative to the U.S. dollar. In addition to the direct effect of changes in exchange rates, which are a changed dollar value of the resulting sales, changes in exchange rates also affect the volume of sales or the foreign currency sales price as competitors products become more or less attractive. Our sensitivity analysis of the effects of changes in foreign currency exchange rates does not factor in a potential change in sales levels or local currency prices.

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Item 4. Controls and Procedures

We carried out an evaluation under the supervision and with the participation of our management, including the Chief Executive Officer and the Chief Financial Officer of the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective for recording, processing and summarizing the information we are required to disclose in the reports we file under the Securities Exchange Act of 1934, within the time periods specified in the SEC s rules, regulations and forms. Our management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures, which by their nature can provide only reasonable assurance regarding management s control objectives.

There has been no change in our internal control over financial reporting during our last quarter, identified in connection with the evaluation referred to above, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

See **Note 6** to our Condensed Consolidated Financial Statements.

Item 6. Exhibits and Reports on Form 8-K

(a)

10.1 Second Amendment to Loan and Security Agreement among Jacuzzi Brands, Inc., the other borrowers named on the signature pages thereto, Fleet Capital Corporation, Silver Point Finance LLC, the Revolving Credit Lenders named therein, and the Term Loan B Lenders named therein dated June 30, 2004.

31.1 Certification of principal executive officer required by Rule 13a-14(a) of the Exchange Act.

31.2 Certification of principal financial officer required by Rule 13a-14(a) of the Exchange Act.

32.1 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) A Current Report on Form 8-K was furnished May 18, 2004, responsive to Item 12 regarding our financial results for the second quarter of fiscal 2004.

A Current Report on Form 8-K was filed July 12, 2004, responsive to Item 5 to announce the terms of an amendment to our credit facility.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

JACUZZI BRANDS, INC.

Date: August 12, 2004

By: /s/ Jeffrey B. Park

Jeffrey B. Park
Senior Vice President,
Chief Financial Officer and Treasurer (Principal Financial Officer)

/s/ Francisco V. Puñal

Francisco V. Puñal
Vice President and Controller
(Principal Accounting Officer)

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Other assets

178,550 225,064 800,818 (438,493) 765,939

Total Assets

$(8,089,600) $ 11,858,820 $ 13,131,280 $ 7,974,975 $ (7,415,093) $ 17,460,382

Accounts payable and accrued expenses

$(941) $63,888 $400,449 $646,093 $(31,423) $1,078,066

Intercompany payable(1)

6,939,391 53,162 (6,992,553)

Current portion of long-term debt

826,059 41,676 867,735

Deferred income

49,423 103,355 152,778

Total Current Liabilities

	(941)	889,947	7,389,263	844,286	(7,023,976)	2,098,579
Long-term debt		18,172,562	4,000	2,522,133	(959,078)	19,739,617
Long-term intercompany payable		383,778			(383,778)	
Intercompany long-term debt			212,000		(212,000)	
Deferred income taxes	(12,665)	269,578	927,685	865,598		2,050,196
Other long-term liabilities		263,208	261,434	252,034		776,676
Total member s interest (deficit)	(8,075,994)	(8,120,253)	4,336,898	3,490,924	1,163,739	(7,204,686)
Total Liabilities and Member s Interest (Deficit)	$ (8,089,600)	$11,858,820	$13,131,280	$7,974,975	$(7,415,093)	$17,460,382

(1) The intercompany payable balance includes approximately $7.3 billion of designated amounts of borrowings under the senior secured credit facilities by certain Guarantor Subsidiaries that are Co-Borrowers and primary obligors thereunder with respect to these amounts. These amounts were incurred by the Co-Borrowers at the time of the closing of the merger, but were funded and will be repaid through accounts of the Subsidiary Issuer. The intercompany receivables balance includes the amount of such borrowings, which are required to be repaid to the lenders under the senior secured credit facilities by the Guarantor Subsidiaries as Co-Borrowers and primary obligors thereunder.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

	Three Months Ended March 31, 2011					
(In thousands)	Parent Company	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenue	$	$	$ 668,528	$ 657,075	$ (4,777)	$ 1,320,826
Operating expenses:						
Direct operating expenses			207,645	392,444	(3,834)	596,255
Selling, general and administrative expenses			231,261	130,206	(943)	360,524
Corporate expenses	2,659		27,705	21,983		52,347
Depreciation and amortization			80,808	102,903		183,711
Other operating income net			11,912	4,802		16,714
Operating income (loss)	(2,659)		133,021	14,341		144,703
Interest expense net	7	344,939	(1,277)	(50)	26,047	369,666
Equity in earnings (loss) of nonconsolidated affiliates	(104,094)	111,770	(6,946)	2,960	(715)	2,975
Other income (expense) net		(5,721)	(206)	3,891		(2,036)
Income (loss) before income taxes	(106,760)	(238,890)	127,146	21,242	(26,762)	(224,024)
Income tax benefit (expense)	975	134,796	(45,153)	2,043		92,661
Consolidated net income (loss)	(105,785)	(104,094)	81,993	23,285	(26,762)	(131,363)
Less amount attributable to noncontrolling interest			1,320	(851)		469
Net income (loss) attributable to the Company	$ (105,785)	$ (104,094)	$ 80,673	$ 24,136	$ (26,762)	$ (131,832)
Other comprehensive income (loss), net of tax:						
Foreign currency translation adjustments			(279)	39,586		39,307
Unrealized gain (loss) on securities and derivatives:						
Unrealized holding gain on marketable securities			483	2,469		2,952
Unrealized holding gain on cash flow derivatives		13,342				13,342
Reclassification adjustment				89		89
Equity in subsidiary comprehensive income (loss)	48,992	35,650	39,842		(124,484)	
Comprehensive income (loss)	(56,793)	(55,102)	120,719	66,280	(151,246)	(76,142)
Less amount attributable to noncontrolling interest			4,396	2,302		6,698
Comprehensive income (loss) attributable to the Company	$ (56,793)	$ (55,102)	$ 116,323	$ 63,978	$ (151,246)	$ (82,840)

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

	Three Months Ended March 31, 2010					
(In thousands)	Parent Company	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Revenue	$	$	$ 649,811	$ 615,284	$ (1,317)	$ 1,263,778
Operating expenses:						
Direct operating expenses			217,521	380,086	(260)	597,347
Selling, general and administrative expenses			234,648	115,705	(1,057)	349,296
Corporate expenses	3,008	3	40,713	20,772		64,496
Depreciation and amortization			79,248	102,086		181,334
Other operating income net			2,754	1,018		3,772
Operating income (loss)	(3,008)	(3)	80,435	(2,347)		75,077
Interest expense net	4	351,618	5,324	14,653	14,196	385,795
Equity in earnings (loss) of nonconsolidated affiliates	(219,600)	481	(46,285)	1,880	265,395	1,871
Other income (expense) net			(598)	(1,656)	60,289	58,035
Income (loss) before income taxes	(222,612)	(351,140)	28,228	(16,776)	311,488	(250,812)
Income tax benefit (expense)	1,105	131,540	(56,106)	(5,354)		71,185
Consolidated net income (loss)	(221,507)	(219,600)	(27,878)	(22,130)	311,488	(179,627)
Less amount attributable to noncontrolling interest			(3,216)	(997)		(4,213)
Net income (loss) attributable to the Company	$ (221,507)	$ (219,600)	$ (24,662)	$ (21,133)	$ 311,488	$ (175,414)
Other comprehensive income (loss), net of tax:						
Foreign currency translation adjustments			(523)	(38,926)		(39,449)
Unrealized gain (loss) on securities and derivatives:						
Unrealized holding gain (loss) on marketable securities			6,565	(2,620)		3,945
Unrealized holding loss on cash flow derivatives		(3,154)				(3,154)
Reclassification adjustment				225		225
Equity in subsidiary comprehensive income (loss)	(33,765)	(30,610)	(41,478)		105,853	
Comprehensive income (loss)	(255,272)	(253,364)	(60,098)	(62,454)	417,341	(213,847)
Less amount attributable to noncontrolling interest			(4,826)	158		(4,668)
Comprehensive income (loss) attributable to the Company	$ (255,272)	$ (253,364)	$ (55,272)	$ (62,612)	$ 417,341	$ (209,179)

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

	Three Months Ended March 31, 2011					
(In thousands)	Parent Company	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Cash flows from operating activities:						
Consolidated net income (loss)	$ (105,785)	$ (104,094)	$ 81,993	$ 23,285	$ (26,762)	$ (131,363)
Reconciling items:						
Depreciation and amortization			80,808	102,903		183,711
Deferred taxes	(449)	(78,315)	38,082	(19,984)		(60,666)
Gain on disposal of operating assets			(11,912)	(4,802)		(16,714)
Loss on extinguishment of debt		5,721				5,721
Provision for doubtful accounts			2,368	2,349		4,717
Share-based compensation			(765)	3,056		2,291
Equity in (earnings) loss of nonconsolidated affiliates	104,094	(111,770)	6,946	(2,960)	715	(2,975)
Amortization of deferred financing charges, bond premiums and accretion of note discounts, net		66,979	(1,421)	(34,747)	26,047	56,858
Other reconciling items net			(28)	4,972		4,944
Changes in operating assets and liabilities:						
Decrease in accounts receivable			87,632	39,837		127,469
Increase in deferred income			10,643	48,588		59,231
Decrease in accrued expenses			(100,416)	(59,966)		(160,382)
Decrease in accounts payable and other liabilities		(5,743)	(54,694)	(4,897)		(65,334)
Increase (decrease) in accrued interest		(64,859)		696	18,480	(45,683)
Changes in other operating assets and liabilities, net of effects of acquisitions and dispositions	(1,763)	(7,635)	(16,206)	(43,050)	(18,480)	(87,134)
Net cash provided by (used for) operating activities	(3,903)	(299,716)	123,030	55,280		(125,309)
Cash flows from investing activities:						
Proceeds from maturity of Clear Channel notes				57,263	(57,263)	
Purchases of property, plant and equipment			(17,588)	(46,381)		(63,969)
Purchases of businesses and other operating assets			(537)	(10,689)		(11,226)
Proceeds from disposal of assets			37,563	4,765		42,328
Change in other net			2	97		99
Net cash provided by (used for) investing activities			19,440	5,055	(57,263)	(32,768)
Cash flows from financing activities:						
Draws on credit facilities		10,000				10,000
Payments on credit facilities		(135,449)		(1,851)		(137,300)
Intercompany funding	3,903	603,216	(600,569)	(6,550)		
Proceeds on long-term debt		1,000,000	1,604			1,001,604
Payments on long-term debt		(1,178,051)	(196)	(2,535)	57,263	(1,123,519)
Change in other net				(2,830)		(2,830)
Net cash provided by (used for) financing activities	3,903	299,716	(599,161)	(13,766)	57,263	(252,045)
			(456,691)	46,569		(410,122)

Net increase (decrease) in cash and cash equivalents													
Cash and cash equivalents at beginning of period					1		1,220,362		700,563				1,920,926
Cash and cash equivalents at end of period	$		$		1	$	763,671	$	747,132	$		$	1,510,804

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

	Three Months Ended March 31, 2010					
(In thousands)	Parent Company	Subsidiary Issuer	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Cash flows from operating activities:						
Consolidated net income (loss)	$ (221,507)	$ (219,600)	$ (27,878)	$ (22,130)	$ 311,488	$ (179,627)
Reconciling items:						
Depreciation and amortization			79,248	102,086		181,334
Deferred taxes	252	9,096	(72,881)	(20,309)		(83,842)
Gain on disposal of operating assets			(2,754)	(1,018)		(3,772)
Gain on extinguishment of debt					(60,289)	(60,289)
Provision for doubtful accounts			2,454	464		2,918
Share-based compensation			5,468	2,647		8,115
Equity in (earnings) loss of nonconsolidated affiliates	219,600	(481)	46,285	(1,880)	(265,395)	(1,871)
Amortization of deferred financing charges, bond premiums and accretion of note discounts, net		61,271	1,820	(24,583)	14,196	52,704
Other reconciling items net			(243)	3,298		3,055
Changes in operating assets and liabilities:						
Decrease in accounts receivable			57,646	31,724		89,370
Increase in deferred income			7,730	41,950		49,680
Increase (decrease) in accrued expenses		(25)	5,435	(4,811)		599
Increase (decrease) in accounts payable and other liabilities		686	3,918	(4,406)		198
Increase (decrease) in accrued interest		(9,470)	(926)	437		(9,959)
Changes in other operating assets and liabilities, net of effects of acquisitions and dispositions	751	252,643	(282,364)	10,592		(18,378)
Net cash provided by (used for) operating activities	(904)	94,120	(177,042)	114,061		30,235
Cash flows from investing activities:						
Proceeds from maturity of Clear Channel notes				10,025	(10,025)	
Investment in Clear Channel notes			(125,000)		125,000	
Purchases of property, plant and equipment			(5,975)	(49,349)		(55,324)
Purchases of businesses and other operating assets			(10,389)			(10,389)
Proceeds from disposal of assets			6,330	1,810		8,140
Change in other net		(93)	(3,551)	(10,443)		(14,087)
Net cash provided by (used for) investing activities		(93)	(138,585)	(47,957)	114,975	(71,660)
Cash flows from financing activities:						
Draws on credit facilities		75,000		304		75,304
Payments on credit facilities		(37,000)		(29,706)		(66,706)
Intercompany funding	904	117,973	(89,951)	(28,926)		
Payments on long-term debt		(250,000)	(2)	(4,132)	10,025	(244,109)
Repurchases of long-term debt					(125,000)	(125,000)
Change in other net				233		233
Net cash provided by (used for) financing activities	904	(94,027)	(89,953)	(62,227)	(114,975)	(360,278)
Net increase (decrease) in cash and cash equivalents			(405,580)	3,877		(401,703)
Cash and cash equivalents at beginning of period			1,258,993	625,001		1,883,994

Cash and cash equivalents at end of period	$	$	$ 853,413	$ 628,878	$	$ 1,482,291

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

Note 11: SUBSEQUENT EVENT

On April 29, 2011, Clear Channel Acquisition, LLC, our wholly-owned subsidiary, purchased the traffic business of Westwood One, Inc. (Westwood One) for $24.25 million through the acquisition of the stock of certain wholly-owned subsidiaries of Westwood One to increase the growth of our traffic business by adding a complementary traffic operation and to improve the Company s traffic operations. In addition, after closing, the acquired subsidiaries repaid pre-existing, intercompany debt owed by the subsidiaries to Westwood One in the amount of $95.0 million. Clear Channel Acquisition, LLC, simultaneously entered into a Transition Services Agreement by which it will provide certain services to Westwood One.

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Members

Clear Channel Capital I, LLC

We have audited the accompanying consolidated balance sheets of Clear Channel Capital I, LLC (Clear Channel Capital) as of December 31, 2010 and 2009, the related consolidated statements of operations, member s (deficit)/shareholders equity, and cash flows of Clear Channel Capital for the years ended December 31, 2010 and 2009 and for the period from July 31, 2008 through December 31, 2008, and the related consolidated statement of operations, shareholders equity, and cash flows of Clear Channel Communications, Inc. (Clear Channel) for the period from January 1, 2008 through July 30, 2008. Our audits also included the financial statement schedule listed in the index to Clear Channel s 2010 Annual Report on Form 10-K as Item 15(a)2. These financial statements and schedule are the responsibility of Clear Channel Capital s management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Clear Channel Capital at December 31, 2010 and 2009, the consolidated results of Clear Channel Capital s operations and cash flows for the years ended December 31, 2010 and 2009 and for the period from July 31, 2008 through December 31, 2008, and the consolidated results of Clear Channel s operations and cash flows for the period from January 1, 2008 through July 30, 2008, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Clear Channel Capital s internal control over financial reporting as of December 31, 2010, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 14, 2011 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

San Antonio, Texas

February 14, 2011

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CONSOLIDATED BALANCE SHEETS OF CLEAR CHANNEL

CAPITAL I, LLC

(In thousands)

	December 31, 2010	December 31, 2009
CURRENT ASSETS		
Cash and cash equivalents	$ 1,920,926	$ 1,883,994
Accounts receivable, net of allowance of $74,660 in 2010 and $71,650 in 2009	1,393,365	1,301,700
Prepaid expenses	124,114	132,118
Other current assets	184,253	341,033
Total Current Assets	3,622,658	3,658,845
PROPERTY, PLANT AND EQUIPMENT		
Structures, net	2,007,399	2,143,972
Other property, plant and equipment, net	1,138,155	1,188,421
INTANGIBLE ASSETS		
Definite-lived intangibles, net	2,288,149	2,599,244
Indefinite-lived intangibles licenses	2,423,828	2,429,839
Indefinite-lived intangibles permits	1,114,413	1,132,218
Goodwill	4,119,326	4,125,005
OTHER ASSETS		
Other assets	765,939	769,557
Total Assets	$ 17,479,867	$ 18,047,101
CURRENT LIABILITIES		
Accounts payable	$ 127,263	$ 132,193
Accrued expenses	849,089	726,311
Accrued interest	121,199	137,236
Current portion of long-term debt	867,735	398,779
Deferred income	152,778	149,617
Total Current Liabilities	2,118,064	1,544,136
Long-term debt	19,739,617	20,303,126
Deferred income taxes	2,050,196	2,220,023
Other long-term liabilities	776,676	824,554
Commitments and contingent liabilities (Note 10)		
MEMBER S DEFICIT		
Noncontrolling interest	490,920	455,648
Member s interest	2,128,383	2,109,007
Retained deficit	(9,555,173)	(9,076,084)
Accumulated other comprehensive loss	(268,816)	(333,309)
Total Member s Deficit	(7,204,686)	(6,844,738)

Total Liabilities and Member s Deficit	$	17,479,867	$	18,047,101

See Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS OF OPERATIONS OF CLEAR CHANNEL

CAPITAL I, LLC

(In thousands, except per share data)	Post-Merger Year Ended December 31, 2010	Year Ended December 31, 2009	Period from July 31 through December 31, 2008	Pre-Merger Period from January 1 through July 30, 2008
Revenue	$ 5,865,685	$ 5,551,909	$ 2,736,941	$ 3,951,742
Operating expenses:				
Direct operating expenses (excludes depreciation and amortization)	2,442,167	2,583,263	1,198,345	1,706,099
Selling, general and administrative expenses (excludes depreciation and amortization)	1,509,692	1,466,593	806,787	1,022,459
Corporate expenses (excludes depreciation and amortization)	284,042	253,964	102,276	125,669
Depreciation and amortization	732,869	765,474	348,041	348,789
Merger expenses			68,085	87,684
Impairment charges	15,364	4,118,924	5,268,858	
Other operating income (expense) net	(16,710)	(50,837)	13,205	14,827
Operating income (loss)	864,841	(3,687,146)	(5,042,246)	675,869
Interest expense	1,533,341	1,500,866	715,768	213,210
Gain (loss) on marketable securities	(6,490)	(13,371)	(116,552)	34,262
Equity in earnings (loss) of nonconsolidated affiliates	5,702	(20,689)	5,804	94,215
Other income (expense) net	46,455	679,716	131,505	(5,112)
Income (loss) before income taxes and discontinued operations	(622,833)	(4,542,356)	(5,737,257)	586,024
Income tax benefit (expense)	159,980	493,320	696,623	(172,583)
Income (loss) before discontinued operations	(462,853)	(4,049,036)	(5,040,634)	413,441
Income (loss) from discontinued operations, net			(1,845)	640,236
Consolidated net income (loss)	(462,853)	(4,049,036)	(5,042,479)	1,053,677
Less amount attributable to noncontrolling interest	16,236	(14,950)	(481)	17,152
Net income (loss) attributable to the Company	$ (479,089)	$ (4,034,086)	$ (5,041,998)	$ 1,036,525
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	26,301	151,422	(382,760)	46,679
Unrealized gain (loss) on securities and derivatives:				
Unrealized holding gain (loss) on marketable securities	17,187	1,678	(95,669)	(52,460)
Unrealized holding gain (loss) on cash flow derivatives	15,112	(74,100)	(75,079)	
Reclassification adjustment for realized (gain) loss on securities and derivatives included in net income	14,750	10,008	102,766	(29,791)
Comprehensive income (loss)	(405,739)	(3,945,078)	(5,492,740)	1,000,953
Less amount attributable to noncontrolling interest	8,857	20,788	(49,212)	19,210
Comprehensive income (loss) attributable to the Company	$ (414,596)	$ (3,965,866)	$ (5,443,528)	$ 981,743
Net income (loss) per common share:				
Basic:				
Income (loss) attributable to the Company before discontinued operations				$ 0.80
Discontinued operations				1.29

Net income (loss) attributable to the Company	$	2.09
Weighted average common shares outstanding		495,044
Diluted:		
Income (loss) attributable to the Company before discontinued operations	$	0.80
Discontinued operations		1.29
Net income (loss) attributable to the Company	$	2.09
Weighted average common shares outstanding		496,519

See Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS OF CHANGES IN MEMBER S (DEFICIT)/SHAREHOLDERS EQUITY

(In thousands, except share data)			Controlling Interest					
	Common Shares Issued	Noncontrolling Interest	Common Stock	Additional Paid-in Capital/ Member s Interest	Retained Deficit	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
Pre-merger Balances at December 31, 2007	**498,075,417**	**$ 464,551**	**$ 49,808**	**$ 26,858,079**	**$ (18,489,143)**	**$ 355,507**	**$ (4,951)**	**$ 9,233,851**
Net income		17,152			1,036,525			1,053,677
Exercise of stock options and other	82,645		30	4,963			(2,024)	2,969
Amortization of deferred compensation		10,767		57,855				68,622
Other		(39,813)				33,383		(6,430)
Comprehensive income:								
Currency translation adjustment		22,367				24,312		46,679
Unrealized loss on investments		(3,125)				(49,335)		(52,460)
Reclassification adjustments		(32)				(29,759)		(29,791)
Pre-merger Balances at July 30, 2008	**498,158,062**	**471,867**	**49,838**	**26,920,897**	**(17,452,618)**	**334,108**	**(6,975)**	**10,317,117**
Elimination of pre-merger equity	(498,158,062)	(471,867)	(49,838)	(26,920,897)	17,452,618	(334,108)	6,975	(10,317,117)
Post-merger Balances at July 31, 2008		**471,867**		**2,089,347**				**2,561,214**
Net loss		(481)			(5,041,998)			(5,042,479)
Amortization of deferred compensation		4,182		11,729				15,911
Other		(136)				1		(135)
Comprehensive income:								
Currency translation adjustment		(50,010)				(332,750)		(382,760)
Unrealized loss on cash flow derivatives						(75,079)		(75,079)
Unrealized loss on investments		(6,856)				(88,813)		(95,669)
Reclassification adjustments		7,654				95,112		102,766
Post-merger Balances at December 31, 2008		**426,220**		**2,101,076**	**(5,041,998)**	**(401,529)**		**(2,916,231)**
Net loss		(14,950)			(4,034,086)			(4,049,036)
Issuance (forfeiture) of restricted stock				(180)				(180)
Amortization of deferred compensation		12,104		27,682				39,786
Other		11,486		(19,571)				(8,085)
Comprehensive income:								
Currency translation adjustment		21,201				130,221		151,422
Unrealized loss on cash flow derivatives						(74,100)		(74,100)
Unrealized gain (loss) on investments		(1,140)				2,818		1,678
Reclassification adjustments		727				9,281		10,008
Post-merger Balances at December 31, 2009		**$ 455,648**	**$**	**$ 2,109,007**	**$ (9,076,084)**	**$ (333,309)**	**$**	**$ (6,844,738)**
Net income (loss)		16,236			(479,089)			(462,853)
Issuance (forfeiture) of restricted stock		792		(1,908)				(1,116)
Amortization of deferred compensation		12,046		22,200				34,246
Other		(2,659)		(916)				(3,575)
Comprehensive income:								
Currency translation adjustment		7,360				18,941		26,301
Unrealized gain on cash flow derivatives						15,112		15,112
Unrealized gain (loss) on investments		(896)				18,083		17,187
Reclassification adjustments		2,393				12,357		14,750
Post-merger Balances at December 31, 2010		**$ 490,920**	**$**	**$ 2,128,383**	**$ (9,555,173)**	**$ (268,816)**	**$**	**$ (7,204,686)**

See Notes to Consolidated Financial Statements

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CONSOLIDATED STATEMENTS OF CASH FLOWS OF CLEAR CHANNEL

CAPITAL I, LLC

	Post-Merger			Pre-Merger
(In thousands)	Year Ended December 31, 2010	Year Ended December 31, 2009	Period from July 31 through December 31, 2008	Period from January 1 through July 30, 2008
CASH FLOWS FROM OPERATING ACTIVITIES:				
Consolidated net income (loss)	$ (462,853)	$ (4,049,036)	$ (5,042,479)	$ 1,053,677
Less: Income (loss) from discontinued operations, net			(1,845)	640,236
Net income (loss) from continuing operations	(462,853)	(4,049,036)	(5,040,634)	413,441
Reconciling Items:				
Impairment charges	15,364	4,118,924	5,268,858	
Depreciation and amortization	732,869	765,474	348,041	348,789
Deferred taxes	(211,180)	(417,191)	(619,894)	145,303
Provision for doubtful accounts	23,118	52,498	54,603	23,216
Amortization of deferred financing charges and note discounts, net	214,950	229,464	102,859	3,530
Share-based compensation	34,246	39,786	15,911	62,723
(Gain) loss on disposal of operating and fixed assets	16,710	50,837	(13,205)	(14,827)
(Gain) loss on securities	6,490	13,371	116,552	(36,758)
Equity in loss (earnings) of nonconsolidated affiliates	(5,702)	20,689	(5,804)	(94,215)
(Gain) loss on extinguishment of debt	(60,289)	(713,034)	(116,677)	13,484
Other reconciling items, net	26,090	46,166	12,089	11,629
Changes in operating assets and liabilities, net of effects of acquisitions and dispositions:				
Decrease (increase) in accounts receivable	(119,860)	99,225	158,142	24,529
Decrease in Federal income taxes receivable	132,309	75,939		
Increase (decrease) in accounts payable, accrued expenses and other liabilities	110,508	(27,934)	(130,172)	190,834
Increase (decrease) in accrued interest	87,053	33,047	98,909	(16,572)
Increase (decrease) in deferred income	796	2,168	(54,938)	51,200
Changes in other operating assets and liabilities, net of effects of acquisitions and dispositions	41,754	(159,218)	51,386	(91,048)
Net cash provided by operating activities	582,373	181,175	246,026	1,035,258
CASH FLOWS FROM INVESTING ACTIVITIES:				
Proceeds from sale of other investments	1,200	41,627		173,467
Purchases of property, plant and equipment	(241,464)	(223,792)	(190,253)	(240,202)
Proceeds from disposal of assets	28,637	48,818	16,955	72,806
Acquisition of operating assets	(16,110)	(8,300)	(23,228)	(153,836)
Cash used to purchase equity			(17,472,459)	
Change in other net	(12,460)	(102)	(42,718)	(268,486)
Net cash used for investing activities	(240,197)	(141,749)	(17,711,703)	(416,251)
CASH FLOWS FROM FINANCING ACTIVITIES:				
Draws on credit facilities	198,670	1,708,625	180,000	692,614
Payments on credit facilities	(152,595)	(202,241)	(128,551)	(872,901)
Proceeds from long-term debt	145,639	500,000	557,520	5,476
Proceeds from issuance of subsidiary senior notes		2,500,000		
Payments on long-term debt	(369,372)	(472,419)	(554,664)	(1,282,348)
Payments on senior secured credit facilities		(2,000,000)		
Repurchases of long-term debt	(125,000)	(343,466)	(24,425)	
Deferred financing charges		(60,330)		
Debt proceeds used to finance the merger			15,382,076	
Equity contribution used to finance the merger			2,142,830	
Dividends paid				(93,367)
Change in other net	(2,586)	(25,447)	(47)	(96,415)

Net cash provided by (used for) financing activities	(305,244)	1,604,722	17,554,739	(1,646,941)
CASH FLOWS FROM DISCONTINUED OPERATIONS:				
Net cash provided by (used for) operating activities			2,429	(67,751)
Net cash provided by investing activities				1,098,892
Net cash provided by financing activities				
Net cash provided by discontinued operations			2,429	1,031,141
Net increase in cash and cash equivalents	36,932	1,644,148	91,491	3,207
Cash and cash equivalents at beginning of period	1,883,994	239,846	148,355	145,148
Cash and cash equivalents at end of period	$ 1,920,926	$ 1,883,994	$ 239,846	$ 148,355
SUPPLEMENTAL DISCLOSURES:				
Cash paid during the year for:				
Interest	$ 1,235,755	$ 1,240,322	$ 527,083	$ 231,163
Income taxes			37,029	138,187

See Notes to Consolidated Financial Statements

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS OF CLEAR CHANNEL CAPITAL I, LLC

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As permitted by the rules and regulations of the Securities and Exchange Commission (the SEC), the financial statements and related footnotes included in Item 8 of Part II of this Annual Report on Form 10-K are those of Clear Channel Capital I, LLC (the Company or the Parent Company), the direct parent of Clear Channel Communications, Inc., a Texas corporation (Clear Channel or Subsidiary Issuer), and contain certain footnote disclosures regarding the financial information of Clear Channel and Clear Channel s domestic wholly-owned subsidiaries that guarantee certain of Clear Channel s outstanding indebtedness.

Nature of Business

The Company is a limited liability company organized under Delaware law, with all of its interests being held by Clear Channel Capital II, LLC, a direct, wholly owned subsidiary of CC Media Holdings, Inc. (CCMH). CCMH was formed in May 2007 by private equity funds sponsored by Bain Capital Partners, LLC and Thomas H. Lee Partners, L.P. (together, the Sponsors) for the purpose of acquiring the business of Clear Channel. The acquisition was completed on July 30, 2008 pursuant to the Agreement and Plan of Merger, dated November 16, 2006, as amended on April 18, 2007, May 17, 2007 and May 13, 2008 (the Merger Agreement).

Clear Channel is a wholly-owned subsidiary of the Company. Upon the consummation of the merger, CCMH became a public company and Clear Channel was no longer a public company. Prior to the acquisition, the Company had not conducted any activities, other than activities incident to its formation and in connection with the acquisition, and did not have any assets or liabilities, other than as related to the acquisition. Subsequent to the acquisition, Clear Channel became a direct, wholly-owned subsidiary of the Company and the business of the Company became that of Clear Channel and its subsidiaries. As a result, all of the operations of the Company are conducted by Clear Channel.

Format of Presentation

The accompanying consolidated statements of operations, statements of cash flows and shareholders equity are presented for the post-merger and pre-merger periods. The merger resulted in a new basis of accounting beginning on July 31, 2008 and the financial reporting periods are presented as follows:

The years ended December 31, 2010 and 2009, and the period from July 31 through December 31, 2008 reflect the post-merger period of the Company, including the merger of a wholly-owned subsidiary of CCMH with and into Clear Channel. Subsequent to the acquisition, Clear Channel became a direct, wholly-owned subsidiary of the Company and the business of the Company became that of Clear Channel and its subsidiaries.

The period from January 1 through July 30, 2008 reflects the pre-merger period of Clear Channel. The consolidated financial statements for the pre-merger period were prepared using the historical basis of accounting for Clear Channel. As a result of the merger and the associated purchase accounting, the consolidated financial statements of the post-merger periods are not comparable to periods preceding the merger.

CCMH Purchase Accounting Adjustments

Purchase accounting adjustments, including goodwill, are reflected in the financial statements of the Company and its subsidiaries.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Omission of Per Share Information for the Post-Merger Period

Net loss per share information is not presented for the post-merger period as such information is not meaningful. During the post-merger periods ended December 31, 2010, 2009 and 2008, Clear Channel Capital II, LLC is the sole member of the Company and owns 100% of the limited liability company interests. The Company does not have any publicly traded common stock or potential common stock.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts have been eliminated in consolidation. Investments in companies in which the Company owns 20 percent to 50 percent of the voting common stock or otherwise exercises significant influence over operating and financial policies of the company are accounted for using the equity method of accounting.

Certain prior period amounts have been reclassified to conform to the 2010 presentation.

The Company owns certain radio stations which, under current FCC rules, are not permitted or transferable. These radio stations were placed in a trust in order to comply with FCC rules at the time of the closing of the merger that resulted in the Company s acquisition of Clear Channel. The Company is the beneficial owner of the trust, but the radio stations are managed by an independent trustee. The Company will have to divest all of these radio stations unless any stations may be owned by the Company under then-current FCC rules, in which case the trust will be terminated with respect to such stations. The trust agreement stipulates that the Company must fund any operating shortfalls of the trust activities, and any excess cash flow generated by the trust is distributed to the Company. The Company is also the beneficiary of proceeds from the sale of stations held in the trust. The Company consolidates the trust in accordance with ASC 810-10, which requires an enterprise involved with variable interest entities to perform an analysis to determine whether the enterprise s variable interest or interests give it a controlling financial interest in the variable interest entity, as the trust was determined to be a variable interest entity and the Company is its primary beneficiary.

Cash and Cash Equivalents

Cash and cash equivalents include all highly liquid investments with an original maturity of three months or less.

Allowance for Doubtful Accounts

The Company evaluates the collectability of its accounts receivable based on a combination of factors. In circumstances where it is aware of a specific customer s inability to meet its financial obligations, it records a specific reserve to reduce the amounts recorded to what it believes will be collected. For all other customers, it recognizes reserves for bad debt based on historical experience of bad debts as a percent of revenue for each business unit, adjusted for relative improvements or deteriorations in the agings and changes in current economic conditions. The Company believes its concentration of credit risk is limited due to the large number and the geographic diversification of its customers.

Land Leases and Other Structure Licenses

Most of the Company s outdoor advertising structures are located on leased land. Americas outdoor land rents are typically paid in advance for periods ranging from one to 12 months. International outdoor land rents are paid both in advance and in arrears, for periods ranging from one to 12 months. Most international street furniture display faces are operated through contracts with municipalities for up to 20 years. The leased land and street furniture contracts often include a percent of revenue to be paid along with a base rent payment. Prepaid land leases are recorded as an asset and expensed ratably over the related rental term and license and rent payments in arrears are recorded as an accrued liability.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Purchase Accounting

The Company accounts for its business combinations under the acquisition method of accounting. The total cost of an acquisition is allocated to the underlying identifiable net assets, based on their respective estimated fair values. The excess of the purchase price over the estimated fair values of the net assets acquired is recorded as goodwill. Determining the fair value of assets acquired and liabilities assumed requires management s judgment and often involves the use of significant estimates and assumptions, including assumptions with respect to future cash inflows and outflows, discount rates, asset lives and market multiples, among other items. Various acquisition agreements may include contingent purchase consideration based on performance requirements of the investee. The Company accounts for these payments in conformity with the provisions of ASC 805-20-30, which establish the requirements related to recognition of certain assets and liabilities arising from contingencies.

Property, Plant and Equipment

Property, plant and equipment are stated at cost. Depreciation is computed using the straight-line method at rates that, in the opinion of management, are adequate to allocate the cost of such assets over their estimated useful lives, which are as follows:

Buildings and improvements - 10 to 39 years

Structures - 5 to 40 years

Towers, transmitters and studio equipment - 7 to 20 years

Furniture and other equipment - 3 to 20 years

Leasehold improvements - shorter of economic life or lease term assuming renewal periods, if appropriate

For assets associated with a lease or contract, the assets are depreciated at the shorter of the economic life or the lease or contract term, assuming renewal periods, if appropriate. Expenditures for maintenance and repairs are charged to operations as incurred, whereas expenditures for renewal and betterments are capitalized.

The Company tests for possible impairment of property, plant, and equipment whenever events and circumstances indicate that depreciable assets might be impaired and the undiscounted cash flows estimated to be generated by those assets are less than the carrying amounts of those assets. When specific assets are determined to be unrecoverable, the cost basis of the asset is reduced to reflect the current fair market value.

The Company impaired outdoor advertising structures in its Americas outdoor segment by $4.0 million during 2010.

During 2009, the Company recorded a $21.0 million impairment to street furniture tangible assets in its International outdoor segment and an $11.3 million impairment of corporate assets.

Intangible Assets

The Company classifies intangible assets as definite-lived, indefinite-lived or goodwill. Definite-lived intangibles include primarily transit and street furniture contracts, talent and representation contracts, customer and advertiser relationships, and site-leases, all of which are amortized over the respective lives of the agreements, or over the period of time the assets are expected to contribute directly or indirectly to the Company s future cash flows. The Company periodically reviews the appropriateness of the amortization periods related to its definite-lived assets. These assets are recorded at cost.

The Company tests for possible impairment of definite-lived intangible assets whenever events and circumstances indicate that amortizable long-lived assets might be impaired and the undiscounted cash flows

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

estimated to be generated by those assets are less than the carrying amounts of those assets. When specific assets are determined to be unrecoverable, the cost basis of the asset is reduced to reflect the current fair market value.

The Company impaired certain definite-lived intangible assets primarily related to a talent contract in its Radio broadcasting segment by $3.9 million during 2010.

The Company impaired definite-lived intangible assets related to certain street furniture and billboard contract intangible assets in its Americas outdoor and International outdoor segments by $55.3 million during 2009.

The Company s indefinite-lived intangibles include Federal Communications Commission (FCC) broadcast licenses in its Radio broadcasting segment and billboard permits in its Americas outdoor advertising segment. The Company s indefinite-lived intangibles are not subject to amortization, but are tested for impairment at least annually. The Company tests for possible impairment of indefinite-lived intangible assets whenever events or changes in circumstances, such as a significant reduction in operating cash flow or a dramatic change in the manner for which the asset is intended to be used indicate that the carrying amount of the asset may not be recoverable.

The Company performs its annual impairment test for its FCC licenses and permits using a direct valuation technique as prescribed in ASC 805-20-S99. The Company engages Mesirow Financial Consulting LLC (Mesirow Financial), a third party valuation firm, to assist the Company in the development of these assumptions and the Company s determination of the fair value of its FCC licenses and permits.

The Company performed its annual impairment test on its indefinite-lived intangible assets on October 1, 2010, which resulted in a non-cash impairment charge of $5.3 million related to its indefinite-lived FCC licenses and permits. See Note 4 for further discussion.

The Company performed impairment tests during 2009 and 2008, which resulted in non-cash impairment charges of $935.6 million and $1.7 billion, respectively, on its indefinite-lived FCC licenses and permits. See Note 4 for further discussion.

At least annually, the Company performs its impairment test for each reporting unit s goodwill using a discounted cash flow model to determine if the carrying value of the reporting unit, including goodwill, is less than the fair value of the reporting unit. The Company identified its reporting units in accordance with ASC 350-20-55. The U.S. radio markets are aggregated into a single reporting unit and the U.S. outdoor advertising markets are aggregated into a single reporting unit for purposes of the goodwill impairment test. The Company also determined that within its Americas outdoor segment, Canada, Mexico, Peru, and Brazil constitute separate reporting units and each country in its International outdoor segment constitutes a separate reporting unit.

The Company performed its annual goodwill impairment test on October 1, 2010, and recognized a non-cash impairment charge of $2.1 million related to a specific reporting unit in its International outdoor segment. See Note 4 for further discussion.

The Company performed impairment tests during 2009 and 2008, and recognized non-cash impairment charges of $3.1 billion and $3.6 billion, respectively. See Note 4 for further discussion.

Nonconsolidated Affiliates

In general, investments in which the Company owns 20 percent to 50 percent of the common stock or otherwise exercises significant influence over the investee are accounted for under the equity method. The Company does not recognize gains or losses upon the issuance of securities by any of its equity method investees. The Company

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

reviews the value of equity method investments and records impairment charges in the statement of operations as a component of Equity in earnings (loss) of nonconsolidated affiliates for any decline in value that is determined to be other-than-temporary.

For the years ended December 31, 2010 and 2009, the Company recorded non-cash impairment charges of $8.3 million and $22.9 million, respectively, related to certain equity investments in its International outdoor segment.

Other Investments

Other investments are composed primarily of equity securities. These securities are classified as available-for-sale or trading and are carried at fair value based on quoted market prices. Securities are carried at historical value when quoted market prices are unavailable. The net unrealized gains or losses on the available-for-sale securities, net of tax, are reported in accumulated other comprehensive loss as a component of shareholders equity. In addition, the Company holds investments that do not have quoted market prices. The Company periodically assesses the value of available-for-sale and non-marketable securities and records impairment charges in the statement of operations for any decline in value that is determined to be other-than-temporary. The average cost method is used to compute the realized gains and losses on sales of equity securities.

The Company periodically assesses the value of its available-for-sale securities. Based on these assessments, the Company concluded that other-than-temporary impairments existed at December 31, 2010, September 30, 2009 and December 31, 2008, and recorded non-cash impairment charges of $6.5 million, $11.3 million and $116.6 million, respectively, during each of these years. Such charges are recorded on the statement of operations in Gain (loss) on marketable securities .

Financial Instruments

Due to their short maturity, the carrying amounts of accounts and notes receivable, accounts payable, accrued liabilities, and short-term borrowings approximated their fair values at December 31, 2010 and 2009.

Income Taxes

The Company accounts for income taxes using the liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting bases and tax bases of assets and liabilities and are measured using the enacted tax rates expected to apply to taxable income in the periods in which the deferred tax asset or liability is expected to be realized or settled. Deferred tax assets are reduced by valuation allowances if the Company believes it is more likely than not that some portion or the entire asset will not be realized. As all earnings from the Company s foreign operations are permanently reinvested and not distributed, the Company s income tax provision does not include additional U.S. taxes on foreign operations. It is not practical to determine the amount of Federal income taxes, if any, that might become due in the event that the earnings were distributed.

Revenue Recognition

Radio broadcasting revenue is recognized as advertisements or programs are broadcast and is generally billed monthly. Outdoor advertising contracts typically cover periods of a few weeks up to one year and are generally billed monthly. Revenue for outdoor advertising is recognized ratably over the term of the contract. Advertising revenue is reported net of agency commissions. Agency commissions are calculated based on a stated percentage applied to gross billing revenue for the Company s broadcasting and outdoor operations. Payments received in advance of being earned are recorded as deferred income.

Barter transactions represent the exchange of advertising spots or display space for merchandise or services. These transactions are generally recorded at the fair market value of the advertising spots or display space or the fair value of the merchandise or services received, whichever is most readily determinable. Revenue is

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

recognized on barter and trade transactions when the advertisements are broadcasted or displayed. Expenses are recorded ratably over a period that estimates when the merchandise or service received is utilized or the event occurs. Barter and trade revenues and expenses from continuing operations are included in consolidated revenue and selling, general and administrative expenses, respectively. Barter and trade revenues and expenses from continuing operations were:

(In millions)	Post-Merger			Pre-Merger
	Year ended December 31, 2010	Year ended December 31, 2009	Period from July 31 through December 31, 2008	Period from January 1 through July 30, 2008
Barter and trade revenues	$ 67.0	$ 71.9	$ 33.7	$ 40.2
Barter and trade expenses	66.4	86.7	35.0	38.9

Barter and trade expenses for 2009 include $14.9 million of trade receivables written off as it was determined they no longer had value to the Company.

Share-Based Compensation

Under the fair value recognition provisions of ASC 718-10, share-based compensation cost is measured at the grant date based on the fair value of the award. For awards that vest based on service conditions, this cost is recognized as expense on a straight-line basis over the vesting period. For awards that will vest based on market or performance conditions, this cost will be recognized when it becomes probable that the performance conditions will be satisfied. Determining the fair value of share-based awards at the grant date requires assumptions and judgments about expected volatility and forfeiture rates, among other factors. If actual results differ significantly from these estimates, the Company s results of operations could be materially impacted.

The Company does not have any equity incentive plans under which it grants stock awards to employees. Employees of subsidiaries of the Company receive equity awards from CCMH s equity incentive plans. Prior to the merger, Clear Channel granted equity awards to its employees under its own equity incentive plans.

Derivative Instruments and Hedging Activities

The provisions of ASC 815-10 require the Company to recognize its interest rate swap agreements as either assets or liabilities in the consolidated balance sheet at fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship, and further, on the type of hedging relationship. The interest rate swaps are designated and qualify as hedging instruments, and are characterized as cash flow hedges. The Company formally documents all relationships between hedging instruments and hedged items, as well as its risk management objectives and strategies for undertaking various hedge transactions. The Company formally assesses, both at inception and at least quarterly thereafter, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in either the fair value or cash flows of the hedged item. If a derivative ceases to be a highly effective hedge, the Company discontinues hedge accounting.

Foreign Currency

Results of operations for foreign subsidiaries and foreign equity investees are translated into U.S. dollars using the average exchange rates during the year. The assets and liabilities of those subsidiaries and investees are translated into U.S. dollars using the exchange rates at the balance sheet date. The related translation adjustments are recorded in a separate component of shareholders equity, Accumulated other comprehensive income (loss) . Foreign currency transaction gains and losses are included in operations.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Advertising Expense

The Company records advertising expense as it is incurred. Advertising expenses from continuing operations were $82.0 million, $67.3 million and $107.9 million for the post-merger years ended December 31, 2010 and 2009 and the combined period ended December 31, 2008, respectively.

Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates, judgments, and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes including, but not limited to, legal, tax and insurance accruals. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from those estimates.

New Accounting Pronouncements

In December 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2010-28, *When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts*. This ASU updates ASC Topic 350, *Intangibles Goodwill and Other,* to amend the criteria for performing Step 2 of the goodwill impairment test for reporting units with zero or negative carrying amounts and requires performing Step 2 if qualitative factors indicate that it is more likely than not that a goodwill impairment exists. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2010. The Company does not currently have any reporting units with zero or negative carrying values.

In August 2010, the FASB issued ASU No. 2010-22, *Accounting for Various Topics Technical Corrections to SEC Paragraphs*. This ASU amends various SEC paragraphs and became effective upon issuance. The adoption of ASU No. 2010-22 did not have a material impact on the Company s financial position or results of operations.

In August 2010, the FASB issued ASU No. 2010-21, *Accounting for Technical Amendments to Various SEC Rules and Schedules*. This ASU amends various SEC paragraphs pursuant to the issuance of Release No. 33-9026: Technical Amendments to Rules, Forms, Schedules and Codification of Financial Reporting Policies and became effective upon issuance. The Company adopted the provisions of ASU 2010-21 upon issuance with no material impact to the Company s financial position or results of operations.

In February 2010, the FASB issued ASU 2010-09, *Amendments to Certain Recognition and Disclosure Requirements*. ASU 2010-09 updates ASC Topic 855, *Subsequent Events*. ASU 2010-09 removes the requirement to disclose the date through which an entity has evaluated subsequent events. The Company adopted the provisions of ASU 2010-09 upon issuance with no material impact to the Company s financial position or results of operations.

In January 2010, the FASB issued ASU No. 2010-06, *Improving Disclosures about Fair Value Measurements*. This update amends ASC Topic 820, *Fair Value Measurements and Disclosures,* to require new disclosures for significant transfers in and out of Level 1 and Level 2 fair value measurements, disaggregation regarding classes of assets and liabilities, valuation techniques and inputs used to measure fair value for both recurring and nonrecurring fair value measurements for Level 2 or Level 3. These disclosures are effective for the interim and annual reporting periods beginning after December 15, 2009. Additional new disclosures regarding the purchases, sales, issuances and settlements in the roll forward of activity in Level 3 fair value measurements are effective for fiscal years beginning after December 15, 2010 beginning with the first interim period. The Company adopted certain of the relevant disclosure provisions of ASU 2010-06 on January 1, 2010 and adopted certain other provisions on January 1, 2011.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 2 BUSINESS ACQUISITIONS

2009 Purchases of Additional Equity Interests

During 2009, the Company s Americas outdoor segment purchased the remaining 15% interest in its consolidated subsidiary, Paneles Napsa S.A., for $13.0 million and the Company s International outdoor segment acquired an additional 5% interest in its consolidated subsidiary, Clear Channel Jolly Pubblicita SPA, for $12.1 million.

2008 Acquisitions

CCMH completed its acquisition of Clear Channel on July 30, 2008. The transaction was accounted for as a purchase in accordance with Statement of Financial Accounting Standards No. 141, *Business Combinations*, and Emerging Issues Task Force Issue 88-16, *Basis in Leveraged Buyout Transactions*. CCMH allocated a portion of the consideration paid to the assets and liabilities acquired at their respective fair values with the remaining portion recorded at the continuing shareholders basis. Excess consideration after this allocation was recorded as goodwill. The purchase price allocation was complete as of July 30, 2009 in accordance with ASC 805-10-25, which requires that the allocation period not exceed one year from the date of acquisition.

The Company also acquired assets in its operating segments in addition to the merger described above. The Company acquired FCC licenses in its radio segment for $11.7 million in cash during 2008. The Company acquired outdoor display faces and additional equity interests in international outdoor companies for $96.5 million in cash during 2008. The Company s national representation business acquired representation contracts for $68.9 million in cash during 2008.

NOTE 3 DISCONTINUED OPERATIONS

Sale of non-core radio stations and television business

Consistent with the provisions of ASC 360-10, the Company classified radio station assets as discontinued operations during 2008.

On March 14, 2008, Clear Channel completed the sale of its television business to Newport Television, LLC and recorded a gain of $662.9 million as a component of Income (loss) from discontinued operations, net in its consolidated statement of operations during the first quarter of 2008.

Summarized operating results for the year ended December 31, 2008 from these businesses classified as discontinued operations are as follows:

(In thousands)	Post-Merger Period from July 31 through December 31, 2008	Pre-Merger Period from January 1 through July 30, 2008
Revenue	$ 1,364	$ 74,783
Income (loss) before income taxes	$ (3,160)	$ 702,698

Included in income (loss) from discontinued operations, net is an income tax benefit of $1.3 million for the period July 31 through December 31, 2008. Included for the period from January 1 through July 30, 2008 is income tax expense of $62.4 million and a gain of $695.8 million related to the sale of Clear Channel s television business and certain radio stations.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 4 PROPERTY, PLANT AND EQUIPMENT, INTANGIBLE ASSETS AND GOODWILL

Property, Plant and Equipment

The Company s property, plant and equipment consisted of the following classes of assets at December 31, 2010 and 2009, respectively.

(In thousands)	December 31, 2010	December 31, 2009
Land, buildings and improvements	$ 652,575	$ 633,222
Structures	2,623,561	2,514,602
Towers, transmitters and studio equipment	397,434	381,046
Furniture and other equipment	282,385	234,101
Construction in progress	65,173	88,391
	4,021,128	3,851,362
Less: accumulated depreciation	875,574	518,969
Property, plant and equipment, net	$ 3,145,554	$ 3,332,393

Definite-lived Intangible Assets

The following table presents the gross carrying amount and accumulated amortization for each major class of definite-lived intangible assets at December 31, 2010 and 2009, respectively:

(In thousands)	December 31, 2010		December 31, 2009	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Transit, street furniture, and other outdoor contractual rights	$ 789,867	$ 241,461	$ 803,297	$ 166,803
Customer / advertiser relationships	1,210,205	289,824	1,210,205	169,897
Talent contracts	317,352	99,050	320,854	57,825
Representation contracts	231,623	101,650	218,584	54,755
Other	551,197	80,110	550,041	54,457
Total	$ 3,100,244	$ 812,095	$ 3,102,981	$ 503,737

Total amortization expense from continuing operations related to definite-lived intangible assets was $332.3 million, $341.6 million and $208.6 million for the post-merger years ended December 31, 2010 and 2009, and the combined period ended December 31, 2008, respectively.

As acquisitions and dispositions occur in the future, amortization expense may vary. The following table presents the Company s estimate of amortization expense for each of the five succeeding fiscal years for definite-lived intangible assets:

(In thousands)	
2011	$ 302,958
2012	289,694
2013	274,295
2014	253,772
2015	235,056

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Goodwill and Indefinite-lived Intangible Assets

The Company s indefinite-lived intangible assets consist of FCC broadcast licenses and billboard permits. FCC broadcast licenses are granted to radio stations for up to eight years under the Telecommunications Act of 1996 (the Act). The Act requires the FCC to renew a broadcast license if the FCC finds that the station has served the public interest, convenience and necessity, there have been no serious violations of either the Communications Act of 1934 or the FCC s rules and regulations by the licensee, and there have been no other serious violations which taken together constitute a pattern of abuse. The licenses may be renewed indefinitely at little or no cost. The Company does not believe that the technology of wireless broadcasting will be replaced in the foreseeable future.

The Company s billboard permits are granted for the right to operate an advertising structure at the specified location as long as the structure is in compliance with the laws and regulations of each jurisdiction. The Company s permits are located on owned land, leased land or land for which we have acquired permanent easements. In cases where the Company s permits are located on leased land, the leases typically have initial terms of between 10 and 20 years and renew indefinitely, with rental payments generally escalating at an inflation-based index. If the Company loses its lease, the Company will typically obtain permission to relocate the permit or bank it with the municipality for future use. Due to significant differences in both business practices and regulations, billboards in the International segment are subject to long-term, finite contracts unlike the Company s permits in the United States and Canada. Accordingly, there are no indefinite-lived assets in the International segment.

The impairment tests for indefinite-lived intangible assets consist of a comparison between the fair value of the indefinite-lived intangible at the market level with its carrying amount. If the carrying amount of the indefinite-lived intangible exceeds its fair value, an impairment loss is recognized equal to that excess. After an impairment loss is recognized, the adjusted carrying amount of the indefinite-lived asset is its new accounting basis. The fair value of the indefinite-lived asset is determined using the direct valuation method as prescribed in ASC 805-20-S99. Under the direct valuation method, the fair value of the indefinite-lived asset is calculated at the market level as prescribed by ASC 350-30-35. The Company engaged Mesirow Financial, a third-party valuation firm, to assist it in the development of the assumptions and the Company s determination of the fair value of its indefinite-lived assets.

The application of the direct valuation method attempts to isolate the income that is properly attributable to the indefinite-lived asset alone (that is, apart from tangible and identified intangible assets and goodwill). It is based upon modeling a hypothetical greenfield build-up to a normalized enterprise that, by design, lacks inherent goodwill and whose only other assets have essentially been paid for (or added) as part of the build-up process. The Company forecasts revenue, expenses, and cash flows over a ten-year period for each of its markets in its application of the direct valuation method. The Company also calculates a normalized residual year which represents the perpetual cash flows of each market. The residual year cash flow was capitalized to arrive at the terminal value of the licenses in each market.

Under the direct valuation method, it is assumed that rather than acquiring indefinite-lived intangible assets as part of a going concern business, the buyer hypothetically develops indefinite-lived intangible assets and builds a new operation with similar attributes from scratch. Thus, the buyer incurs start-up costs during the build-up phase which are normally associated with going concern value. Initial capital costs are deducted from the discounted cash flow model which results in value that is directly attributable to the indefinite-lived intangible assets.

The key assumptions using the direct valuation method are market revenue growth rates, market share, profit margin, duration and profile of the build-up period, estimated start-up capital costs and losses incurred during the build-up period, the risk-adjusted discount rate and terminal values. This data is populated using industry normalized information representing an average FCC license or billboard permit within a market.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Annual Impairment Test to FCC Licenses and Billboard permits

The Company performs its annual impairment test on October 1 of each year.

The aggregate fair value of the Company s FCC licenses on October 1, 2010 increased approximately 14% from the fair value at October 1, 2009. The increase in fair value resulted primarily from improvements to general market conditions leading to increased advertising spending, which results in higher revenues for the industry.

The aggregate fair value of the Company s permits on October 1, 2010 increased approximately 58% from the fair value at October 1, 2009. The increase in fair value resulted primarily from improvements to general market conditions leading to increased advertising spending, which results in higher revenues for the industry.

Although the aggregate fair values of FCC licenses and billboard permits increased, certain markets experienced continuing declines. As a result, impairment charges were recorded in 2010 for FCC licenses and billboard permits of $0.5 million and $4.8 million, respectively.

Interim Impairments to FCC Licenses

The Company performed interim impairment tests on its FCC licenses as of December 31, 2008 and again on June 30, 2009 as a result of the poor economic environment during those periods. In determining the fair value of the Company s FCC licenses, the following key assumptions were used:

(i) Industry revenue forecast by BIA Financial Network, Inc. (BIA) of 1.9% and 1.8%, respectively, were used during the three year build-up period in the December 31, 2008 and June 30, 2009 impairment tests;

(ii) Operating margin of 12.5% in the first year gradually climbs to the industry average margin in year 3 of 30% and 29%, respectively, in the December 31, 2008 and June 30, 2009 impairment tests;

(iii) 2% revenue growth was assumed beyond the discrete build-up projection period in both the December 31, 2008 and June 30, 2009 impairment tests; and

(iv) Assumed discount rates of 10% for the 13 largest markets and 10.5% for all other markets in both the December 31, 2008 and June 30, 2009 impairment tests;

The discount rate used in the December 31, 2008 impairment model increased 150 basis points compared to the discount rate used in the preliminary purchase price allocation as of July 30, 2008 which resulted in a decline in the fair value of the Company s licenses. As a result, the Company recognized a non-cash impairment charge at December 31, 2008 in approximately one-quarter of its markets, which totaled $936.2 million.

The BIA forecast for 2009 declined 8.7% and declined between 13.8% and 15.7% through 2013 compared to the BIA forecasts used in the 2008 impairment test. Additionally, the industry profit margin declined 100 basis points from the 2008 impairment test. These market driven changes were primarily responsible for the decline in fair value of the FCC licenses below their carrying value. As a result, the Company recognized a non-cash impairment charge at June 30, 2009 in approximately one-quarter of its markets, which totaled $590.3 million.

In calculating the fair value of its FCC licenses, the Company primarily relied on the discounted cash flow models. However, the Company relied on the stick method for those markets where the discounted cash flow model resulted in a value less than the stick method indicated. Approximately 17% and 23% of the fair value of the Company s FCC licenses at December 31, 2008 and June 30, 2009, respectively, was determined using the stick method.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Interim Impairments to Billboard Permits

The Company performed interim impairment tests on its billboard permits as of December 31, 2008 and again on June 30, 2009 as a result of the poor economic environment during those periods. In determining the fair value of the Company s billboard permits, the following key assumptions were used:

(i) Industry revenue growth of negative 9% and negative 16%, respectively, during the one year build-up period used in the December 31, 2008 and June 30, 2009 impairment tests;

(ii) Cost structure reached a normalized level over a three year period and the operating margins gradually grew over that period to the industry average margins of 46% and 45%, respectively, in the December 31, 2008 and June 30, 2009 impairment tests. The margin in year three was the lower of the industry average margin or the actual margin for the market;

(iii) Industry average revenue growth of 3% beyond the discrete build-up projection period in the December 31, 2008 and June 30, 2009 impairment tests;

(iv) Discount rates of 9.5% and 10%, respectively, in the December 31, 2008 and June 30, 2009 impairment tests.

The discount rate used in the December 31, 2008 impairment model increased approximately 100 basis points over the discount rate used to value the permits in the preliminary purchase price allocation as of July 30, 2008. Industry revenue forecasts declined 10% through 2013 compared to the forecasts used in the preliminary purchase price allocation as of July 30, 2008. These market driven changes were primarily responsible for the decline in fair value of the billboard permits below their carrying value. As a result, the Company recognized a non-cash impairment charge at December 31, 2008 which totaled $722.6 million.

The discount rate used in the June 30, 2009 impairment model increased approximately 50 basis points over the discount rate used to value the permits at December 31, 2008. Industry revenue forecasts declined 8% through 2013 compared to the forecasts used in the 2008 impairment test. These market driven changes were primarily responsible for the decline in fair value of the billboard permits below their carrying value. As a result, the Company recognized a non-cash impairment charge at June 30, 2009 in all but five of its markets in the United States and Canada, which totaled $345.4 million.

Annual Impairment Test to Goodwill

The Company performs its annual impairment test on October 1 of each year. The Company engaged Mesirow Financial to assist the Company in the development of its assumptions and the Company s determination of the fair value of its reporting units.

Each of the Company s U.S. radio markets and outdoor advertising markets are components. The U.S. radio markets are aggregated into a single reporting unit and the U.S. outdoor advertising markets are aggregated into a single reporting unit for purposes of the goodwill impairment test using the guidance in ASC 350-20-55. The Company also determined that within its Americas outdoor segment, Canada, Mexico, Peru, and Brazil constitute separate reporting units and each country in its International outdoor segment constitutes a separate reporting unit.

The goodwill impairment test is a two-step process. The first step, used to screen for potential impairment, compares the fair value of the reporting unit with its carrying amount, including goodwill. If applicable, the second step, used to measure the amount of the impairment loss, compares the implied fair value of the reporting unit goodwill with the carrying amount of that goodwill.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Each of the Company s reporting units is valued using a discounted cash flow model which requires estimating future cash flows expected to be generated from the reporting unit, discounted to their present value using a risk-adjusted discount rate. Terminal values were also estimated and discounted to their present value. Assessing the recoverability of goodwill requires the Company to make estimates and assumptions about sales, operating margins, growth rates and discount rates based on its budgets, business plans, economic projections, anticipated future cash flows and marketplace data. There are inherent uncertainties related to these factors and management s judgment in applying these factors.

The following table presents the changes in the carrying amount of goodwill in each of the Company s reportable segments. The provisions of ASC 350-20-50-1 require the disclosure of cumulative impairment. As a result of the merger, a new basis in goodwill was recorded in accordance with ASC 805-10. All impairments shown in the table below have been recorded subsequent to the merger and, therefore, do not include any pre-merger impairment.

(In thousands)	Radio Broadcasting	Americas Outdoor Advertising	International Outdoor Advertising	Other	Consolidated
Post-Merger					
Balance as of December 31, 2008	$ 5,579,190	$ 892,598	$ 287,543	$ 331,290	$ 7,090,621
Impairment	(2,420,897)	(390,374)	(73,764)	(211,988)	(3,097,023)
Acquisitions	4,518	2,250	110		6,878
Dispositions	(62,410)			(2,276)	(64,686)
Foreign currency		16,293	17,412		33,705
Purchase price adjustments - net	47,086	68,896	45,042	(482)	160,542
Other	(618)	(4,414)			(5,032)
Balance as of December 31, 2009	$ 3,146,869	$ 585,249	$ 276,343	$ 116,544	$ 4,125,005
Impairment			(2,142)		(2,142)
Acquisitions				342	342
Dispositions	(5,325)				(5,325)
Foreign currency		285	3,299		3,584
Other	(1,346)		(792)		(2,138)
Balance as of December 31, 2010	$ 3,140,198	$ 585,534	$ 276,708	$ 116,886	$ 4,119,326

The balance at December 31, 2008 is net of cumulative impairments of $1.1 billion, $2.3 billion, and $173.4 million in the Radio broadcasting, Americas outdoor and International outdoor segments, respectively.

The fair value of the Company s reporting units on October 1, 2010 increased from the fair value at October 1, 2009. The increase in the fair value of the Company s radio reporting unit was primarily the result of a 50 basis point decline in the discount rate and a $210.0 million increase related to industry projections. The increase in the fair value of the Company s Americas outdoor reporting unit was primarily the result of a $638.6 million increase related to forecast revenues and operating margins. As a result of increase in fair value across the radio and Americas outdoor reporting units, no goodwill impairments were recognized in these segments. Within the Company s International outdoor segment, one country experienced a decline in fair value which resulted in a $2.1 million non-cash impairment to goodwill.

Interim Impairment Tests to Goodwill

The discounted cash flow model indicated that the Company failed the first step of the impairment test for certain of its reporting units as of December 31, 2008 and June 30, 2009, which required it to compare the implied fair value of each reporting unit s goodwill with its carrying

value.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The Company forecasted revenue, expenses, and cash flows over a ten-year period for each of its reporting units. Historically, revenues in its industries have been highly correlated to economic cycles. Based on this consideration, among others, the assumed 2008 and 2009 revenue growth rates used in the December 31, 2008 and June 30, 2009 impairment models were negative followed by assumed revenue growth with an anticipated economic recovery in 2009 and 2010, respectively. The Company also calculated a normalized residual year which represents the perpetual cash flows of each reporting unit. The residual year cash flow was capitalized to arrive at the terminal value of the reporting unit.

The Company calculated the weighted average cost of capital (WACC) as of December 31, 2008 resulting in WACCs of 11%, 12.5% and 12.5% for each of the reporting units in the Radio, Americas outdoor and International outdoor segments, respectively. As of June 30, 2009, the Company calculated WACCs of 11%, 12.5% and 13.5% for each of the reporting units in the Radio, Americas outdoor and International outdoor segments, respectively.

The Company also utilized the market approach to provide a test of reasonableness to the results of the discounted cash flow model. The market approach indicates the fair value of the invested capital of a business based on a company s market capitalization (if publicly traded) and a comparison of the business to comparable publicly traded companies and transactions in its industry. This approach can be estimated through the quoted market price method, the market comparable method, and the market transaction method. The three variations of the market approach indicated that the fair value determined by the Company s discounted cash flow model was within a reasonable range of outcomes as of December 31, 2008 and June 30, 2009.

The revenue forecasts for 2009 declined 18%, 21% and 29% for Radio, Americas outdoor and International outdoor, respectively, compared to the forecasts used in the July 30, 2008 preliminary purchase price allocation primarily as a result of the revenues realized for the year ended December 31, 2008. These market driven changes were primarily responsible for the decline in fair value of the reporting units below their carrying value. As a result, the Company recognized a non-cash impairment charge to reduce its goodwill of $3.6 billion at December 31, 2008.

The revenue forecasts for 2009 declined 8%, 7% and 9% for Radio, Americas outdoor and International outdoor, respectively, compared to the forecasts used in the 2008 impairment test primarily as a result of the revenues realized during the first six months of 2009. These market driven changes were primarily responsible for the decline in fair value of the reporting units below their carrying value. As a result, the Company recognized a non-cash impairment charge to reduce its goodwill of $3.1 billion at June 30, 2009.

NOTE 5 INVESTMENTS

The Company s most significant investments in nonconsolidated affiliates are listed below:

Australian Radio Network

The Company owns a fifty-percent (50%) interest in Australian Radio Network (ARN), an Australian company that owns and operates radio stations in Australia and New Zealand.

Grupo ACIR Comunicaciones

Clear Channel sold a portion of its investment in Grupo ACIR for approximately $47.0 million on July 1, 2008 and recorded a gain of $9.2 million in equity in earnings of nonconsolidated affiliates during the pre-merger period ended July 30, 2008. Effective January 30, 2009 the Company sold 57% of its remaining 20% interest in Grupo ACIR. The Company sold the remainder of its interest on July 28, 2009.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Summarized Financial Information

The following table summarizes the Company s investments in nonconsolidated affiliates:

(In thousands)	ARN	Grupo ACIR	All Others	Total
Balance at December 31, 2008	$ 290,808	$ 41,518	$ 51,811	$ 384,137
Reclass to cost method investments and other		(17,469)	1,283	(16,186)
Dispositions of investments, net		(19,153)	(19)	(19,172)
Cash advances (repayments)	(17,263)	3	4,402	(12,858)
Equity in net earnings (loss)	15,191	(4,372)	(31,508)	(20,689)
Foreign currency transaction adjustment	(10,354)			(10,354)
Foreign currency translation adjustment	42,396	(527)	819	42,688
Fair value adjustments			(2,217)	(2,217)
Balance at December 31, 2009	$ 320,778	$	$ 24,571	$ 345,349
Reclass to cost method investments and other			1,574	1,574
Dispositions of investments, net			(987)	(987)
Cash advances			2,556	2,556
Equity in net earnings (loss)	15,685		(9,983)	5,702
Foreign currency transaction adjustment	(6,881)			(6,881)
Foreign currency translation adjustment	21,589		(434)	21,155
Distributions received	(8,386)		(2,331)	(10,717)
Balance at December 31, 2010	$ 342,785	$	$ 14,966	$ 357,751

The investments in the table above are not consolidated, but are accounted for under the equity method of accounting, whereby the Company records its investments in these entities in the balance sheet as Other assets. The Company s interests in their operations are recorded in the statement of operations as Equity in earnings (loss) of nonconsolidated affiliates .

Other Investments

Other investments of $75.3 million and $44.7 million at December 31, 2010 and 2009, respectively, include marketable equity securities and other investments classified as follows:

(In thousands) Investments	Cost	Gross Unrealized Losses	Gross Unrealized Gains	Fair Value
2010				
Available-for sale	$ 12,614	$	$ 57,945	$ 70,559
Other cost investments	4,773			$ 4,773
Total	$ 17,387	$	$ 57,945	$ 75,332
2009				
Available-for sale	$ 19,104	$ (12,237)	$ 32,035	$ 38,902

Other cost investments	5,783			5,783
Total	$ 24,887	$ (12,237)	$ 32,035	$ 44,685

The Company s available-for-sale security, Independent News & Media PLC (INM), was in an unrealized loss position for an extended period of time in 2008 and 2009. As a result, the Company considered the guidance in

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

ASC 320-10-S99 and reviewed the length of the time and the extent to which the market value was less than cost and the financial condition and near-term prospects of the issuer. After this assessment, the Company concluded that the impairment was other than temporary and recorded a non-cash impairment charge of $11.3 million and $59.8 million in Gain (loss) on marketable securities for the years ended December 31, 2009 and 2008, respectively. The fair value of this investment has continued to decline throughout 2010 and the Company has concluded based on the guidance in ASC 320-10-S99 that such decline is other than temporary. Accordingly, the Company recorded a non-cash impairment charge of $6.5 million in 2010 to write the investment down to fair value, recorded in Gain (loss) on marketable securities.

In addition, the fair value of the Company s available-for-sale security, Sirius XM Radio, Inc., was below its cost for an extended period of time in 2008. After considering ASC 320-10-S99 guidance, the Company concluded that the impairment was other than temporary and recorded a non-cash impairment charge of $56.7 million in Gain (loss) on marketable securities for the year ended December 31, 2008.

Clear Channel sold its American Tower Corporation securities in the second quarter of 2008 and recorded a gain of $30.4 million on the statement of operations in Gain (loss) on marketable securities .

Other cost investments include various investments in companies for which there is no readily determinable market value.

NOTE 6 - ASSET RETIREMENT OBLIGATION

The Company s asset retirement obligation is reported in Other long-term liabilities and relates to its obligation to dismantle and remove outdoor advertising displays from leased land and to reclaim the site to its original condition upon the termination or non-renewal of a lease. Asset retirement obligations are also recorded as necessary for other structures residing on leased property. When the liability is recorded, the cost is capitalized as part of the related long-lived assets carrying value. Due to the high rate of lease renewals over a long period of time, the calculation assumes that all related assets will be removed at some period over the next 50 years. An estimate of third-party cost information is used with respect to the dismantling of the structures and the reclamation of the site. The interest rate used to calculate the present value of such costs over the retirement period is based on an estimated risk adjusted credit rate for the same period.

The following table presents the activity related to the Company s asset retirement obligation:

(In thousands)	Years Ended December 31,	
	2010	2009
Beginning balance	$ 51,301	$ 55,592
Adjustment due to change in estimate of related costs	(1,839)	(6,721)
Accretion of liability	5,202	5,209
Liabilities settled	(2,565)	(2,779)
Ending balance	$ 52,099	$ 51,301

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 7 - LONG-TERM DEBT

Long-term debt at December 31, 2010 and 2009 consisted of the following:

(In thousands)	December 31, 2010	December 31, 2009
Senior Secured Credit Facilities:		
Term loan A Facility Due 2014(1)	$ 1,127,657	$ 1,127,657
Term loan B Facility Due 2016	9,061,911	9,061,911
Term loan C - Asset Sale Facility Due 2016(1)	695,879	695,879
Revolving Credit Facility Due 2014	1,842,500	1,812,500
Delayed Draw Facilities Due 2016	1,013,227	874,432
Receivables Based Facility Due 2014	384,232	355,732
Other Secured Long-term Debt	4,692	5,225
Total Consolidated Secured Debt	14,130,098	13,933,336
Senior Cash Pay Notes	796,250	796,250
Senior Toggle Notes	829,831	915,200
Clear Channel Senior Notes:		
7.65% Senior Notes Due 2010		116,181
4.5% Senior Notes Due 2010		239,975
6.25% Senior Notes Due 2011	692,737	692,737
4.4% Senior Notes Due 2011	140,241	140,241
5.0% Senior Notes Due 2012	249,851	249,851
5.75% Senior Notes Due 2013	312,109	312,109
5.5% Senior Notes Due 2014	541,455	541,455
4.9% Senior Notes Due 2015	250,000	250,000
5.5% Senior Notes Due 2016	250,000	250,000
6.875% Senior Debentures Due 2018	175,000	175,000
7.25% Senior Debentures Due 2027	300,000	300,000
Subsidiary Senior Notes:		
9.25% Series A Senior Notes Due 2017	500,000	500,000
9.25% Series B Senior Notes Due 2017	2,000,000	2,000,000
Other long-term debt	63,115	77,657
Purchase accounting adjustments and original issue discount	(623,335)	(788,087)
	20,607,352	20,701,905
Less: current portion	867,735	398,779
Total long-term debt	$ 19,739,617	$ 20,303,126

(1) These facilities are subject to an amortization schedule with the final payment on the Term Loan A and Term Loan C due 2014 and 2016, respectively.

The Company s weighted average interest rate at December 31, 2010 was 5.8%. The aggregate market value of the Company s debt based on quoted market prices for which quotes were available was approximately $18.7 billion and $17.7 billion at December 31, 2010 and 2009, respectively.

The Company and its subsidiaries have from time to time repurchased certain debt obligations of Clear Channel and may in the future, as part of various financing and investment strategies, purchase additional outstanding indebtedness of Clear Channel or its subsidiaries or outstanding equity securities of Clear Channel Outdoor

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Holdings, Inc. (CCOH) or CCMH, in tender offers, open market purchases, privately negotiated transactions or otherwise. The Company or its subsidiaries may also sell certain assets or properties and use the proceeds to reduce its indebtedness. These purchases or sales, if any, could have a material positive or negative impact on the Company s liquidity available to repay outstanding debt obligations or on the Company s consolidated results of operations. These transactions could also require or result in amendments to the agreements governing outstanding debt obligations or changes in the Company s leverage or other financial ratios, which could have a material positive or negative impact on the Company s ability to comply with the covenants contained in its debt agreements. These transactions, if any, will depend on prevailing market conditions, the Company s liquidity requirements, contractual restrictions and other factors. The amounts involved may be material.

Senior Secured Credit Facilities

Borrowings under Clear Channel s senior secured credit facilities bear interest at a rate equal to an applicable margin plus, at Clear Channel s option, either (i) a base rate determined by reference to the higher of (A) the prime lending rate publicly announced by the administrative agent and (B) the Federal funds effective rate from time to time plus 0.50%, or (ii) a Eurocurrency rate determined by reference to the costs of funds for deposits for the interest period relevant to such borrowing adjusted for certain additional costs.

The margin percentages applicable to the term loan facilities and revolving credit facility are the following percentages per annum:

- with respect to loans under the term loan A facility and the revolving credit facility, (i) 2.40% in the case of base rate loans and (ii) 3.40% in the case of Eurocurrency rate loans; and

- with respect to loans under the term loan B facility, term loan C - asset sale facility and delayed draw term loan facilities, (i) 2.65%, in the case of base rate loans and (ii) 3.65%, in the case of Eurocurrency rate loans.

The margin percentages are subject to adjustment based upon Clear Channel s leverage ratio.

Clear Channel is required to pay each revolving credit lender a commitment fee in respect of any unused commitments under the revolving credit facility, which is currently 0.50% per annum, but subject to adjustment based on Clear Channel s leverage ratio. The delayed draw term facilities are fully drawn, therefore there are currently no commitment fees associated with any unused commitments thereunder.

Prepayments

The senior secured credit facilities require Clear Channel to prepay outstanding term loans, subject to certain exceptions, with:

- 50% (which percentage may be reduced to 25% and to 0% based upon Clear Channel s leverage ratio) of Clear Channel s annual excess cash flow (as calculated in accordance with the senior secured credit facilities), less any voluntary prepayments of term loans and revolving credit loans (to the extent accompanied by a permanent reduction of the commitment) and subject to customary credits;

- 100% of the net cash proceeds of sales or other dispositions of specified assets being marketed for sale (including casualty and condemnation events), subject to certain exceptions;

- 100% (which percentage may be reduced to 75% and 50% based upon Clear Channel s leverage ratio) of the net cash proceeds of sales or other dispositions by Clear Channel or its wholly-owned restricted subsidiaries of assets other than specified assets being marketed

for sale, subject to reinvestment rights and certain other exceptions; and

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

100% of the net cash proceeds of (i) any incurrence of certain debt, other than debt permitted under Clear Channel s senior secured credit facilities, (ii) certain securitization financing and (iii) certain issuances of Permitted Additional Notes (as defined in the senior secured credit facilities).

The foregoing prepayments with the net cash proceeds of certain incurrences of debt and annual excess cash flow will be applied (i) first to the term loans other than the term loan C - asset sale facility loans (on a pro rata basis) and (ii) second to the term loan C - asset sale facility loans, in each case to the remaining installments thereof in direct order of maturity. The foregoing prepayments with the net cash proceeds of the sale of assets (including casualty and condemnation events) will be applied (i) first to the term loan C - asset sale facility loans and (ii) second to the other term loans (on a pro rata basis), in each case to the remaining installments thereof in direct order of maturity.

Clear Channel may voluntarily repay outstanding loans under the senior secured credit facilities at any time without premium or penalty, other than customary breakage costs with respect to Eurocurrency rate loans.

Amortization of Term Loans

Clear Channel is required to repay the loans under the term loan facilities, after giving effect to the December 2009 prepayment of $2.0 billion of term loans with proceeds from the issuance of subsidiary senior notes discussed elsewhere in this MD&A, as follows:

The term loan A facility amortizes in quarterly installments commencing on the third interest payment date after the fourth anniversary of the closing date of the merger, in annual amounts equal to 4.7% of the original funded principal amount of such facility in year five, 10% thereafter, with the balance being payable on the final maturity date (July 2014) of such term loans;

The term loan B facility and the delayed draw facilities will be payable in full on the final maturity date (January 2016) of such term loans; and

The term loan C asset sale facility amortizes in quarterly installments on the first interest payment date after the third anniversary of the closing date of the merger, in annual amounts equal to 2.5% of the original funded principal amount of such facilities in years four and five and 1% thereafter, with the balance being payable on the final maturity date (January 2016) of such term loans.

Collateral and Guarantees

The senior secured credit facilities are guaranteed by the Company and each of the Company s existing and future material wholly-owned domestic restricted subsidiaries, subject to certain exceptions.

All obligations under the senior secured credit facilities, and the guarantees of those obligations, are secured, subject to permitted liens, including prior liens permitted by the indenture governing the Clear Channel senior notes, and other exceptions, by:

a lien on the capital stock of Clear Channel;

100% of the capital stock of any future material wholly-owned domestic license subsidiary that is not a Restricted Subsidiary under the indenture governing the Clear Channel senior notes;

certain assets that do not constitute principal property (as defined in the indenture governing the Clear Channel senior notes);

certain specified assets of Clear Channel and the guarantors that constitute principal property (as defined in the indenture governing the Clear Channel senior notes) securing obligations under the senior secured credit facilities up to the maximum amount permitted to be secured by such assets without requiring equal and ratable security under the indenture governing the Clear Channel senior notes; and

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

a lien on the accounts receivable and related assets securing Clear Channel s receivables based credit facility that is junior to the lien securing Clear Channel s obligations under such credit facility.

The obligations of any foreign subsidiaries that are borrowers under the revolving credit facility are also guaranteed by certain of their material wholly-owned restricted subsidiaries, and secured by substantially all assets of all such borrowers and guarantors, subject to permitted liens and other exceptions.

Certain Events of Default

The senior secured credit facilities contain a financial covenant that requires Clear Channel to comply on a quarterly basis with a maximum consolidated senior secured net debt to adjusted EBITDA ratio (maximum of 9.5:1). This financial covenant becomes more restrictive over time. Clear Channel s senior secured debt consists of the senior secured facilities, the receivables based credit facility and certain other secured subsidiary debt. The Company was in compliance with this covenant as of December 31, 2010.

In addition, the senior secured credit facilities include negative covenants that, subject to significant exceptions, limit the Company s ability and the ability of its restricted subsidiaries to, among other things:

incur additional indebtedness;

create liens on assets;

engage in mergers, consolidations, liquidations and dissolutions;

sell assets;

pay dividends and distributions or repurchase Clear Channel s capital stock;

make investments, loans, or advances;

prepay certain junior indebtedness;

engage in certain transactions with affiliates;

amend material agreements governing certain junior indebtedness; and

change lines of business.

The senior secured credit facilities include certain customary representations and warranties, affirmative covenants and events of default, including payment defaults, breach of representations and warranties, covenant defaults, cross-defaults to certain indebtedness, certain events of bankruptcy, certain events under ERISA, material judgments, the invalidity of material provisions of the senior secured credit facilities documentation, the failure of collateral under the security documents for the senior secured credit facilities, the failure of the senior secured credit facilities to be senior debt under the subordination provisions of certain of the Company s subordinated debt and a change of control. If an event of default occurs, the lenders under the senior secured credit facilities will be entitled to take various actions, including the acceleration of all amounts due under the senior secured credit facilities and all actions permitted to be taken by a secured creditor.

Receivables Based Credit Facility

As of December 31, 2010, the Company had a total of $384.2 million outstanding under Clear Channel s receivables based credit facility.

The receivables based credit facility provides revolving credit of $783.5 million, subject to a borrowing base. The borrowing base at any time equals 85% of the Company s and certain of its subsidiaries eligible accounts receivable. The receivables based credit facility includes a letter of credit sub-facility and a swingline loan sub-facility. The maturity of the receivables based credit facility is July 2014.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

All borrowings under the receivables based credit facility are subject to the absence of any default, the accuracy of representations and warranties and compliance with the borrowing base. In addition, borrowings under the receivables based credit facility, excluding the initial borrowing, are subject to compliance with a minimum fixed charge coverage ratio of 1.0:1.0 if at any time excess availability under the receivables based credit facility is less than $50 million, or if aggregate excess availability under the receivables based credit facility and revolving credit facility is less than 10% of the borrowing base.

Clear Channel and certain subsidiary borrowers are the borrowers under the receivables based credit facility. Clear Channel has the ability to designate one or more of its restricted subsidiaries as borrowers under the receivables based credit facility. The receivables based credit facility loans and letters of credit are available in U.S. dollars.

Borrowings under the receivables based credit facility bear interest at a rate equal to an applicable margin plus, at Clear Channel s option, either (i) a base rate determined by reference to the higher of (A) the prime lending rate publicly announced by the administrative agent and (B) the Federal funds effective rate from time to time plus 0.50%, or (ii) a Eurocurrency rate determined by reference to the costs of funds for deposits for the interest period relevant to such borrowing adjusted for certain additional costs.

The margin percentage applicable to the receivables based credit facility is (i) 1.40%, in the case of base rate loans and (ii) 2.40% in the case of Eurocurrency rate loans subject to adjustment if Clear Channel s leverage ratio of total debt to EBITDA decreases below 7 to 1.

Clear Channel is required to pay each lender a commitment fee in respect of any unused commitments under the receivables based credit facility, which is currently 0.375% per annum, subject to adjustment based on Clear Channel s leverage ratio.

Prepayments

If at any time the sum of the outstanding amounts under the receivables based credit facility (including the letter of credit outstanding amounts and swingline loans thereunder) exceeds the lesser of (i) the borrowing base and (ii) the aggregate commitments under the receivables based credit facility, Clear Channel will be required to repay outstanding loans and cash collateralize letters of credit in an aggregate amount equal to such excess.

Clear Channel may voluntarily repay outstanding loans under the receivables based credit facility at any time without premium or penalty, other than customary breakage costs with respect to Eurocurrency rate loans.

Collateral and Guarantees

The receivables based credit facility is guaranteed by, subject to certain exceptions, the guarantors of the senior secured credit facilities. All obligations under the receivables based credit facility, and the guarantees of those obligations, are secured by a perfected security interest in all of the Company s and all of the guarantors accounts receivable and related assets and proceeds thereof, that is senior to the security interest of the senior secured credit facilities in such accounts receivable and related assets and proceeds thereof, subject to permitted liens, including prior liens permitted by the indenture governing the Clear Channel senior notes, and certain exceptions.

The receivables based credit facility includes negative covenants, representations, warranties, events of default, and termination provisions substantially similar to those governing the senior secured credit facilities.

Senior Cash Pay Notes and Senior Toggle Notes

As of December 31, 2010, the Company had outstanding $796.3 million aggregate principal amount of 10.75% senior cash pay notes due 2016 and $829.8 million aggregate principal amount of 11.00%/11.75% senior toggle notes due 2016.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The senior cash pay notes and senior toggle notes are unsecured and are guaranteed by the Company and each of its existing and future material wholly-owned domestic restricted subsidiaries, subject to certain exceptions. The senior toggle notes mature on August 1, 2016 and may require a special redemption of up to $30.0 million on August 1, 2015. Clear Channel may elect on each interest election date to pay all or 50% of such interest on the senior toggle notes in cash or by increasing the principal amount of the senior toggle notes or by issuing new senior toggle notes (such increase or issuance, PIK Interest). Interest on the senior toggle notes payable in cash will accrue at a rate of 11.00% per annum and PIK Interest will accrue at a rate of 11.75% per annum.

Clear Channel may redeem some or all of the senior cash pay notes and senior toggle notes at any time prior to August 1, 2012, at a price equal to 100% of the principal amount of such notes plus accrued and unpaid interest thereon to the redemption date and an applicable premium, as described in the indenture governing such notes. Clear Channel may redeem some or all of the senior cash pay notes and senior toggle notes at any time on or after August 1, 2012 at the redemption prices set forth in the indenture governing such notes. In addition, Clear Channel may redeem up to 40% of any series of the outstanding senior cash pay notes and senior toggle notes at any time on or prior to August 1, 2011 with the net cash proceeds raised in one or more equity offerings. If Clear Channel undergoes a change of control, sells certain of the Company s assets, or issues certain debt, it may be required to offer to purchase the senior cash pay notes and senior toggle notes from holders.

The senior cash pay notes and senior toggle notes are senior unsecured debt and rank equal in right of payment with all of the Company s existing and future senior debt. Guarantors of obligations under the senior secured credit facilities and the receivables based credit facility guarantee the senior cash pay notes and senior toggle notes with unconditional guarantees that are unsecured and equal in right of payment to all existing and future senior debt of such guarantors, except that the guarantees are subordinated in right of payment only to the guarantees of obligations under the senior secured credit facilities and the receivables based credit facility. In addition, the senior cash pay notes and senior toggle notes and the guarantees are structurally senior to the Clear Channel senior notes and existing and future debt to the extent that such debt is not guaranteed by the guarantors of the senior cash pay notes and senior toggle notes. The senior cash pay notes and senior toggle notes and the guarantees are effectively subordinated to the Company s existing and future secured debt and that of the guarantors to the extent of the value of the assets securing such indebtedness and are structurally subordinated to all obligations of subsidiaries that do not guarantee the senior cash pay notes and senior toggle notes.

On July 16, 2010, Clear Channel made the election to pay interest on the senior toggle notes entirely in cash, effective for the interest period commencing August 1, 2010. Assuming the cash interest election remains in effect for the remaining term of the notes, Clear Channel will be contractually obligated to make a payment to bondholders of $57.4 million on August 1, 2013.

Clear Channel Senior Notes

As of December 31, 2010, Clear Channel s senior notes and debentures represented approximately $2.9 billion of aggregate principal amount of indebtedness outstanding.

The senior notes and debentures were the obligations of Clear Channel prior to the merger. The senior notes and debentures are senior, unsecured obligations that are effectively subordinated to the Company s secured indebtedness to the extent of the value of the assets securing such indebtedness and the guarantees of such indebtedness from the Company s existing and future material wholly-owned domestic restricted subsidiaries, subject to certain exceptions. The senior notes and debentures rank equally in right of payment with all of the Company s existing and future senior indebtedness and senior in right of payment to all existing and future subordinated indebtedness. The senior notes and debentures are not guaranteed by Clear Channel s subsidiaries.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Subsidiary Senior Notes

As of December 31, 2010, the Company had outstanding $2.5 billion aggregate principal amount of subsidiary senior notes, which consisted of $500.0 million aggregate principal amount of Series A Senior Notes due 2017 (the Series A Notes) and $2.0 billion aggregate principal amount of Series B Senior Notes due 2017 (the Series B Notes). The subsidiary senior notes were issued by Clear Channel Worldwide Holdings, Inc. (CCWH) and are guaranteed by CCOH, Clear Channel Outdoor, Inc. (CCOI) and certain of CCOH s direct and indirect subsidiaries.

The subsidiary senior notes bear interest on a daily basis and contain customary provisions, including covenants requiring the Company to maintain certain levels of credit availability and limitations on incurring additional debt.

The subsidiary senior notes are senior obligations that rank pari passu in right of payment to all unsubordinated indebtedness of CCWH and the guarantees of the subsidiary senior notes rank pari passu in right of payment to all unsubordinated indebtedness of the guarantors.

The indentures governing the subsidiary senior notes require the Company to maintain at least $100 million in cash or other liquid assets or have cash available to be borrowed under committed credit facilities consisting of (i) $50.0 million at the issuer and guarantor entities (principally the Americas outdoor segment) and (ii) $50.0 million at the non-guarantor subsidiaries (principally the International outdoor segment) (together the Liquidity Amount), in each case under the sole control of the relevant entity. In the event of a bankruptcy, liquidation, dissolution, reorganization, or similar proceeding of Clear Channel, for the period thereafter that is the shorter of such proceeding and 60 days, the Liquidity Amount shall be reduced to $50.0 million, with a $25.0 million requirement at the issuer and guarantor entities and a $25.0 million requirement at the non-guarantor subsidiaries.

In addition, interest on the subsidiary senior notes accrues daily and is payable into an account established by the trustee for the benefit of the bondholders (the Trustee Account). Failure to make daily payment on any day does not constitute an event of default so long as (a) no payment or other transfer by CCOH or any of its subsidiaries shall have been made on such day under the cash management sweep with Clear Channel and (b) on each semiannual interest payment date the aggregate amount of funds in the Trustee Account is equal to at least the aggregate amount of accrued and unpaid interest on the subsidiary senior notes.

The indenture governing the Series A Notes contains covenants that limit CCOH and its restricted subsidiaries ability to, among other things:

- incur or guarantee additional debt to persons other than Clear Channel and its subsidiaries (other than CCOH) or issue certain preferred stock;
- create liens on its restricted subsidiaries assets to secure such debt;
- create restrictions on the payment of dividends or other amounts to CCOH from its restricted subsidiaries that are not guarantors of the notes;
- enter into certain transactions with affiliates;
- merge or consolidate with another person, or sell or otherwise dispose of all or substantially all of its assets; and

sell certain assets, including capital stock of its subsidiaries, to persons other than Clear Channel and its subsidiaries (other than CCOH).

The indenture governing the Series A Notes does not include limitations on dividends, distributions, investments or asset sales.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The indenture governing the Series B Notes contains covenants that limit CCOH and its restricted subsidiaries ability to, among other things:

- incur or guarantee additional debt or issue certain preferred stock;
- redeem, repurchase or retire CCOH s subordinated debt;
- make certain investments;
- create liens on its or its restricted subsidiaries assets to secure debt;
- create restrictions on the payment of dividends or other amounts to it from its restricted subsidiaries that are not guarantors of the subsidiary senior notes;
- enter into certain transactions with affiliates;
- merge or consolidate with another person, or sell or otherwise dispose of all or substantially all of its assets;
- sell certain assets, including capital stock of its subsidiaries;
- designate its subsidiaries as unrestricted subsidiaries;
- pay dividends, redeem or repurchase capital stock or make other restricted payments; and
- purchase or otherwise effectively cancel or retire any of the Series B Notes if after doing so the ratio of (a) the outstanding aggregate principal amount of the Series A Notes to (b) the outstanding aggregate principal amount of the Series B Notes shall be greater than 0.250. This stipulation ensures, among other things, that as long as the Series A Notes are outstanding, the Series B Notes are outstanding.

The Series A Notes indenture and Series B Notes indenture restrict CCOH s ability to incur additional indebtedness but permit CCOH to incur additional indebtedness based on an incurrence test. In order to incur additional indebtedness under this test, CCOH s debt to adjusted EBITDA ratios (as defined by the indentures) must be lower than 6.5:1 and 3.25:1 for total debt and senior debt, respectively. The indentures contain certain other exceptions that allow CCOH to incur additional indebtedness. The Series B Notes indenture also permits CCOH to pay dividends from the proceeds of indebtedness or the proceeds from asset sales if its debt to adjusted EBITDA ratios (as defined by the indenture) are lower than 6.0:1 and 3.0:1 for total debt and senior debt, respectively. The Series A Notes indenture does not limit CCOH s ability to pay dividends. The Series B Notes indenture contains certain exceptions that allow CCOH to incur additional indebtedness and pay dividends, including a $500.0 million exception for the payment of dividends. CCOH was in compliance with these covenants as of December 31, 2010.

A portion of the proceeds of the subsidiary senior notes offering were used to (i) pay the fees and expenses of the offering, (ii) fund $50.0 million of the Liquidity Amount (the $50.0 million liquidity amount of the non-guarantor subsidiaries was satisfied) and (iii) apply $2.0 billion of the cash proceeds (which amount is equal to the aggregate principal amount of the Series B Notes) to repay an equal amount of indebtedness under Clear Channel s senior secured credit facilities. In accordance with the senior secured credit facilities, the $2.0 billion cash proceeds were applied ratably to the term loan A, term loan B, and both delayed draw term loan facilities, and within each such class, such prepayment was applied to remaining scheduled installments of principal.

The balance of the proceeds is available to CCOI for general corporate purposes. In this regard, all of the remaining proceeds could be used to pay dividends from CCOI to CCOH. In turn, CCOH could declare a dividend to its shareholders of which Clear Channel would receive its proportionate share. Payment of such dividends would not be prohibited by the terms of the subsidiary senior notes or any of the loan agreements or credit facilities of CCOI or CCOH.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Refinancing Transactions

Clear Channel announced on February 7, 2011 that it intends to offer, subject to market and customary conditions, $750 million in aggregate principal amount of priority guarantee notes due 2021 (the Notes) in a private offering that is exempt from registration under the Securities Act of 1933, as amended. Clear Channel intends to use the proceeds of the Notes together with cash on hand to repay $500 million of the indebtedness outstanding under its senior secured credit facilities, to repay at maturity $250 million in aggregate principal amount of its 6.25% senior notes due 2011, to pay fees and expenses incurred in connection with concurrent amendments to its senior secured credit facilities and its receivables based credit facility, the receipt of which is a condition to completion of the offering, and to pay fees and expenses in connection with the offering.

The concurrent amendments to its senior secured credit facilities and its receivables based credit facility would, among other things, permit Clear Channel to request future extensions of the maturities of its senior secured credit facilities, provide Clear Channel with greater flexibility in the use of its accordion provisions, provide Clear Channel with greater flexibility to incur new debt, provided that such new debt is used to pay down senior secured credit facility indebtedness, and provide greater flexibility for Clear Channel s indirect subsidiary, CCOH, and its subsidiaries to incur new debt (provided the incurrence of that new debt is otherwise permitted to be incurred by such subsidiaries).

The Notes and related guarantees will be offered only to qualified institutional buyers in reliance on the exemption from registration pursuant to Rule 144A under the Securities Act and to persons outside of the United States in compliance with Regulation S under the Securities Act. The Notes and the related guarantees have not been registered under the Securities Act, or the securities laws of any state or other jurisdiction, and may not be offered or sold in the United States without registration or an applicable exemption from the Securities Act and applicable state securities or blue sky laws and foreign securities laws.

This disclosure is for informational purposes only and shall not constitute an offer to sell nor the solicitation of an offer to buy the Notes or any other securities. The Notes offering is not being made to any person in any jurisdiction in which the offer, solicitation or sale is unlawful. Any offers of the Notes will be made only by means of a private offering circular.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Debt Repurchases, Tender Offers, Maturities and Other

Between 2008 and 2010, CC Investments, Inc. (CC Investments), CC Finco, LLC and Clear Channel Acquisition, LLC (previously known as CC Finco II, LLC), indirect wholly-owned subsidiaries of the Company, repurchased certain of Clear Channel s outstanding senior notes, senior cash pay notes and senior toggle notes through open market repurchases, privately negotiated transactions and tenders as shown in the table below. Notes repurchased and held by CC Investments, CC Finco, LLC and Clear Channel Acquisition, LLC are eliminated in consolidation.

(In thousands)	Post-Merger Periods Ended December 31,		
	2010	2009	2008
CC Investments			
Principal amount of debt repurchased	$ 185,185	$	$
Deferred loan costs and other	104		
Gain recorded in Other income (expense) net (2)	(60,289)		
Cash paid for repurchases of long-term debt	$ 125,000	$	$
CC Finco, LLC			
Principal amount of debt repurchased	$	$ 801,302	$ 102,241
Purchase accounting adjustments(1)		(146,314)	(24,367)
Deferred loan costs and other		(1,468)	
Gain recorded in Other income (expense) net (2)		(368,591)	(53,449)
Cash paid for repurchases of long-term debt	$	$ 284,929	$ 24,425
Clear Channel Acquisition, LLC			
Principal amount of debt repurchased(3)	$	$ 433,125	$
Deferred loan costs and other		(813)	
Gain recorded in Other income (expense) net (2)		(373,775)	
Cash paid for repurchases of long-term debt	$	$ 58,537	$

(1) Represents unamortized fair value purchase accounting discounts recorded as a result of the merger.
(2) CC Investments, CC Finco, LLC and Clear Channel Acquisition, LLC, repurchased certain of Clear Channel s senior notes, senior cash pay notes and senior toggle notes at a discount, resulting in a gain on the extinguishment of debt.
(3) Clear Channel Acquisition, LLC immediately cancelled these notes subsequent to the purchase.

During 2010, Clear Channel repaid its remaining 7.65% senior notes upon maturity for $138.8 million, including $5.1 million of accrued interest, with proceeds from its delayed draw term loan facility that was specifically designated for this purpose. Also during 2010, Clear Channel repaid its remaining 4.50% senior notes upon maturity for $240.0 million with available cash on hand.

During 2009, Clear Channel repaid the remaining principal amount of its 4.25% senior notes at maturity with a draw under the $500.0 million delayed draw term loan facility that was specifically designated for this purpose.

On November 24, 2008, Clear Channel announced that it commenced a cash tender offer to purchase its outstanding 7.65% Senior Notes due 2010. The tender offer and consent payment expired on December 23, 2008. The aggregate principal amount of 7.65% senior notes validly tendered and accepted for payment was $252.4 million. The Company recorded an aggregate gain on the extinguishment of debt of $74.7 million

in Other income (expense) net during the post-merger period as a result of this tender offer.

Clear Channel repurchased $639.2 million aggregate principal amount of the AMFM Operating Inc. 8% senior notes pursuant to a tender offer and consent solicitation in connection with the merger. The remaining 8% senior

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

notes were repaid at maturity on November 1, 2008. The aggregate loss on the extinguishment of debt recorded in Other income (expense) net in 2008 as a result of the tender offer for the AMFM Operating Inc. 8% senior notes was $8.0 million.

On August 7, 2008, Clear Channel announced that it commenced a cash tender offer and consent solicitation for its outstanding $750.0 million principal amount of 7.65% senior notes due 2010. The tender offer and consent payment expired on September 9, 2008. The aggregate principal amount of 7.65% senior notes validly tendered and accepted for payment was $363.9 million. Clear Channel recorded a $21.8 million loss in Other income (expense) net during the pre-merger period as a result of the tender.

Clear Channel terminated its cross currency swaps on July 30, 2008 by paying the counterparty $196.2 million from available cash on hand.

On January 15, 2008, Clear Channel repaid its 4.625% senior notes at their maturity for $500.0 million with proceeds from its bank credit facility. On June 15, 2008, Clear Channel repaid its 6.625% Senior Notes at their maturity for $125.0 million with available cash on hand.

Future maturities of long-term debt at December 31, 2010 are as follows:

(In thousands)		
2011	$	885,087
2012		292,819
2013		459,778
2014		3,775,159
2015		254,173
Thereafter		15,563,671
Total [(1)]	$	21,230,687

(1) Excludes a negative purchase accounting fair value adjustment of $623.3 million, which is amortized through interest expense over the life of the underlying debt obligations.

NOTE 8 - FINANCIAL INSTRUMENTS

Interest Rate Swaps

The Company s $2.5 billion notional amount interest rate swap agreement is designated as a cash flow hedge and the effective portion of the gain or loss on the swap is reported as a component of other comprehensive income. Ineffective portions of a cash flow hedging derivative s change in fair value are recognized currently in earnings. No ineffectiveness was recorded in earnings related to this interest rate swap.

The Company entered into its swap agreement to effectively convert a portion of its floating-rate debt to a fixed basis, thus reducing the impact of interest rate changes on future interest expense. The Company assesses at inception, and on an ongoing basis, whether its interest rate swap agreement is highly effective in offsetting changes in the interest expense of its floating rate debt. A derivative that is not a highly effective hedge does not qualify for hedge accounting.

The Company continually monitors its positions with, and credit quality of, the financial institution which is counterparty to its interest rate swap. The Company may be exposed to credit loss in the event of nonperformance by its counterparty to the interest rate swap. However, the Company considers this risk to be low. If a derivative instrument no longer qualifies as a cash flow hedge, hedge accounting is discontinued and the gain or loss that was recorded in other comprehensive income is recognized currently in income.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

NOTE 9 FAIR VALUE MEASUREMENTS

The Company adopted FASB Statement No. 157, *Fair Value Measurements,* codified in ASC 820-10, on January 1, 2008 and began to apply its recognition and disclosure provisions to its financial assets and financial liabilities that are remeasured at fair value at least annually. ASC 820-10-35 establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

The Company s marketable equity securities and interest rate swap are measured at fair value on each reporting date.

The marketable equity securities are measured at fair value using quoted prices in active markets. Due to the fact that the inputs used to measure the marketable equity securities at fair value are observable, the Company has categorized the fair value measurements of the securities as Level 1. The fair value of these securities at December 31, 2010 and 2009 was $70.6 million and $38.9 million, respectively.

The swap agreement is valued using a discounted cash flow model that takes into account the present value of the future cash flows under the terms of the agreements by using market information available as of the reporting date, including prevailing interest rates and credit spread. Due to the fact that the inputs are either directly or indirectly observable, the Company classified the fair value measurement of the agreement as Level 2.

In accordance with ASC 815-20-35-9, as the critical terms of the swap and the floating-rate debt being hedged were the same at inception and remained the same during the current period, no ineffectiveness was recorded in earnings.

The fair value of the Company s $2.5 billion notional amount interest rate swap designated as a hedging instrument and recorded in Other long-term liabilities was $213.1 million at December 31, 2010.

As of December 31, 2009, the Company had an aggregate $6.0 billion notional amount of interest rate swap agreements with an aggregate fair value of $237.2 million recorded in Other long-term liabilities . In October of 2010, $3.5 billion notional amount of interest rate swap agreements matured.

The following table provides the beginning and ending accumulated other comprehensive loss and the current period activity related to the interest rate swap agreements:

(In thousands)		Accumulated other comprehensive loss
Balance at January 1, 2009	$	75,079
Other comprehensive loss		74,100
Balance at December 31, 2009		149,179
Other comprehensive income		15,112
Balance at December 31, 2010	$	134,067

NOTE 10 - COMMITMENTS AND CONTINGENCIES

The Company accounts for its rentals that include renewal options, annual rent escalation clauses, minimum franchise payments and maintenance related to displays under the guidance in ASC 840.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The Company considers its non-cancelable contracts that enable it to display advertising on buses, trains, bus shelters, etc. to be leases in accordance with the guidance in ASC 840-10. These contracts may contain minimum annual franchise payments which generally escalate each year. The Company accounts for these minimum franchise payments on a straight-line basis. If the rental increases are not scheduled in the lease, for example an increase based on the CPI, those rents are considered contingent rentals and are recorded as expense when accruable. Other contracts may contain a variable rent component based on revenue. The Company accounts for these variable components as contingent rentals and records these payments as expense when accruable.

The Company accounts for annual rent escalation clauses included in the lease term on a straight-line basis under the guidance in ASC 840-10. The Company considers renewal periods in determining its lease terms if at inception of the lease there is reasonable assurance the lease will be renewed. Expenditures for maintenance are charged to operations as incurred, whereas expenditures for renewal and betterments are capitalized.

The Company leases office space, certain broadcasting facilities, equipment and the majority of the land occupied by its outdoor advertising structures under long-term operating leases. The Company accounts for these leases in accordance with the policies described above.

The Company s contracts with municipal bodies or private companies relating to street furniture, billboards, transit and malls generally require the Company to build bus stops, kiosks and other public amenities or advertising structures during the term of the contract. The Company owns these structures and is generally allowed to advertise on them for the remaining term of the contract. Once the Company has built the structure, the cost is capitalized and expensed over the shorter of the economic life of the asset or the remaining life of the contract.

Certain of the Company s contracts contain penalties for not fulfilling its commitments related to its obligations to build bus stops, kiosks and other public amenities or advertising structures. Historically, any such penalties have not materially impacted the Company s financial position or results of operations.

As of December 31, 2010, the Company s future minimum rental commitments under non-cancelable operating lease agreements with terms in excess of one year, minimum payments under non-cancelable contracts in excess of one year, and capital expenditure commitments consist of the following:

(In thousands)	Non-Cancelable Operating Leases	Non-Cancelable Contracts	Capital Expenditure Commitments
2011	$ 369,012	$ 541,186	$ 48,059
2012	316,789	419,836	28,501
2013	291,769	351,403	15,486
2014	257,064	307,978	7,395
2015	249,459	281,004	4,344
Thereafter	1,325,325	624,004	3,322
Total	$ 2,809,418	$ 2,525,411	$ 107,107

Rent expense charged to continuing operations for the years ended December 31, 2010 and 2009 was $1.10 billion and $1.13 billion, respectively. Rent expense charged to continuing operations for the post-merger period from July 31, 2008 to December 31, 2008 and the pre-merger period from January 1, 2008 to July 30, 2008 was $526.6 million and $755.4 million, respectively.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The Company and its subsidiaries are currently involved in certain legal proceedings arising in the ordinary course of business and, as required, the Company has accrued its estimate of the probable costs for resolution of those claims for which the occurrence of loss is probable and the amount can be reasonably estimated. These estimates have been developed in consultation with counsel and are based upon an analysis of potential results, assuming a combination of litigation and settlement strategies. It is possible, however, that future results of operations for any particular period could be materially affected by changes in the Company s assumptions or the effectiveness of its strategies related to these proceedings.

In 2006, two of the Company s operating businesses (L&C Outdoor Ltda. (L&C) and Publicidad Klimes Sao Paulo Ltda. (Klimes), respectively) in the Sao Paulo, Brazil market received notices of infraction from the state taxing authority, seeking to impose a value added tax (VAT) on such businesses, retroactively for the period from December 31, 2001 through January 31, 2006. The taxing authority contends that the Company s businesses fall within the definition of communication services and as such are subject to the VAT.

The Company has filed petitions to challenge the imposition of this tax against each of its businesses, which are proceeding separately. The Company s challenge for L&C was unsuccessful at the first administrative level, but successful at the second administrative level. The state taxing authority filed an appeal to the third and final administrative level, which required consideration by a full panel of 16 administrative law judges. On September 27, 2010, the Company received an unfavorable ruling at this final administrative level concluding that the VAT applied to L&C and intends to appeal this ruling to the judicial level. The Company has filed a petition to have the case remanded to the second administrative level for consideration of the reasonableness of the amount of the penalty assessed against it. The amounts allegedly owed by L&C are approximately $9.3 million in taxes, approximately $18.6 million in penalties and approximately $25.8 million in interest (as of December 31, 2010 at an exchange rate of .58).

The Company s challenge for Klimes was unsuccessful at the first administrative level, and denied at the second administrative level on or about September 24, 2009. On January 5, 2011, the administrative law judges at the third administrative level published a ruling that the VAT applies to Klimes as well but did reduce the penalty assessed by the state taxing authority. With the penalty reduction, the amounts allegedly owed by Klimes are approximately $10.5 million in taxes, approximately $5.2 million in penalties and approximately $16.1 million in interest (as of December 31, 2010 at an exchange rate of .58). In mid-January 2011, the taxing authority filed an extraordinary appeal to the third administrative level, asking that it reconsider the decision to reduce the penalty assessed against Klimes. The president of the third administrative level must decide whether to accept that appeal before it can proceed. Based on the Company s review of the law in similar cases in other Brazilian states, the Company has not accrued any costs related to these claims and believes the occurrence of loss is not probable.

In various areas in which the Company operates, outdoor advertising is the object of restrictive and, in some cases, prohibitive zoning and other regulatory provisions, either enacted or proposed. The impact to the Company of loss of displays due to governmental action has been somewhat mitigated by Federal and state laws mandating compensation for such loss and constitutional restraints.

Certain acquisition agreements include deferred consideration payments based on performance requirements by the seller typically involving the completion of a development or obtaining appropriate permits that enable the Company to construct additional advertising displays. At December 31, 2010, the Company believes its maximum aggregate contingency, which is subject to performance requirements by the seller, is approximately $35.0 million. As the contingencies have not been met or resolved as of December 31, 2010, these amounts are not recorded. If future payments are made, amounts will be recorded as additional purchase price.

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NOTE 11 - GUARANTEES

At December 31, 2010, the Company guaranteed $39.9 million of credit lines provided to certain of its international subsidiaries by a major international bank. Most of these credit lines related to intraday overdraft facilities covering participants in the Company s European cash management pool. As of December 31, 2010, no amounts were outstanding under these agreements.

As of December 31, 2010, the Company had outstanding commercial standby letters of credit and surety bonds of $128.4 million and $46.9 million, respectively. Letters of credit in the amount of $15.7 million are collateral in support of surety bonds and these amounts would only be drawn under the letters of credit in the event the associated surety bonds were funded and the Company did not honor its reimbursement obligation to the issuers.

These letters of credit and surety bonds relate to various operational matters including insurance, bid, and performance bonds as well as other items.

NOTE 12 - INCOME TAXES

The operations of the Company are included in a consolidated federal income tax return filed by CCMH. However, for financial reporting purposes, the Company s provision for income taxes has been computed on the basis that the Company files separate consolidated federal income tax returns with its subsidiaries.

Significant components of the provision for income tax benefit (expense) are as follows:

(In thousands)	Post-Merger			Pre-Merger
	Year ended December 31, 2010	Year ended December 31, 2009	Period from July 31 through December 31, 2008	Period from January 1 through July 30, 2008
Current - Federal	$ (4,534)	$ 104,539	$ 100,578	$ 6,535
Current - foreign	(41,388)	(15,301)	(15,755)	(24,870)
Current - state	(5,278)	(13,109)	(8,094)	(8,945)
Total current benefit (expense)	(51,200)	76,129	76,729	(27,280)
Deferred - Federal	211,137	366,024	555,679	(145,149)
Deferred - foreign	(3,859)	30,399	17,762	12,662
Deferred - state	3,902	20,768	46,453	(12,816)
Total deferred benefit (expense)	211,180	417,191	619,894	(145,303)
Income tax benefit (expense)	$ 159,980	$ 493,320	$ 696,623	$ (172,583)

Current tax expense of $51.2 million was recorded for 2010 as compared to current tax benefits of $76.1 million for 2009 primarily due to the Company s ability to carry back certain net operating losses in 2009 to prior years. On November 6, 2009, the Worker, Homeownership, and Business Assistance Act of 2009 (the Act) was enacted into law. The Act amended Section 172 of the Internal Revenue Code to allow net operating losses realized in a tax year ended after December 31, 2007 and beginning before January 1, 2010 to be carried back for up to five years (such losses were previously limited to a two-year carryback). This change allowed the Company to recognize current tax benefits of $126.4 million in 2009 related to the projected Federal income tax refund available upon the carryback of its fiscal 2009 taxable losses to prior periods. The 2009 Federal income tax return and related net operating loss carryback claim was filed in 2010 and resulted in an actual refund of

approximately $132.3 million, which was received in 2010.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

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For the year ended December 31, 2010, deferred tax benefits decreased $206.0 million as compared to 2009 primarily due to larger impairment charges recorded in 2009 related to tax deductible intangibles. This decrease was partially offset by increases in deferred tax expense in 2009 as a result of the deferral of certain discharge of indebtedness income, for income tax purposes, resulting from the reacquisition of business indebtedness, as provided by the American Recovery and Reinvestment Act of 2009 signed into law on February 17, 2009. In addition, in 2010 the Company recorded additional deferred tax expenses related to excess tax over book depreciation resulting from the accelerated tax depreciation provisions available under the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 that was signed into law on December 17, 2010.

Current tax benefits for 2009 increased $26.7 million compared to the full year for 2008 primarily due to the Company s ability to carry back certain net operating losses to prior years as mentioned above.

For the year ended December 31, 2009, deferred tax benefits decreased $57.4 million as compared to 2008 primarily due to larger impairment charges recorded in 2008 related to the tax deductible intangibles. This decrease was partially offset by increases in deferred tax expense in 2009 as a result of the deferral of certain discharge of indebtedness income, for income tax purposes, resulting from the reacquisition of business indebtedness, as provided by the American Recovery and Reinvestment Act of 2009 signed into law on February 17, 2009.

Significant components of the Company s deferred tax liabilities and assets as of December 31, 2010 and 2009 are as follows:

(In thousands)	2010	2009
Deferred tax liabilities:		
Intangibles and fixed assets	$ 2,202,702	$ 2,074,925
Long-term debt	523,846	530,519
Foreign	55,102	62,661
Investments in nonconsolidated affiliates	48,880	36,955
Other investments	7,012	18,067
Other	18,488	17,310
Total deferred tax liabilities	2,856,030	2,740,437
Deferred tax assets:		
Accrued expenses	123,225	117,041
Unrealized gain in marketable securities	22,229	22,126
Net operating losses	658,352	365,208
Bad debt reserves	12,244	11,055
Deferred Income	700	717
Other	32,241	27,701
Total gross deferred tax assets	848,991	543,848
Less: Valuation allowance	17,434	3,854
Total deferred tax assets	831,557	539,994
Net deferred tax liabilities	$ 2,024,473	$ 2,200,443

Included in the Company s net deferred tax liabilities are $25.7 million and $19.6 million of current net deferred tax assets for 2010 and 2009, respectively. The Company presents these assets in Other current assets on its consolidated balance sheets. The remaining $2.0 billion and $2.2 billion of net deferred tax liabilities for 2010 and 2009, respectively, are presented in Deferred tax liabilities on the consolidated balance sheets.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For the year ended December 31, 2009, the Company recorded certain impairment charges that are not deductible for tax purposes and resulted in a reduction of deferred tax liabilities of approximately $379.6 million. Additional decreases in net deferred tax liabilities are a result of increases in deferred tax assets associated with current period net operating losses. The Company is able to utilize those losses through either carrybacks to prior years as a result of the November 6, 2009 tax law change and expanded loss carryback provisions provided by the Worker, Homeownership, and Business Assistance Act of 2009 (the Act) or based on our expectations as to future taxable income from deferred tax liabilities that reverse in the relevant carryforward period for those net operating losses that cannot be carried back. Increases in 2009 deferred tax liabilities of approximately $338.9 million are a result of the deferral of certain discharge of indebtedness income, for income tax purposes, resulting from the reacquisition of business indebtedness (see Note 7). These gains are allowed to be deferred for tax purposes and recognized in future periods beginning in 2014 through 2019, as provided by the American Recovery and Reinvestment Act of 2009 signed into law on February 17, 2009.

At December 31, 2010, net deferred tax liabilities include a deferred tax asset of $27.5 million relating to stock-based compensation expense under ASC 718-10, *Compensation Stock Compensation*. Full realization of this deferred tax asset requires stock options to be exercised at a price equaling or exceeding the sum of the grant price plus the fair value of the option at the grant date and restricted stock to vest at a price equaling or exceeding the fair market value at the grant date. Accordingly, there can be no assurance that the stock price of the Company s common stock will rise to levels sufficient to realize the entire tax benefit currently reflected in its balance sheet.

The deferred tax liability related to intangibles and fixed assets primarily relates to the difference in book and tax basis of acquired FCC licenses, permits and tax deductible goodwill created from the Company s various stock acquisitions. In accordance with ASC 350-10, *Intangibles Goodwill and Other*, the Company does not amortize FCC licenses and permits. As a result, this deferred tax liability will not reverse over time unless the Company recognizes future impairment charges related to its FCC licenses, permits and tax deductible goodwill or sells its FCC licenses or permits. As the Company continues to amortize its tax basis in its FCC licenses, permits and tax deductible goodwill, the deferred tax liability will increase over time.

The reconciliation of income tax computed at the U.S. Federal statutory tax rates to income tax benefit (expense) is:

	Post-Merger						Pre-Merger	
(In thousands)	Year Ended December 31, 2010		Year Ended December 31, 2009		Period from July 31 through December 31, 2008		Period from January 1 through July 30, 2008	
	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent
Income tax benefit (expense) at statutory rates	$ 217,991	35%	$ 1,589,825	35%	$ 2,008,040	35%	$ (205,108)	35%
State income taxes, net of Federal tax benefit	(1,376)	0%	7,660	0%	38,359	1%	(21,760)	4%
Foreign taxes	(30,967)	(5%)	(92,648)	(2%)	(95,478)	(2%)	29,606	(5%)
Nondeductible items	(3,165)	(0%)	(3,317)	(0%)	(1,591)	(0%)	(2,464)	0%
Changes in valuation allowance and other estimates	(16,263)	(3%)	54,579	1%	(53,877)	(1%)	32,256	(6%)
Impairment charge		0%	(1,050,535)	(23%)	(1,194,182)	(21%)		
Other, net	(6,240)	(1%)	(12,244)	(0%)	(4,648)	(0%)	(5,113)	1%
	$ 159,980	26%	$ 493,320	11%	$ 696,623	12%	$ (172,583)	29%

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

A tax benefit was recorded for the year ended December 31, 2010 of 26%. Foreign income before income taxes was approximately $40.8 million for 2010. The effective tax rate for 2010 was impacted by the Company s inability to benefit from tax losses in certain foreign jurisdictions due to the uncertainty of the ability to utilize those losses in future years. In addition, the Company recorded a valuation allowance of $13.6 million against deferred tax assets in foreign jurisdictions due to the uncertainty of the ability to realize those assets in future periods.

A tax benefit was recorded for the year ended December 31, 2009 of 11%. The effective tax rate for the post-merger period was primarily impacted by the goodwill impairment charges which are not deductible for tax purposes (see Note 4). In addition, the Company was unable to benefit tax losses in certain foreign jurisdictions due to the uncertainty of the ability to utilize those losses in future years. These impacts were partially offset by the reversal of valuation allowances on certain net operating losses as a result of the Company s ability to utilize those losses through either carrybacks to prior years or based on our expectations as to future taxable income from deferred tax liabilities that reverse in the relevant carryforward period for those net operating losses that cannot be carried back.

A tax benefit was recorded for the post-merger period ended December 31, 2008 of 12% and reflects the Company s ability to recover a limited amount of the Company s prior period tax liabilities through certain net operating loss carrybacks. The effective tax rate for the 2008 post-merger period was primarily impacted by the goodwill impairment charges which are not deductible for tax purposes (see Note 4). In addition, the Company recorded a valuation allowance on certain net operating losses generated during the post-merger period that are not able to be carried back to prior years. The effective tax rate for the 2008 pre-merger period was primarily impacted by the tax effect of the disposition of certain radio broadcasting assets and investments.

The remaining Federal net operating loss carryforwards of $1.805 billion expires in various amounts from 2020 to 2030.

The Company continues to record interest and penalties related to unrecognized tax benefits in current income tax expense. The total amount of interest accrued at December 31, 2010 and 2009 was $87.5 million and $70.7 million, respectively. The total amount of unrecognized tax benefits and accrued interest and penalties at December 31, 2010 and 2009 was $312.9 million and $308.3 million, respectively, of which $269.3 million and $301.5 million is included in Other long-term liabilities , and $35.3 million and $6.8 million is included in Accrued Expenses on the Company s consolidated balance sheets. In addition, $8.3 million of unrecognized tax benefits are recorded net with the Company s deferred tax assets for its net operating losses as opposed to being recorded in Other long-term liabilities at December 31, 2010. The total amount of unrecognized tax benefits at December 31, 2010 and 2009 that, if recognized, would impact the effective income tax rate is $312.9 million and $308.3 million, respectively.

(In thousands)	Years Ended December 31,	
Unrecognized Tax Benefits	2010	2009
Balance at beginning of period	$ 237,517	$ 214,309
Increases for tax position taken in the current year	5,222	3,347
Increases for tax positions taken in previous years	22,990	33,892
Decreases for tax position taken in previous years	(20,705)	(4,629)
Decreases due to settlements with tax authorities	(14,462)	(203)
Decreases due to lapse of statute of limitations	(5,093)	(9,199)
Balance at end of period	$ 225,469	$ 237,517

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The Company and its subsidiaries file income tax returns in the United States Federal jurisdiction and various state and foreign jurisdictions. During 2010, the Company settled the Internal Revenue Service (IRS) exam for the tax years 2005 and 2006. As a result of the settlement the Company will pay approximately $14.3 million, inclusive of interest, to the IRS and reverse the excess liabilities related to the effectively settled tax years. In addition, the Company effectively settled several state and foreign tax audits that resulted in a decrease to the liabilities recorded. During 2009, the Company increased its unrecognized tax benefits for issues in prior years as a result of certain ongoing examinations in both the United States and certain foreign jurisdictions. In addition, the Company released certain unrecognized tax benefits in certain foreign jurisdictions as a result of the lapse of the statute of limitations for certain tax years. The IRS is currently auditing the Company s 2007 and 2008 pre and post merger periods. The company is currently in U.S. Tax Court for the 2003 and 2004 tax years. The Company expects to settle the 2003 and 2004 U.S. tax years and certain state examinations during the next twelve months. Substantially all material state, local, and foreign income tax matters have been concluded for years through 2000.

NOTE 13 - MEMBER S INTEREST

In connection with the merger, CCMH issued approximately 23.6 million shares of Class A common stock, approximately 0.6 million shares of Class B common stock and approximately 59.0 million shares of Class C common stock. Every holder of shares of Class A common stock is entitled to one vote for each share of Class A common stock. Every holder of shares of Class B common stock is entitled to a number of votes per share equal to the number obtained by dividing (a) the sum of the total number of shares of Class B common stock outstanding as of the record date for such vote and the number of shares of Class C common stock outstanding as of the record date for such vote by (b) the number of shares of Class B common stock outstanding as of the record date for such vote. Except as otherwise required by law, the holders of outstanding shares of Class C common stock are not entitled to any votes upon any matters presented to our stockholders.

Except with respect to voting as described above, and as otherwise required by law, all shares of Class A common stock, Class B common stock and Class C common stock have the same powers, privileges, preferences and relative participating, optional or other special rights, and the qualifications, limitations or restrictions thereof, and are identical to each other in all respects.

Vesting of certain Clear Channel stock options and restricted stock awards was accelerated upon closing of the merger. As a result, except for certain executive officers and holders of certain options that could not, by their terms, be cancelled prior to their stated expiration date, holders of stock options received cash or, if elected, an amount of CCMH Class A common stock, in each case equal to the intrinsic value of the awards based on a market price of $36.00 per share. Holders of restricted stock awards received $36.00 per share in cash or a share of CCMH Class A common stock per share of Clear Channel restricted stock. Approximately $39.2 million of share-based compensation was recognized in the pre-merger period as a result of the accelerated vesting of the stock options and restricted stock awards.

Dividends

The Company has not paid cash dividends since its formation and its ability to pay dividends is subject to restrictions should it seek to do so in the future. Clear Channel s debt financing arrangements include restrictions on its ability to pay dividends thereby limiting the Company s ability to pay dividends.

Prior to the merger, Clear Channel s Board of Directors declared a quarterly cash dividend of $93.4 million on December 3, 2007 and paid on January 15, 2008.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Share-Based Compensation

Stock Options

The Company does not have any compensation plans under which it grants stock awards to employees. Prior to the merger, Clear Channel granted options to purchase its common stock to its employees and directors and its affiliates under its various equity incentive plans typically at no less than the fair value of the underlying stock on the date of grant. These options were granted for a term not exceeding ten years and were forfeited, except in certain circumstances, in the event the employee or director terminated his or her employment or relationship with Clear Channel or one of its affiliates. Prior to acceleration, if any, in connection with the merger, these options vested over a period of up to five years. All equity incentive plans contained anti-dilutive provisions that permitted an adjustment of the number of shares of Clear Channel s common stock represented by each option for any change in capitalization.

CCMH has granted options to purchase its Class A common stock to certain key executives under its equity incentive plan at no less than the fair value of the underlying stock on the date of grant. These options are granted for a term not to exceed ten years and are forfeited, except in certain circumstances, in the event the executive terminates his or her employment or relationship with the Company or one of its affiliates. Approximately one-third of the options granted vest based solely on continued service over a period of up to five years with the remainder becoming eligible to vest over five years if certain predetermined performance targets are met. The equity incentive plan contains antidilutive provisions that permit an adjustment of the number of shares of the CCMH s common stock represented by each option for any change in capitalization.

The Company accounts for its share-based payments using the fair value recognition provisions of ASC 718-10. The fair value of the portion of options that vest based on continued service is estimated on the grant date using a Black-Scholes option-pricing model and the fair value of the remaining options which contain vesting provisions subject to service, market and performance conditions is estimated on the grant date using a Monte Carlo model. Expected volatilities were based on implied volatilities from traded options on peer companies, historical volatility on peer companies stock, and other factors. The expected life of the options granted represents the period of time that the options granted are expected to be outstanding. CCMH used historical data to estimate option exercises and employee terminations within the valuation model. The risk free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods equal to the expected life of the option. The following assumptions were used to calculate the fair value of these options:

	2010	2009
Expected volatility	58%	58%
Expected life in years	5.0 7.0	5.5 7.5
Risk-free interest rate	2.03% 2.74%	2.30% 3.26%
Dividend yield	0%	0%

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The following table presents a summary of CCMH s stock options outstanding at and stock option activity during the year ended December 31, 2010 (Price reflects the weighted average exercise price per share):

(In thousands, except per share data)	Options	Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding, January 1, 2010	6,160	$ 35.15		
Granted(1)	520	10.00		
Exercised		n/a		
Forfeited	(319)	36.00		
Expired	(41)	52.44		
Outstanding, December 31, 2010(2)	6,320	32.93	7.7 years	$ 0
Exercisable	1,086	29.09	6.9 years	0
Expect to Vest	2,303	30.84	7.9 years	0

(1) The weighted average grant date fair value of options granted during the year ended December 31, 2010 was $4.79 per share.

(2) Non-cash compensation expense has not been recorded with respect to 3.4 million shares as the vesting of these options is subject to performance conditions that have not yet been determined probable to meet.

A summary of CCMH s unvested options and changes during the year ended December 31, 2010 is presented below:

(In thousands, except per share data)	Options	Weighted Average Grant Date Fair Value
Unvested, January 1, 2010	5,352	$ 19.29
Granted	520	4.79
Vested	(319)	14.02
Forfeited	(319)	16.75
Unvested, December 31, 2010	5,234	18.32

Restricted Stock Awards

Prior to the merger, Clear Channel granted restricted stock awards to its employees and directors and its affiliates under its various equity incentive plans. These common shares held a legend which restricted their transferability for a term of up to five years and were forfeited, except in certain circumstances, in the event the employee or director terminated his or her employment or relationship with Clear Channel prior to the lapse of the restriction. Recipients of the restricted stock awards were entitled to all cash dividends as of the date the award was granted.

At July 30, 2008, there were 2,692,904 outstanding Clear Channel restricted stock awards held by Clear Channel s employees and directors under Clear Channel s equity incentive plans. Pursuant to the Merger Agreement, 1,876,315 of the Clear Channel restricted stock awards became fully vested and converted into the right to receive, with respect to each share of such restricted stock, a cash payment or equity in CCMH equal to the

value of $36.00 per share. The remaining 816,589 shares of Clear Channel restricted stock were converted on a one-for-one basis into restricted stock of CCMH. These converted shares continue to vest in accordance with their original terms. Following the merger, Clear Channel restricted stock automatically ceased to exist and is no longer outstanding, and, following the receipt of the cash payment or equity, if any, described above, the holders thereof no longer have any rights with respect to Clear Channel restricted stock.

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CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

On July 30, 2008, CCMH granted 555,556 shares of restricted stock to each its Chief Executive Officer and Chief Financial Officer under its 2008 Incentive Plan. The aggregate fair value of these awards was $40.0 million, based on the market value of a share of the CCMH s Class A common stock on the grant date, or $36.00 per share. These Class A common shares are subject to restrictions on their transferability, which lapse ratably over a term of five years and will be forfeited, except in certain circumstances, in the event the employee terminates his employment or relationship with CCMH prior to the lapse of the restriction. The following table presents a summary of the CCMH s restricted stock outstanding at and restricted stock activity during the year ended December 31, 2010 (Price reflects the weighted average share price at the date of grant):

(In thousands, except per share data)

	Awards	Price
Outstanding January 1, 2010	1,377	$ 36.00
Granted		n/a
Vested (restriction lapsed)	(466)	36.00
Forfeited	(16)	36.00
Outstanding, December 31, 2010	895	36.00

On August 23, 2010, Mark P. Mays tendered 200,000 shares to CCMH for purchase at $36.00 per share pursuant to a put option included in his amended employment agreement.

CCOH Share-Based Awards

CCOH Stock Options

The Company s subsidiary, CCOH, grants options to purchase shares of its Class A common stock to its employees and directors and its affiliates under its equity incentive plan typically at no less than the fair market value of the underlying stock on the date of grant. These options are granted for a term not exceeding ten years and are forfeited, except in certain circumstances, in the event the employee or director terminates his or her employment or relationship with CCOH or one of its affiliates. These options vest over a period of up to five years. A portion of the options granted vest based solely on continued service over a period of up to four years with the remainder becoming eligible to vest over five years if certain predetermined performance targets are met. The incentive stock plan contains anti-dilutive provisions that permit an adjustment of the number of shares of CCOH s common stock represented by each option for any change in capitalization.

CLEAR CHANNEL CAPITAL I, LLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The fair value of each option awarded on CCOH common stock is estimated on the date of grant using a Black-Scholes option-pricing model. Expected volatilities are based on implied volatilities from traded options on CCOH s stock, historical volatility on CCOH s stock, and other factors. The expected life of options granted represents the period of time that options granted are expected to be outstanding. CCOH uses historical data to estimate option exercises and employee terminations within the valuation model. CCOH includes estimated forfeitures in its compensation cost and updates the estimated forfeiture rate through the final vesting date of awards. The risk free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods equal to the expected life of the option. The following assumptions were used to calculate the fair value of CCOH s options on the date of grant:

	Post-Merger			Pre-Merger
	Years Ended December 31,		Period from July 31 through December 31,	Period from January 1 through July 30,
	2010	2009	2008	2008
Expected volatility	58%	58%	n/a	27%
Expected life in years	5.5 7.0	5.5 7.0	n/a	5.5 7.0
Risk-free interest rate	1.38% 3.31%	2.31% 3.25%	n/a	3.24% 3.38%
Dividend yield	0%	0%	n/a	0%

The following table presents a summary of CCOH s stock options outstanding at and stock option activity during the year ended December 31, 2010 (Price reflects the weighted average exercise price per share):

(In thousands, except per share data)	Options	Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding, January 1, 2010	9,040	$ 17.48		
Granted [1]	2,092	9.87		
Exercised [2]	(178)	5.26		
Forfeited	(798)	13.03		
Expired	(1,115)	23.72		
Outstanding, December 31, 2010	9,041	15.55	6.2 years	$ 23,799
Exercisable	4,652	19.80	4.1 years	3,195
Expect to vest	3,890	11.20	8.4 years	