NEXSTAR BROADCASTING GROUP INC
Form 10-K
March 16, 2006
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
for the fiscal year ended December 31, 2005

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
for the transition period from ______ to ______.

Commission File Number: 000-50478

NEXSTAR BROADCASTING GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware	**23-3083125**
(State of Organization or Incorporation)	**(IRS Employer Identification No.)**
909 Lake Carolyn Parkway, Suite 1450	**(972) 373-8800**
Irving, Texas 75039	

(Address of Principal Executive Offices, including Zip Code)	(Registrant s Telephone Number, Including Area Code)

Securities Registered Pursuant to Section 12(b) of the Act: None

Securities Registered Pursuant to Section 12(g) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Class A Common Stock, $0.01 par value per share	The Nasdaq Stock Market s National Market

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

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 it was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of June 30, 2005, the aggregate market value of the voting stock held by non-affiliates of the Registrant was $48,510,065.

As of January 31, 2006, the Registrant had outstanding:

14,289,310 shares of Class A Common Stock;

13,411,588 shares of Class B Common Stock; and

662,529 shares of Class C Common Stock.

Documents Incorporated By Reference

Portions of the Proxy Statement for the Registrant s 2006 Annual Meeting of Stockholders will be filed with the Commission within 120 days after the close of the Registrant s fiscal year and incorporated by reference in Part III.

TABLE OF CONTENTS

Table of Contents

General

As used in this Annual Report on Form 10-K and unless the context indicates otherwise, (1) Nexstar refers to Nexstar Broadcasting Group, Inc. and its consolidated subsidiaries; (2) Nexstar Broadcasting refers to Nexstar Broadcasting, Inc., our indirect subsidiary, (formerly known as Nexstar Finance, Inc.); (3) Nexstar Finance Holdings refers to Nexstar Finance Holdings, Inc., our wholly-owned subsidiary; (4) Nexstar Group refers to our predecessor, Nexstar Broadcasting Group, L.L.C. but not its direct or indirect subsidiaries; (5) Mission refers to Mission Broadcasting, Inc.; (6) Quorum refers to Quorum Broadcast Holdings, LLC; (7) ABRY refers to Nexstar Broadcasting Group, Inc. s principal stockholder, ABRY Partners, LLC and its affiliated funds; and (8) all references to we, our, ours, and us refer to Nexstar.

Nexstar has time brokerage agreements, shared services agreements and joint sales agreements (which we generally refer to as local service agreements) relating to the television stations owned by Mission, but does not own any of the equity interests in Mission. For a description of the relationship between Nexstar and Mission, see Certain Relationships and Related Transactions.

On December 30, 2003, we completed the acquisition of all the direct and indirect subsidiaries of Quorum. Quorum owned and operated 11 television stations and provided management, sales or other services to an additional 5 stations, primarily in medium-sized markets. The Quorum acquisition was structured as a merger of Quorum s direct subsidiaries with and into us. The merger constituted a tax-free reorganization and has been accounted for as a merger under common control in a manner similar to pooling of interests. Accordingly, our consolidated financial statements herein have been restated to include the financial results of all of the Quorum subsidiaries for all periods prior to 2004. Common control existed because ABRY Partners, LLC, our principal stockholder, through its various funds both before and after the merger, held more than 50% of the voting ownership of both Nexstar and Quorum. This conclusion was based on the guidance in Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards No. 141 Business Combinations (SFAS No. 141) and FASB Emerging Issues Task Force Issue 02-05 Definition of Common Control in relation to SFAS No. 141.

Additionally, on December 30, 2003, Mission completed a merger with VHR Broadcasting, Inc. and its subsidiaries (VHR) and with Mission Broadcasting of Amarillo, Inc. (Mission of Amarillo). Prior to December 30, 2003, Quorum provided sales or other services under local service agreements with VHR and Mission of Amarillo that were substantially similar to Nexstar s local service agreements with Mission. Upon completion of the Quorum acquisition and the Mission mergers, Nexstar became a party to these local service agreements as successor to the Quorum subsidiaries and Mission became a party to such agreements as the successor to VHR and Mission of Amarillo.

In the context of describing ownership of television stations in a particular market, the term duopoly refers to owning or deriving the majority of the economic benefit, through local service agreements, from two or more stations in a particular market. For more information on how we derive economic benefit from a duopoly, see Item 1. Business and Item 13. Certain Relationships and Related Transactions.

There are 210 generally recognized television markets, known as Designated Market Areas, or DMAs, in the United States. DMAs are ranked in size according to various factors based upon actual or potential audience. DMA rankings contained in this Annual Report on Form 10-K are from *Investing in Television Market Report 2005 4th Edition*, as published by BIA Financial Network, Inc.

Unless the context indicates otherwise: (1) the term station or commercial station means a television broadcast station and does not include non-commercial television stations, cable program services or networks (for example, CNN, MTV and ESPN) or stations that do not meet the minimum Nielsen reporting standards; and (2) the term independent describes a commercial television station that is not affiliated with the ABC, CBS, NBC, Fox, WB, PAX or UPN television networks.

Table of Contents

Reference is made in this Annual Report on Form 10-K to the following trademarks/tradenames which are owned by the third parties referenced in parentheses: *Seinfeld* (Columbia Tristar Television Distribution, a unit of Sony Pictures) and *Entertainment Tonight* (Paramount Distribution, a division of Viacom Inc.).

Cautionary Note Regarding Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements other than statements of historical fact are forward-looking statements for purposes of federal and state securities laws, including: any projections or expectations of earnings, revenue, financial performance, liquidity and capital resources or other financial items; any assumptions or projections about the television broadcasting industry, any statements of our plans, strategies and objectives for our future operations, performance, liquidity and capital resources or other financial items; any statements concerning proposed new products, services or developments; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing. Forward-looking statements may include the words may, will, should, could, would, predicts, potential, continue, expects, anticipates, future, intends, plans, believes, words.

Although we believe that the expectations reflected in any of our forward-looking statements are reasonable, actual results could differ from a projection or assumption in any of our forward-looking statements. Our future financial position and results of operations, as well as any forward-looking statements are subject to change and inherent risks and uncertainties discussed under Item 1A. Risk Factors elsewhere in this Annual Report on Form 10-K and in our other filings with the Securities and Exchange Commission. The forward-looking statements made in this Annual Report on Form 10-K are made only as of the date hereof, and, we do not have or undertake any obligation to update any forward-looking statements to reflect subsequent events or circumstances unless otherwise required by law.

Available Information

We file annual, quarterly and current reports, proxy statements and other information with the Securities and Exchange Commission (SEC). You may read and copy any reports, statements and other information filed by us at the SEC s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549-0102. Please call (800) SEC-0330 for further information on the Public Reference Room. The SEC maintains an Internet web site that contains reports, proxy and information statements and other information regarding issuers, including us, that file electronically with the SEC. The address for the SEC s web site is http://www.sec.gov.

We make available, free of charge, through our investor relations web site our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, statements of changes in beneficial ownership of securities, and amendments to those reports and statements as soon as reasonably practicable after they are filed with the SEC. The address for our web site is http://www.nexstar.tv.

Table of Contents

PART I

Item 1. Business
Overview

We are a television broadcasting company focused exclusively on the acquisition, development and operation of television stations in medium-sized markets in the United States, primarily markets that rank from 50 to 175, as reported by A.C. Nielsen Company. As of December 31, 2005, we owned and operated 29 stations, and provided sales or other services to an additional 17 stations that are owned by Mission and other entities. In 16 of the 27 markets that we serve, we own, operate, program or provide sales and other services to more than one station. We refer to these markets as duopoly markets. We have more than doubled the size of our portfolio since January 1, 2003, having acquired 15 stations and begun providing services to 11 additional stations. The stations that we own, operate, program or provide sales and other services to are in markets located in New York, Pennsylvania, Illinois, Indiana, Missouri, Texas, Louisiana, Arkansas, Alabama, Montana and Maryland. These stations are diverse in their network affiliations: 42 have primary affiliation agreements with one of the four major networks 12 with NBC, 13 with Fox, 9 with ABC, and 8 with CBS. Three of the remaining four stations have agreements with UPN and one is an independent station.

We believe that medium-sized markets offer significant advantages over large-sized markets, most of which result from a lower level of competition. First, because there are fewer well-capitalized acquirers with a medium-market focus, we have been successful in purchasing stations on more favorable terms than acquirers of large market stations. Second, in many of our markets only three or four other local commercial television stations exist. As a result, we achieve lower programming costs than stations in larger markets because the supply of quality programming exceeds the demand. Lastly, we believe that the stations we own, operate, program or provide sales and other services to are better managed than many of our competitors stations. By providing equity incentives, we have been able to attract and retain station general managers with experience in larger markets who employ marketing and sales techniques that are not typically utilized in our markets.

We seek to grow our revenue and broadcast cash flow by increasing the audience and revenue shares of the stations we own, operate, program or provide sales and other services to. We strive to increase the audience share of the stations by creating a strong local broadcasting presence based on highly-rated local news, local sports coverage and active community sponsorship. We seek to improve revenue share by employing and supporting a high-quality local sales force that leverages the stations strong local brand and community presence with local advertisers. Additionally, we have further improved broadcast cash flow by maintaining strict control over operating and programming costs. The benefits achieved through these initiatives are magnified in our duopoly markets by broadcasting the programming of multiple networks, capitalizing on multiple sales forces and achieving an increased level of operational efficiency. As a result of our operational enhancements, we expect revenue from the stations we have acquired or begun providing services to in the last four years to grow faster than that of our more mature stations.

We completed our initial public offering on November 28, 2003. Concurrent with our offering, we completed a corporate reorganization whereby our predecessor, Nexstar Broadcasting Group, L.L.C., and certain direct and indirect subsidiaries of Nexstar Broadcasting Group, L.L.C. merged with and into us. Nexstar Broadcasting Group, L.L.C. was organized as a limited liability company on December 12, 1996 in the State of Delaware and commenced operations on April 15, 1997.

On December 30, 2003, we completed the acquisition of all of the direct and indirect subsidiaries of Quorum. Quorum owned and operated 11 television stations and provided sales or other services to an additional 5 stations, primarily in medium-sized markets. The Quorum acquisition was structured as a merger of Quorum s direct subsidiaries with and into us. The merger constituted a tax-free reorganization and has been accounted for as a merger under common control in a manner similar to pooling of interests. Accordingly, our consolidated financial statements herein have been restated to include the financial results of all of the Quorum subsidiaries for all periods prior to 2004.

Our principal offices are at 909 Lake Carolyn Parkway, Suite 1450, Irving, TX 75039. Our telephone number is (972) 373-8800 and our website is http://www.nexstar.tv.

Operating Strategy

We seek to generate revenue and broadcast cash flow growth through the following strategies:

Develop Leading Local Franchises. Each of the stations that we own, operate, program, or provide sales and other services to creates a highly recognizable local brand, primarily through the quality of local news programming and community presence. Based on internally generated analysis, we believe that in approximately two-thirds of our markets that feature local newscasts produced by Nexstar, we rank among the top two stations in local news viewership. Strong local news typically generates higher ratings among attractive demographic profiles and enhances audience loyalty, which may result in higher ratings for programs both preceding and following the news. High ratings and strong community identity make the stations that we own, operate, program, or provide sales and other services to more attractive to local advertisers. For the year ended December 31, 2005, we earned approximately one-third of our advertising revenue from spots aired during local news programming. Our stations and the stations we provide services to currently provide approximately 552 hours per week of local news programming. Extensive local sports coverage and active sponsorship of community events further differentiate us from our competitors and strengthen our community relationships and our local advertising appeal.

Emphasize Local Sales. We employ a high-quality local sales force in each of our markets to increase revenue from local advertisers by capitalizing on our investment in local programming. We believe that local advertising is attractive because our sales force is more effective with local advertisers, giving us a greater ability to influence this revenue source. Additionally, local advertising has historically been a more stable source of revenue than national advertising for television broadcasters. For the year ended December 31, 2005, the percentage of Nexstar s and Mission s consolidated spot revenue, excluding political revenue, from local advertising was 68.6%. In most of our markets we have increased the size and quality of our local sales force. We also invest in our sales efforts by implementing comprehensive training programs and employing a sophisticated inventory tracking system to help maximize advertising rates and the amount of inventory sold in each time period.

Operate Duopoly Markets. Owning or providing services to more than one station in a given market enables us to broaden our audience share, enhance our revenue share and achieve significant operating efficiencies. Duopoly markets broaden audience share by providing programming from multiple networks with different targeted demographics. These markets increase revenue share by capitalizing on multiple sales forces. Additionally, we achieve significant operating efficiencies by consolidating physical facilities, eliminating redundant management and leveraging capital expenditures between stations. We derived approximately 72% of our net broadcast revenue for the year ended December 31, 2005 from our duopoly markets.

Maintain Strict Cost Controls. We emphasize strict controls on operating and programming costs in order to increase broadcast cash flow. We continually seek to identify and implement cost savings at each of our stations and the stations we provide services to and our overall size benefits each station with respect to negotiating favorable terms with programming suppliers and other vendors. By leveraging our size and corporate management expertise, we are able to achieve economies of scale by providing programming, financial, sales and marketing support to our stations and the stations we provide services to. Due to the significant negotiating leverage afforded by limited competition in our markets, Nexstar and Mission on a combined basis reduced the cash broadcast payments as a percentage of net broadcast revenue for the years ended December 31, 2005 and 2004, as compared to the previous three years. Our and Mission s cash broadcast payments were 4.7%, 4.7%, 6.4%, 6.3%, and 7.5% of net broadcast revenue for the years ended December 31, 2005, 2004, 2003, 2002 and 2001, respectively.

Capitalize on Diverse Network Affiliations. We currently own, operate, program, or provide sales and other services to a balanced portfolio of television stations with diverse network affiliations, including NBC, CBS,

Table of Contents

ABC, Fox and UPN affiliated stations which represented approximately 34.1%, 28.5%, 16.6%, 20.2%, and 0.6%, respectively, of our 2005 net broadcast revenue. The networks provide these stations with quality programming and numerous sporting events such as NBA basketball, Major League baseball, NFL football, NCAA sports, PGA golf and the Olympic Games. Because network programming and ratings change frequently, the diversity of our station portfolio s network affiliations reduces our reliance on the quality of programming from a single network.

Attract and Retain High Quality Management. We seek to attract and retain station general managers with proven track records in larger television markets by providing equity incentives not typically offered by other station operators in our markets. Our station general managers have been granted stock options and have an average of over 20 years of experience in the television broadcasting industry.

Acquisition Strategy

We selectively pursue acquisitions of television stations primarily in markets ranking from 50 to 175, where we believe we can improve revenue and cash flow through active management. Since January 1, 2003, we have more than doubled the number of stations that we own, operate and provide sales and other services to, having acquired 15 stations and contracted to provide services to 11 additional stations. When considering an acquisition, we evaluate the target audience share, revenue share, overall cost structure and proximity to our regional clusters. Additionally, we seek to acquire or enter into local service agreements with stations to create duopoly markets.

Relationship with Mission

Through various local service agreements with Mission, we currently provide sales, programming and other services to 15 television stations that are owned and operated by Mission. Mission is 100% owned by an independent third party. We do not own Mission or any of its television stations. In order for both us and Mission to comply with Federal Communications Commission (FCC) regulations, Mission maintains complete responsibility for and control over programming, finances, personnel and operations of its stations. However, as a result of our guarantee of the obligations incurred under Mission s senior credit facility and our arrangements under local service agreements and purchase option agreements with Mission, we are deemed under accounting principles generally accepted in the United States of America (U.S. GAAP) to have a controlling financial interest in Mission. As a result of our controlling financial interest in Mission under U.S. GAAP and in order to present fairly our financial position, results of operations and cash flows, we consolidate the financial position, results of operations and cash flows of Mission with us as if Mission were a wholly-owned entity.

Table of Contents

The Stations

The following chart sets forth general information about the stations we owned, operated, programmed or provided sales and other services to as of December 31, 2005:

Market Rank[1]	Market	Station	Affiliation	Status[2]	Commercial Stations in Market[3]	FCC License Expiration Date
8	Washington, DC/Hagerstown, MD[4]	WHAG	NBC	O&O		[8]
54	Wilkes Barre-Scranton, PA	WBRE	NBC	O&O	6	8/1/07
		WYOU	CBS	LSA		8/1/07
57	Little Rock-Pine Bluff, AR	KARK	NBC	O&O	7	[8]
77	Springfield, MO	KOLR	CBS	LSA	7	[8]
		KSFX[5]	Fox	O&O		[8]
79	Rochester, NY	WROC	CBS	O&O	4	6/1/07
		WUHF	Fox	LSA		6/1/07
81	Shreveport, LA	KTAL	NBC	O&O	6	8/1/06
82	Champaign-Springfield-Decatur, IL	WCIA	CBS	O&O	6	[8]
		WCFN	UPN	O&O		[8]
100	Evansville, IN	WTVW	Fox	O&O	5	[8]
104	Ft. Smith-Fayetteville-Springdale-Rogers, AR	KFTA/ KNWA[6]	NBC	O&O	6	[8]
106	Ft. Wayne, IN	WFFT	Fox	O&O	4	[8]
117	Peoria-Bloomington, IL	WMBD	CBS	O&O	5	[8]
		WYZZ	Fox	LSA		[8]
131	Amarillo, TX	KAMR	NBC	O&O	6	8/1/06
		KCIT	Fox	LSA		8/1/06
		KCPN-LP		LSA		8/1/06
133	Rockford, IL	WQRF	Fox	O&O	4	[8]
		WTVO	ABC	LSA		[8]
135	Monroe, LA-El Dorado, AR	KARD	Fox	O&O	6	[8]
140	Beaumont-Port Arthur, TX	KBTV	NBC	O&O	4	8/1/06
142	Erie, PA	WJET	ABC	O&O	4	8/1/07
		WFXP	Fox	LSA		8/1/07
144	Wichita Falls, TX-Lawton, OK	KFDX	NBC	O&O	5	8/1/06
		KJTL	Fox	LSA		8/1/06
		KJBO-LP	UPN	LSA		8/1/06
145	Joplin, MO-Pittsburg, KS	KSNF	NBC	O&O	4	[8]
		KODE	ABC	LSA		[8]
146	Lubbock, TX	KLBK	CBS	O&O	5	8/1/06
		KAMC	ABC	LSA		8/1/06
150	Terre Haute, IN	WTWO	NBC	O&O	3	[8]
		WFXW[7]	Fox	LSA		[8]
159	Odessa-Midland, TX	KMID	ABC	O&O	6	8/1/06
164	Abilene-Sweetwater, TX	KTAB	CBS	O&O	5	8/1/06
		KRBC	NBC	LSA		8/1/06
166	Utica, NY	WFXV	Fox	O&O	4	6/1/07
		WPNY-LP	UPN	O&O		6/1/07
		WUTR	ABC	LSA		6/1/07
171	Billings, MT	KSVI	ABC	O&O	4	4/1/06[8]
		KHMT	Fox	LSA		4/1/06[8]
172	Dothan, AL	WDHN	ABC	O&O	3	[8]
197	San Angelo, TX	KSAN	NBC	LSA	4	8/1/06
		KLST	CBS	O&O		8/1/06
201	St. Joseph, MO	KQTV	ABC	O&O	1	[8]

(1)

Market rank refers to ranking the size of the Designated Market Area (DMA) in which the station is located in relation to other DMAs. Source: *Investing in Television Market Report 2005 4th Edition,* as published by BIA Financial Network, Inc.

(2) O&O refers to stations that we own and operate. LSA, or local service agreement, is the general term we use to refer to a contract under which we provide services to a station owned and/or operated by an independent third party. Local service agreements include time brokerage agreements, shared services agreements, joint sales agreements and outsourcing agreements. For further information regarding the LSAs to which we are party, see Certain Transactions.

(3) The term commercial station means a television broadcast station and excludes non-commercial stations, religious stations, cable program services or networks. Source: *Investing in Television Market Report 2005 4th Edition,* as published by BIA Financial Network, Inc.

(4) Although WHAG is located within the Washington, DC DMA, its signal does not reach the entire Washington, DC metropolitan area. WHAG serves the Hagerstown, MD sub-market within the DMA.

(5) Effective January 17, 2005, KDEB changed its call letters to KSFX.

(6) KFTA/KNWA is treated as one station since KNWA is a satellite station rebroadcasting the same programming as KFTA.

(7) Effective June 1, 2005, WBAK changed its call letters to WFXW.

(8) Application for renewal of license timely was submitted to the FCC. Under the FCC s rules, a license expiration date automatically is extended pending review of and action on the renewal application by the FCC.

Table of Contents

Industry Background

Industry Overview

All television stations in the country are grouped by A.C. Nielsen Company, a national audience measuring service, into 210 generally recognized television markets, known as designated market areas (DMAs), that are ranked in size according to various metrics based upon actual or potential audience. Each DMA is an exclusive geographic area consisting of all counties in which the home-market commercial stations receive the greatest percentage of total viewing hours. A.C. Nielsen periodically publishes data on estimated audiences for the television stations in the various television markets throughout the country. The estimates are expressed in terms of a rating, which is a station s percentage of the total potential audience in the market, or a share, which is the station s percentage of the audience actually watching television. A.C. Nielsen provides this data on the basis of local television households and selected demographic groupings in the market. A.C. Nielsen uses two methods to determine a station s ratings. In larger geographic markets, A.C. Nielsen uses a combination of meters connected directly to selected television sets and weekly diaries of television viewing, while in smaller markets A.C. Nielsen uses only weekly diaries.

Whether or not a station is affiliated with one of the four major networks (NBC, ABC, CBS or Fox) has a significant impact on the composition of the station s revenue, expenses and operations. A typical network affiliate receives a significant part of its programming including prime-time hours from the network. This programming, along with cash payments for some NBC, ABC and CBS affiliates, is provided to the affiliate by the network in exchange for a substantial majority of the advertising time during network programs. The network then sells this advertising time and retains the revenue. The affiliate retains the revenue from the remaining advertising time sold during network programs and from advertising time sold during non-network programs.

Broadcast television stations compete for advertising revenue primarily with other commercial broadcast television stations, cable television systems, direct broadcast satellite (DBS) systems, and, to a lesser extent, with newspapers, radio stations and cable system operators serving the same market. Non-commercial, religious and Spanish-language broadcasting stations in many markets also compete with commercial stations for viewers. In addition, the Internet and other leisure activities may draw viewers away from commercial television stations.

Television Broadcasting History

Commercial television broadcasting began in the United States on a regular basis in the 1940s. There are a limited number of channels available for broadcasting in any one geographic area. Television stations can be distinguished by the frequency on which they broadcast. Television stations that broadcast over the very high frequency or VHF band (channels 2-13) of the spectrum generally have some competitive advantage over television stations which broadcast over the ultra-high frequency or UHF band (channels above 13) of the spectrum because the former usually have better signal coverage and operate at a lower transmission cost. However, the improvement of UHF transmitters and receivers, the complete elimination from the marketplace of VHF-only receivers and the expansion of cable television systems have reduced the VHF signal advantage. In addition, any disparity between VHF and UHF is likely to diminish even further in the coming era of digital television.

Through the 1970s, network-affiliated television broadcasters enjoyed virtual dominance in viewership and television advertising revenue because network-affiliated stations competed only with each other in most local markets. Beginning in the 1980s and continuing through today, however, this level of dominance has changed as more local stations have been authorized by the FCC and marketplace choices expanded with the growth of independent stations, new networks such as UPN, WB and PAX, and cable and satellite television services.

Cable television systems, which grew at a rapid rate beginning in the early 1970s, were initially used to retransmit broadcast television programming to paying subscribers in areas with poor broadcast signal reception. In the aggregate, cable-originated programming has emerged as a significant competitor for viewers of broadcast

Table of Contents

television programming. With the increase in cable penetration, the advertising share of cable networks has increased. Notwithstanding these increases in cable viewership and advertising, over-the-air broadcasting remains the primary distribution system for mass market television advertising. Basic cable penetration (the percentage of television households which are connected to a cable system) ranges from 43% to 78%.

DBS systems have also rapidly increased their penetration rate in the last decade, reaching approximately 21% of U.S. households. DBS services provide nationwide distribution of video programming (including in some cases pay-per-view programming and programming packages unique to DBS) using small receiving dishes and digital transmission technologies. In November 2004, Congress passed the Satellite Home Viewer Extension and Reauthorization Act, which permits DBS operators to continue to distribute the signals of local television stations to subscribers in the stations local market areas, or local-into-local service, provided the DBS operator obtains carriage rights from the broadcast station.

In acquiring programming to supplement network programming, network affiliates compete with other broadcast stations in their markets. Cable systems generally do not compete with local stations for programming. In the past, the cost of programming increased dramatically, primarily because of an increase in the number of new independent stations and a shortage of desirable programming. Recently, however, program prices have stabilized as a result of increases in the supply of programming.

The FCC finalized its allotment of new advanced television channels to existing broadcast stations in the first half of 1998. Advanced television is a digital television (DTV) transmission system that delivers improved video and audio signals including high definition television and also has substantial multiplexing and data transmission capabilities. For each licensed television station, the FCC allocated a matching DTV channel. Stations were required to construct digital facilities according to a schedule set by Congress and the FCC based on the type of station and the size of market the station is located in. Television broadcasters will be required to cease non-digital broadcasting by February 17, 2009 and return one of their channels to the FCC.

Advertising Sales

General

Television station revenue is primarily derived from the sale of local and national advertising. Television stations compete for advertising revenue primarily with other broadcast television stations, radio stations, cable system operators and programmers, DBS systems and newspapers serving the same market.

All network-affiliated stations are required to carry advertising sold by their networks which reduces the amount of advertising time available for sale by stations. Our and Mission s stations sell the remaining advertising to be inserted in network programming and the advertising in non-network programming, retaining all of the revenue received from these sales. A national syndicated program distributor will often retain a portion of the available advertising time for programming it supplies in exchange for no fees or reduced fees charged to stations for such programming. These programming arrangements are referred to as barter programming.

Advertisers wishing to reach a national audience usually purchase time directly from the networks, or advertise nationwide on a case-by-case basis. National advertisers who wish to reach a particular region or local audience often buy advertising time directly from local stations through national advertising sales representative firms. Local businesses purchase advertising time directly from the stations local sales staff.

Advertising rates are based upon a number of factors, including:

- a program s popularity among the viewers that an advertiser wishes to target;
- the number of advertisers competing for the available time;
- the size and the demographic composition of the market served by the station;

the availability of alternative advertising media in the market area;

the effectiveness of the sales forces;

development of projects, features and programs that tie advertiser messages to programming; and

the level of spending commitment made by the advertiser.

Advertising rates are also determined by a station s overall ability to attract viewers in its market area, as well as the station s ability to attract viewers among particular demographic groups that an advertiser may be targeting. Advertising revenue is positively affected by strong local economies. Conversely, declines in advertising budgets of advertisers, particularly in recessionary periods, adversely affect the broadcast industry, and as a result may contribute to a decrease in the revenue of broadcast television stations.

Seasonality

Advertising revenue is positively affected by national and regional political election campaigns, and certain events such as the Olympic Games or the Super Bowl. The stations advertising revenue is generally highest in the second and fourth quarters of each year, due in part to increases in consumer advertising in the spring and retail advertising in the period leading up to, and including, the holiday season. In addition, advertising revenue is generally higher during even-numbered years resulting from political advertising and advertising aired during the Olympic Games.

Local Sales

Local advertising time is sold by each station s local sales staff who call upon advertising agencies and local businesses, which typically include car dealerships, retail stores and restaurants. Compared to revenue from national advertising accounts, revenue from local advertising is generally more stable and more predictable. We seek to attract new advertisers to television and to increase the amount of advertising time sold to existing local advertisers by relying on experienced local sales forces with strong community ties, producing news and other programming with local advertising appeal and sponsoring or co-promoting local events and activities. We place a strong emphasis on the experience of our local sales staff and maintain an on-going training program for sales personnel.

National Sales

National advertising time is sold through national sales representative firms which call upon advertising agencies, whose clients typically include automobile manufacturers and dealer groups, telecommunications companies, fast food franchisers, and national retailers (some of which may advertise locally).

Table of Contents

Network Affiliations

Each station that we own and operate, program or provide sales and other services to is affiliated with a network pursuant to an affiliation agreement, as described below:

Station