SALEM MEDIA GROUP, INC. /DE/
Form 10-Q
May 08, 2015

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 MARCH 31, 2015

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 000-26497

SALEM MEDIA GROUP, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE	**77-0121400**
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)	(I.R.S. EMPLOYER IDENTIFICATION NUMBER)
4880 SANTA ROSA ROAD	**93012**

CAMARILLO, CALIFORNIA (ZIP CODE)

(ADDRESS OF PRINCIPAL

EXECUTIVE OFFICES)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (805) 987-0400

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 ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.)

Yes x No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer," and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer (Do not check if a Smaller Reporting Company)	¨	Smaller Reporting Company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

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

Class A	Outstanding at May 1, 2015
Common Stock, $0.01 par value per share	19,865,605 shares

Class B	Outstanding at May 1, 2015
Common Stock, $0.01 par value per share	5,553,696 shares

SALEM MEDIA GROUP, INC.
INDEX

CERTAIN DEFINITIONS

Unless the context requires otherwise, all references in this report to “Salem” or the “company,” including references to Salem by “we” “us” “our” and “its” refer to Salem Media Group, Inc. and our subsidiaries.

NOTE REGARDING FORWARD-LOOKING STATEMENTS

Salem Media Group, Inc. (“Salem” or the “company,” including references to Salem by “we,” “us” and “our”) makes “forward-looking statements” from time to time in both written reports (including this report) and oral statements, within the meaning of federal and state securities laws. Disclosures that use words such as the company “believes,” “anticipates,” “estimates,” “expects,” “intends,” “will,” “may,” “intends,” “could,” “would,” “should” “seeks” “predicts,” or “plans” and sim are intended to identify forward-looking statements, as defined under the Private Securities Litigation Reform Act of 1995.

You should not place undue reliance on these forward-looking statements, which reflect our expectations based upon data available to the company as of the date of this report. Such statements are subject to certain risks and uncertainties that could cause actual results to differ materially from expectations. These risks, as well as other risks and uncertainties, are detailed in Salem’s reports on Forms 10-K, 10-Q and 8-K filed with or furnished to the Securities and Exchange Commission. Except as required by law, the company undertakes no obligation to update or revise any forward-looking statements made in this report. Any such forward-looking statements, whether made in this report or elsewhere, should be considered in context with the various disclosures made by Salem about its business. These projections and other forward-looking statements fall under the safe harbors of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

PART I – FINANCIAL INFORMATION

SALEM MEDIA GROUP, INC.

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

SALEM MEDIA GROUP, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except share and per share data)

	December 31, 2014 (Note 1)	**March 31, 2015 (Unaudited)**
ASSETS		
Current assets:		
Cash and cash equivalents	$ 33	$ **182**
Trade accounts receivable (net of allowances of $12,727 in 2014 and $11,919 in 2015)	34,781	**33,520**
Other receivables	3,546	**3,456**
Inventories (net of reserves of $1,227 in 2014 and $1,408 in 2015)	572	**641**
Prepaid expenses	5,580	**6,031**
Deferred income taxes	8,153	**8,153**
Assets held for sale	1,700	**1,700**
Total current assets	54,365	**53,683**
Notes receivable (net of allowances of $539 in 2014 and $499 in 2015)	228	**200**
Fair value of interest rate swap	475	**—**
Property and equipment (net of accumulated depreciation of $155,495 in 2014 and $157,364 in 2015)	99,227	**99,378**
Broadcast licenses	385,726	**386,302**
Goodwill	24,684	**24,690**
Other indefinite-lived intangible assets	833	**833**
Amortizable intangible assets (net of accumulated amortization of $34,130 in 2014 and $35,459 in 2015)	12,395	**11,780**
Deferred financing costs	3,166	**2,982**
Other assets	2,060	**2,505**
Total assets	$ 583,159	$ **582,353**
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 2,964	$ **5,801**
Accrued expenses	12,704	**15,104**
Accrued compensation and related expenses	8,777	**8,337**
Accrued interest	48	**43**
Deferred revenue	13,205	**13,069**
Income tax payable	154	**207**
Current portion of long-term debt and capital lease obligations	1,898	**593**
Total current liabilities	39,750	**43,154**
Long-term debt and capital lease obligations, less current portion	275,607	**273,642**
Fair value of interest rate swap	—	**945**
Deferred income taxes	49,109	**49,144**
Deferred revenue	10,576	**11,201**

Other liabilities	4,123	**1,059**
Total liabilities	379,165	**379,145**
Commitments and contingencies (Note 16)		
Stockholders' equity:		
Class A common stock, $0.01 par value; authorized 80,000,000 shares; 22,082,140 and 22,155,255 issued and 19,764,490 and 19,837,605 outstanding at December 31, 2014 and March 31, 2015, respectively	221	**222**
Class B common stock, $0.01 par value; authorized 20,000,000 shares; 5,553,696 issued and outstanding at December 31, 2014 and March 31, 2015, respectively	56	**56**
Additional paid-in capital	240,493	**241,058**
Accumulated deficit	(2,770)	**(4,122)**
Treasury stock, at cost (2,317,650 shares at December 31, 2014 and March 31, 2015)	(34,006)	**(34,006)**
Total stockholders' equity	203,994	**203,208**
Total liabilities and stockholders' equity	$ 583,159	**$ 582,353**

See accompanying notes

4

SALEM MEDIA GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Dollars in thousands, except share and per share data)

(Unaudited)

	Three Months Ended March 31,	
	2014	**2015**
Net broadcast revenue	$46,769	$**46,539**
Net digital media revenue	11,312	**10,791**
Net publishing revenue	4,263	**4,526**
Total net revenue	62,344	**61,856**
Operating expenses:		
Broadcast operating expenses, exclusive of depreciation and amortization shown below (including $359 and $361 for the three months ended March 31, 2014 and 2015, respectively, paid to related parties)	33,346	**33,917**
Digital media operating expenses, exclusive of depreciation and amortization shown below	8,850	**9,000**
Publishing operating expenses, exclusive of depreciation and amortization shown below	5,006	**4,497**
Unallocated corporate expenses exclusive of depreciation and amortization shown below (including $164 and $33 for the three months ended March 31, 2014 and 2015, respectively, paid to related parties)	5,064	**3,991**
Depreciation	3,129	**3,172**
Amortization	1,608	**1,329**
Change in the estimated fair value of contingent earn-out consideration	127	**118**
(Gain) loss on the sale or disposal of assets	(117)	**129**
Total operating expenses	57,013	**56,153**
Operating income	5,331	**5,703**
Other income (expense):		
Interest income	15	**1**
Interest expense	(3,779)	**(3,804)**
Change in the fair value of interest rate swap	(1,096)	**(1,420)**
Loss on early retirement of long-term debt	(8)	**(41)**
Net miscellaneous income and expenses	66	**7**
Income from operations before income taxes	529	**446**
Provision for income taxes	98	**151**
Net income	$431	$**295**
Basic earnings per share data:		
Basic earnings per share	$0.02	$**0.01**
Diluted earnings per share data:		
Diluted earnings per share	$0.02	$**0.01**
Distributions per share	$0.06	$**0.06**

Basic weighted average shares outstanding	25,064,982	**25,346,499**
Diluted weighted average shares outstanding	25,881,811	**25,921,118**

See accompanying notes

5

SALEM MEDIA GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

	Three Months Ended March 31, 2014	Three Months Ended March 31, 2015
OPERATING ACTIVITIES		
Net income from operations	$431	**$295**
Adjustments to reconcile net income from operations to net cash provided by operating activities:		
Non-cash stock-based compensation	603	**331**
Tax benefit related to stock options exercised	69	**60**
Depreciation and amortization	4,737	**4,501**
Amortization of bank loan fees	172	**158**
Accretion of discount on Term Loan B	46	**46**
Accretion of acquisition-related deferred payments and contingent consideration	214	**91**
Provision for bad debts	686	**385**
Deferred income taxes	(28)	**35**
Change in the fair value of interest rate swap	1,096	**1,420**
Change in the estimated fair value of contingent earn-out consideration	127	**118**
Loss on early retirement of long-term debt	8	**41**
(Gain) loss on the sale or disposal of assets	(117)	**129**
Changes in operating assets and liabilities:		
Accounts receivable	5,084	**5,870**
Prepaid expenses and other current assets	231	**(520)**
Accounts payable and accrued expenses	680	**(1,770)**
Deferred revenue	(3,364)	**(4,432)**
Other liabilities	(424)	**327**
Income taxes payable	49	**53**
Net cash provided by operating activities	10,300	**7,138**
INVESTING ACTIVITIES		
Cash paid for capital expenditures net of tenant improvement allowances	(2,935)	**(2,040)**
Capital expenditures reimbursable under tenant improvement allowances and non-cash transactions from trade agreements	(75)	**(767)**
Escrow deposits related to acquisitions	—	**(188)**
Purchases of broadcast assets and radio stations	(1,784)	**(1,235)**
Purchases of digital media businesses and assets	(2,899)	**(122)**
Purchases of publishing businesses and assets	(1,274)	**—**
Proceeds from the sale of assets	2	**—**
Other	129	**(245)**

Net cash used in investing activities	(8,836)	**(4,597**)
FINANCING ACTIVITIES		
Payments under Term Loan B	(2,250)	**(2,000**)
Proceeds from borrowings under Revolver	8,610	**8,414**
Payments under Revolver	(6,291)	**(9,715**)
Payments of costs related to bank credit facility	(4)	**—**
Payments of acquisition related contingent earn-out consideration	—	**(300**)
Proceeds from the exercise of stock options	467	**175**
Payments on capital lease obligations	(32)	**(30**)
Payment of cash distributions on common stock	(1,444)	**(1,647**)
Book overdraft	(307)	**2,711**
Net cash used in financing activities	(1,251)	**(2,392**)
Net increase in cash and cash equivalents	213	**149**
Cash and cash equivalents at the beginning of year	65	**33**
Cash and cash equivalents at end of period	278	**182**

See accompanying notes

6

SALEM MEDIA GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)

(Dollars in thousands)

(Unaudited)

Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Cash paid for interest, net of capitalized interest	$3,350	$3,512
Cash paid for income taxes	$8	$4
Other supplemental disclosures of cash flow information:		
Trade revenue	$1,686	$1,683
Trade expense	$1,387	$1,591
Non-cash investing and financing activities:		
Capital expenditures reimbursable under tenant improvement allowances	$75	$756
Non-cash capital expenditures for property & equipment acquired under trade agreements	$—	$11
Estimated present value of contingent earn-out consideration	$2,047	$158
Deferred payments due 2014 under asset purchase agreement	$200	$—
Present value of deferred cash payments (due 2015)	$2,392	$—
Present value of deferred cash payments (due 2016)	$2,289	$—

See accompanying notes

7

SALEM MEDIA GROUP, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. BASIS OF PRESENTATION

The accompanying Condensed Consolidated Financial Statements of Salem Media Group, Inc. (“Salem” “we,” “us,” “our” or the “company”) includes the company and all wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated.

Information with respect to the three months ended March 31, 2015 and 2014 is unaudited. The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by GAAP for complete financial statements. In the opinion of management, the unaudited interim financial statements contain all adjustments, consisting of normal recurring accruals, necessary for a fair presentation of the financial position, results of operations and cash flows of the company. The unaudited interim financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in the Annual Report for Salem filed on Form 10-K for the year ended December 31, 2014. Our results are subject to seasonal fluctuations. Therefore, the results of operations for the interim periods presented are not necessarily indicative of the results of operations for the full year.

The balance sheet at December 31, 2014 included in this report has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by GAAP.

Description of Business

Salem is a domestic multi-media company with integrated operations including radio broadcasting, digital media, and publishing. Effective as of February 19, 2015, we changed our name from Salem Communications Corporation to Salem Media Group, Inc. Salem was formed in 1986 as a California corporation and was reincorporated in Delaware in 1999. Our content is intended for audiences interested in Christian and family-themed programming and conservative news talk. We maintain a website at www.salemmedia.com.

Our foundational business is the ownership and operation of radio stations in large metropolitan markets. We also own and operate Salem Radio Network® (“SRN”), SRN News Network (“SNN”), Salem Music Network (“SMN”), Solid Gospel Network (“SGN”), Salem Media Representatives (“SMR”) and Vista Media Representatives (“VMR”). SRN, SNN, SMN and SGN are networks that develop, produce and syndicate a broad range of programming specifically targeted to Christian and family-themed talk stations, music stations and general News Talk stations throughout the United States, including Salem owned and operated stations. SMR, a national advertising sales firm with offices in 11 U.S. cities, specializes in placing national advertising on religious and other commercial radio stations. As of December 2014, we merged Vista Media Representatives (“VMR”), our national advertising sales firm established for non-Christian format stations, into SMR as our SMR and VMR sales teams consistently pursue advertising for all station formats.

Web based and digital content has been a significant growth area for Salem and continues to be a focus of future development. Salem Web Network™ (“SWN”) and our other web-based businesses provide Christian and conservative-themed content, audio and video streaming, and other resources digitally through the web. SWN’s web portals include Christian content websites: OnePlace.com, Christianity.com, Crosswalk.com®, GodVine.com, Jesus.org and BibleStudyTools.com. Our conservative opinion websites, collectively known as Townhall Media, include Townhall.com™, HotAir.com, Twitchy.com, HumanEvents.com and RedState.com. We also issue digital newsletters, including Eagle Financial Publications, that provide market analysis and investment advice for individual subscribers from financial commentators. Church product websites including WorshipHouseMedia.com, SermonSpice.com, and ChurchStaffing.com offer downloads and service platforms to pastors and other educators. Our web content is accessible through all of our radio station websites that feature content of interest to local listeners throughout the United States.

E-commerce sites include Salem Consumer Products (”SCP”), an e-commerce business that sells books, DVD’s and editorial content developed by our on-air personalities, and Eagle Wellness, an online site offering complimentary health advice and sales of nutritional products.

Our acquisition of Regnery Publishing on January 10, 2014, represented a major shift in our publishing operating segment. Regnery Publishing is a publisher of conservative books that was founded in 1947. Regnery has published dozens of bestselling books by leading conservative authors and personalities, including Ann Coulter, Newt Gingrich, Michelle Malkin, David Limbaugh, Ed Klein, Laura Ingraham, Mark Steyn and Dinesh D'Souza.

Our publishing operating segment also includes Salem Publishing™ and Xulon Press. Salem Publishing™ produces and distributes numerous Christian and conservative opinion print magazines, including*: Homecoming® The Magazine, YouthWorker Journal,*™ *Singing News®, FaithTalk Magazine,*™ and *Preaching Magazine*™. Through December 2014, we also printed and produced *Townhall Magazine*™. Xulon Press™ is a print-on-demand self-publishing service for Christian authors.

Variable Interest Entities

We account for entities qualifying as variable interest entities ("VIEs") in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 810, *Consolidation,* which requires VIEs to be consolidated by the primary beneficiary. The primary beneficiary is the entity that holds the majority of the beneficial interests in the VIE. A VIE is an entity for which the primary beneficiary's interest in the entity can change with variations in factors other than the amount of investment in the entity.

We may enter into Local Marketing Agreements ("LMAs") contemporaneously with entering an Asset Purchase Agreement ("APA") to acquire or sell a radio station. We may also enter into Time Brokerage Agreements ("TBAs"). Typically, both LMAs and TBAs are contractual agreements under which the station owner/licensee makes airtime available to a programmer/licensee in exchange for a fee and reimbursement of certain expenses. LMAs and TBAs are subject to compliance with the antitrust laws and the communications laws, including the requirement that the licensee must maintain independent control over the station and, in particular, its personnel, programming, and finances. The FCC has held that such agreements do not violate the communications laws as long as the licensee of the station receiving programming from another station maintains ultimate responsibility for, and control over, station operations and otherwise ensures compliance with the communications laws.

The requirements of FASB ASC Topic 810 may apply to entities under LMAs or TBAs, depending on the facts and circumstances related to each transaction. As of March 31, 2015, we did not consolidate any entities with which we entered into LMAs or TBAs under the guidance in FASB ASC Topic 810.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. Significant areas for which management uses estimates include: (1) asset impairments, including broadcasting licenses, goodwill and other indefinite-lived intangible assets; (2) income tax valuation allowances; (3) uncertain tax positions; (4) allowance for doubtful accounts; (5) inventory reserves; (6) reserves for royalty advances; (7) self-insurance reserves; (8) fair value of equity awards; (9) estimated lives for tangible and intangible assets; (10) fair value measurements; (11) contingency reserves; (12) probabilities associated with the potential for contingent earn-out consideration; and (13) sales returns and allowances. These estimates require the use of judgment as future events and the effect of these events cannot be predicted with certainty. The estimates will change as new events occur, as more experience is acquired and as more information is obtained. We evaluate and update our assumptions and estimates on an ongoing basis and we may consult outside experts to assist as considered necessary.

Reclassifications

Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation. These reclassifications include the change in composition of our operating segments based on our acquisition of Eagle Publishing during 2014 to conform to how our chief operating decision makers, who we define as a collective group of senior executives, assesses the performance of each operating segment and determines the appropriate allocations of resources to each segment. Refer to Note 17 – Segment Data in the notes to our consolidated financial statements for additional information.

NOTE 2. IMPAIRMENT OF GOODWILL AND OTHER INDEFINITE-LIVED INTANGIBLE ASSETS

Approximately 71% of our total assets as of March 31, 2015 consist of indefinite-lived intangible assets, such as broadcast licenses, goodwill and mastheads, the value of which depends significantly upon the operating results of our businesses. In the case of our radio stations, we would not be able to operate the properties without the related FCC license for each property. Broadcast licenses are renewed with the FCC every eight years for a nominal cost that is expensed as incurred. We continually monitor our stations' compliance with the various regulatory requirements. Historically, all of our broadcast licenses have been renewed at the end of their respective periods, and we expect that all broadcast licenses will continue to be renewed in the future. Accordingly, we consider our broadcast licenses to be indefinite-lived intangible assets in accordance with FASB ASC Topic 350, *Intangibles – Goodwill and Other*. Broadcast licenses account for approximately 94% of our indefinite-lived intangible assets. Goodwill and mastheads account for the remaining 6%. We do not amortize goodwill or other indefinite-lived intangible assets, but rather test for impairment at least annually or more frequently if events or circumstances indicate that an asset may be impaired.

We complete our annual impairment tests in the fourth quarter of each year. We believe that our estimate of the value of our broadcast licenses, mastheads, and goodwill is a critical accounting estimate as the value is significant in relation to our total assets, and our estimates incorporate variables and assumptions that are based on past experiences and judgment about future operating performance of our markets and business segments. If actual future results are less favorable than the assumptions and estimates we used, we are subject to future impairment charges, the amount of which may be material. The fair value measurements for our indefinite-lived intangible assets use significant unobservable inputs that reflect our own assumptions about the estimates that market participants would use in measuring fair value including assumptions about risk. The unobservable inputs are defined in FASB ASC Topic 820 *Fair Value Measurements and Disclosures,* as Level 3 inputs discussed in detail in Note 14. There were no indications of impairment present as of the period ending March 31, 2015.

NOTE 3. IMPAIRMENT OF LONG-LIVED ASSETS

We account for property and equipment in accordance with FASB ASC Topic 360-10, *Property, Plant and Equipment*. We periodically review our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. In accordance with authoritative guidance for impairment of long-lived assets, we must estimate the fair value of assets when events or circumstances indicate that they may be impaired. The fair value measurements for our long-lived assets use significant observable inputs that reflect our own assumptions about the estimates that market participants would use in measuring fair value including assumptions about risk. If actual future results are less favorable than the assumptions and estimates we used, we are subject to future impairment charges, the amount of which may be material. There were no indications of impairment present as of the period ending March 31, 2015.

NOTE 4. ACQUISITIONS AND RECENT TRANSACTIONS

During the three months ending March 31, 2015, we completed or entered into the following transactions:

Debt

On January 30, 2015, we repaid $2.0 million in principal on our current senior secured credit facility, consisting of a term loan of $300.0 million (“Term Loan B”) and paid interest due as of that date. We recorded a $15,000 pre-tax loss on the early retirement of long-term debt related to the unamortized discount and $27,000 in bank loan fees associated with the principal repayment.

Equity

On March 5, 2015 we announced a quarterly distribution in the amount of $0.0650 per share on Class A and Class B common stock. The quarterly distribution of $1.6 million was paid on March 31, 2015 to all Class A and Class B common stockholders of record as of March 17, 2015.

Acquisitions

On March 27, 2015, we completed the acquisition of radio station WDYZ-AM in Orlando, Florida for $1.3 million in cash. We began operating this station under an APA as of December 10, 2014. The accompanying condensed consolidated statements of operations reflect the operating results of this entity as of the APA date within the broadcast operating segment. We recorded goodwill of $3,200 associated with the going concern value of this radio station.

On February 6, 2015, we acquired the assets and assumed deferred subscription liabilities for Bryan Perry's Cash Machine and Bryan Perry's Premium Income financial publications ("Bryan Perry Newsletters"). We recorded the net assets acquired at their estimated fair value of $0.2 million. We paid no cash to the seller upon closing. Amounts payable to the seller in the future are contingent upon net subscriber revenues over the two year period from the closing date, of which we will pay the seller 50%. There is no minimum or maximum contractual amount. The estimated fair value of the contingent earn-out consideration was recorded at the present value of $0.2 million. The estimated fair value of the contingent earn-out consideration was determined using a probability weighted discounted cash flow model. The fair value measurement includes revenue forecasts which are a Level 3 measurement as discussed in Note 14. The fair value of the contingent earn-out consideration will be reviewed quarterly over the two year earn-out period based on actual subscription revenue earned as compared to the estimated subscription revenue used in our forecasts. Any changes in the estimated fair value of the contingent earn-out consideration will be reflected in our results of operations in future periods as they are identified. Changes in the fair value of the contingent earn-out consideration may materially impact and cause volatility in our future operating results. There were no changes in fair value or contingent earn-out estimates as of the quarter ending March 31, 2015. The accompanying condensed consolidated statements of operations reflect the operating results of these newsletters as of the closing date within our digital media operating segment. We recorded goodwill of $2,600 associated with the organizational systems and procedures in place at the time of our purchase.

Throughout the three month period ending March 31, 2015, we acquired domain names and other assets associated with our digital media operating segment for approximately $0.1 million in cash.

A summary of our business acquisitions and asset purchases for the three months ended March 31, 2015, none of which were individually or in the aggregate material to our Condensed Consolidated financial position as of the respective date of acquisition, is as follows:

Acquisition Date	Description	Total Cost (Dollars in thousands)
March 27, 2015	WDYZ-AM, Orlando, Florida (business acquisition)	$ 1,300
February 6, 2015	Bryan Perry's Cash Machine and Premium Income (business acquisition)	158
Various	Purchase of domain names and digital media assets (asset purchases)	122
		$ 1,580

The operating results of our business acquisitions and asset purchases are included in our consolidated results of operations from their respective closing date or the date that we began operating them under an LMA or TBA. Under the acquisition method of accounting as specified in FASB ASC Topic 805, *Business Combinations*, the total acquisition consideration is allocated to the assets acquired and liabilities assumed based on their estimated fair values as of the date of the transaction.

Estimates of the fair value include discounted estimated cash flows to be generated by the assets and their expected useful lives based on historical experience, market trends and any synergies believed to be achieved from the acquisition. Acquisitions may include contingent consideration, the fair value of which is estimated as of the acquisition date as the present value of the expected contingent payments as determined using weighted probabilities of the payment amounts. We may retain a third-party appraiser to estimate the fair value of the acquired net assets as of the acquisition date. As part of the valuation and appraisal process, the third-party appraiser prepares a report assigning estimated fair values to the various asset categories in our financial statements. These fair value estimates are subjective in nature and require careful consideration and judgment. Management reviews the third party reports for reasonableness of the assigned values. We believe that these valuations and analysis provide appropriate estimates of the fair value for net assets acquired.

Property and equipment are recorded at the estimated fair value and depreciated on a straight-line basis over their estimated useful lives. Finite-lived intangible assets are recorded at their estimated fair value and amortized on a straight-line basis over their estimated useful lives. Goodwill, which represents the organizational systems and procedures in place to ensure the effective operation of the entity, may also be recorded and tested for impairment. Costs associated with acquisitions, such as consulting and legal fees are expensed as incurred in corporate operating expenses. We recognized costs associated with acquisitions of $0.1 million during the three month period ending

March 31, 2015 compared to $0.2 million during the same period of the prior year, which are included in unallocated corporate expenses in the accompanying condensed consolidated statements of operations.

The total acquisition consideration is equal to the sum of all cash payments, the fair value of any deferred payments and promissory notes, and the present value of any estimated contingent earn-out consideration. We estimate the fair value of contingent earn-out consideration using a probability-weighted discounted cash flow model. The fair value measurement is based on significant inputs that are not observable in the market and thus represent a Level 3 measurement as defined in Note 14 -Fair Value Measurements. The following table summarizes the total acquisition consideration for the three months ended March 31, 2015:

Description	Total Consideration (Dollars in thousands)
Cash payments	$ 1,357
Escrow deposits paid in prior years	65
Net present value of estimated deferred payments due 2016	88
Net present value of estimated deferred payments due 2017	70
Total purchase price consideration	$ 1,580

The total acquisition consideration was allocated to the net assets acquired as follows:

	Net Broadcast Assets Acquired	**Net Digital Media Assets Acquired**	**Net Assets Acquired**
	(Dollars in thousands)		
Assets			
Property and equipment	$948	$ 10	$ 958
Broadcast licenses	349	—	349
Goodwill	3	3	6
Domain and brand names	—	192	192
Subscriber base and lists	—	522	522
Liabilities			
Deferred revenues	—	(447)	(447)
	$1,300	$ 280	$ 1,580

11

Pending Transactions

On February 20, 2015, we entered into an APA to acquire radio station WDDZ-AM in Pittsburg, Pennsylvania for $1.0 million in cash. The purchase is subject to the approval of the FCC and is expected to close in the second quarter of 2015.

On February 20, 2015, we entered into an APA to acquire radio station WDWD-AM in Atlanta, Georgia for $2.8 million in cash. The acquisition was approved by the FCC and closed on May 7, 2015.

NOTE 5. CONTINGENT EARN-OUT CONSIDERATION

Our acquisitions may include contingent consideration as part of the purchase price. The fair value of the contingent consideration is estimated as of the acquisition date based on the present value of the contingent payments to be made using a probability-weighted discounted cash flow model for probabilities of possible future payments. The unobservable inputs used in determining the fair value of the contingent consideration include assumptions as to the ability of the acquired businesses to meet the targets and discount rates used in the calculation. Should the actual results of the acquired business increase or decrease as compared to our estimates and assumptions, the fair value of the contingent consideration obligations would increase or decrease, up to the contracted limit, as applicable.

The fair value measurement includes revenue forecasts which are a Level 3 measurement as discussed in Note 14. Any changes in the estimated fair value of the contingent earn-out consideration, up to the contractual amounts as applicable, are reflected in our results of operations in the periods they are identified. Any changes in the estimated fair value of the contingent earn-out consideration may materially impact and cause volatility in our future operating results.

On February 6, 2015, we recorded an estimate of contingent earn-out consideration payable upon the realization of subscription revenue from our acquisition of the Bryan Perry Newsletters over a two year period. Using a probability-weighted discounted cash flow model, we estimated the fair value of the $171,000 contingent earn-out consideration at the present value of $158,000. There is no minimum or maximum contractual amount that we may be required to pay to the seller. We believe that our experience with digital publications and renewals provides a reasonable basis for our estimate. The fair value of the contingent earn-out consideration will be reviewed quarterly over the two year earn-out period based on actual subscription revenue earned as compared to the estimated subscription revenue used in our forecasts. Any changes in the estimated fair value of the contingent earn-out consideration will be reflected in our results of operations in future periods as they are identified. Changes in the fair value of the contingent earn-out consideration may materially impact and cause volatility in our future operating results. There were no changes in our estimates as of the quarter ending March 31, 2015.

On January 10, 2014, we recorded an estimate of contingent earn-out consideration payable upon achievement of certain revenue benchmarks over a three-year period related to our acquisition of Eagle Publishing, including Regnery Publishing, HumanEvents.com, RedState.com, Eagle Financial Publications and Eagle Wellness. Using a probability-weighted discounted cash flow model, we estimated the fair value of the $8.5 million total contingent earn-out consideration at the present value of $2.0 million as of the closing date. We have recorded a net increase of $0.5 million in the fair value of the contingent earn-out consideration associated with Eagle entities of which $85,000 is reflected in our results of operations for the three months ending March 31, 2015. The net increase reflects actual revenues earned by Eagle entities in excess of those estimated at the time of our projections. We will continue to review our estimates over the remaining earn-out period of two years. As of March 31, 2015, we have recorded actual liabilities due to Eagle of $0.9 million and we may pay up to an additional $6.0 million over the remaining earn-out period based on the achievement of certain revenue benchmarks. The estimated fair value of the contingent earn-out consideration is recorded at the present value of $1.8 million at March 31, 2015

On December 10, 2013, we recorded an estimate of contingent earn-out consideration payable upon achievement of page view milestones over a two-year period related to our acquisition of Twitchy.com. Using a probability-weighted discounted cash flow model, we estimated the fair value of the $1.2 million total contingent earn-out consideration at the present value of $0.6 million as of the closing date. We have recorded an increase of $0.4 million in the fair value of the contingent earn-out consideration associated with our December 2013 acquisition of Twitchy.com of which $33,000 is reflected in our results of operations for the three months ending March 31, 2015. The increase reflects actual page views in excess of those estimated at the time of our projections. We will continue to review our estimates over the remaining one-year earn-out period. As of March 31, 2015, we have paid $0.6 million in cash toward the contingent earn-out consideration and may pay up to an additional $0.7 million over the remaining earn-out period of 0.75 months based on the achievement of certain page view milestones established in the purchase agreement. The estimated fair value of the contingent earn-out consideration is recorded at the present value of $0.5 million at March 31, 2015.

Any changes in the estimated fair value of the contingent earn-out consideration, up to the contracted amount as applicable, will be reflected in our results of operations in future periods as they are identified. Changes in the fair value of the contingent earn-out consideration may materially impact and cause volatility in our future operating results.

The following table reflects the changes in the present value of our acquisition-related contingent earn-out consideration for the three months ended March 31, 2015:

	Three months ending March 31, 2015		
	Short-Term Accrued Expenses	**Long-Term Other Liabilities**	**Total**
	(dollars in thousands)		
Beginning Balance as of January 1, 2015	$1,575	$ 1,710	$3,285
Acquisitions	88	70	158
Accretion of acquisition-related contingent consideration	10	15	25
Change in the estimated fair value of contingent earn-out consideration	80	38	118
Reclassification of payments due in next 12 months to short-term	798	(798)	—
Payments	(300)	—	(300)
Ending Balance as of March 31, 2015	$2,251	$ 1,035	$3,286

NOTE 6. STOCK INCENTIVE PLAN

The company has one stock incentive plan. The Amended and Restated 1999 Stock Incentive Plan (the “Plan”) allows the company to grant stock options and restricted stock to employees, directors, officers and advisors of the company. A maximum of 5,000,000 shares are authorized under the Plan. Options generally vest over a four-year period and have a maximum term of five years from the vesting date. The Plan provides that vesting may be accelerated upon the occurrence of certain corporate transactions of the company. The Plan provides that the Board of Directors, or a committee appointed by the Board, has discretion, subject to certain limits, to modify the terms of outstanding options. We recognize non-cash stock-based compensation expense related to the estimated fair value of stock options granted in accordance with FASB ASC Topic 718, *Compensation—Stock Compensation*.

The following table reflects the components of stock-based compensation expense recognized in the Condensed Consolidated Statements of Operations for the three months ended March 31, 2014 and 2015:

	Three Months Ended March 31,	
	2014	2015
	(Dollars in thousands)	
Stock option compensation expense included in corporate expenses	$405	$228
Restricted stock shares compensation expense included in corporate expenses	—	1
Stock option compensation expense included in broadcast operating expenses	125	52
Stock option compensation expense included in digital media operating expenses	58	36
Stock option compensation expense included in publishing operating expenses	15	14
Total stock-based compensation expense, pre-tax	$603	$331
Tax provision for stock-based compensation expense	(241)	(132)
Total stock-based compensation expense, net of tax	$362	$199

Stock option and restricted stock grants

The Plan allows the company to grant stock options and shares of restricted stock to employees, directors, officers and advisors of the company. For grants of stock options, the option exercise price is set at the closing price of the company's common stock on the date of grant, and the related number of shares underlying the stock option is fixed at that point in time. The Plan also provides for grants of restricted stock. Eligible employees may receive stock options annually with the number of shares and type of instrument generally determined by the employee's salary grade and performance level. In addition, certain management and professional level employees typically receive a stock option grant upon commencement of employment. The Plan does not allow key employees and directors (restricted persons) to exercise options during pre-defined blackout periods. Employees may participate in plans established pursuant to Rule 10b5-1 under the Exchange Act that allow them to exercise options according to pre-established criteria.

We use the Black-Scholes valuation model to estimate the grant date fair value of stock options and restricted stock. The expected volatility reflects the consideration of the historical volatility of our stock as determined by the closing price over a six to ten year term that is generally commensurate with the expected term of the award. Expected dividends reflect the quarterly distributions authorized and declared on our Class A and Class B common stock as of the grant date. The expected term of the awards are based on evaluations of historical and expected future employee exercise behavior. The risk-free interest rates for periods within the expected term of the award are based on the U.S. Treasury yield curve in effect during the period the options were granted. We use historical data to estimate future forfeiture rates to apply against the gross amount of compensation expense determined using the valuation model.

The weighted-average assumptions used to estimate the fair value of the stock options and restricted stock awards using the Black-Scholes valuation model were as follows for the three months ended March 31, 2014 and 2015:

	Three Months Ended March 31,	
	2014	2015
Expected volatility	86.84%	52.37%
Expected dividends	2.51 %	4.28 %
Expected term (in years)	7.5	3.0
Risk-free interest rate	2.36 %	0.85 %

Stock option information with respect to the company's stock-based equity plans during the three months ended March 31, 2015 is as follows:

Options	Shares	Weighted Average Exercise Price	Weighted Average Grant Date Fair Value	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
	(Dollars in thousands, except weighted average exercise price and weighted average grant date fair value)				
Outstanding at January 1, 2015	1,816,204	$ 4.88	$ 3.39	4.8 years	$ 5,718
Granted	10,000	6.08	1.98		
Exercised	(73,115)	2.39	1.42		
Forfeited or expired	(37,837)	11.68	8.01		
Outstanding at March 31, 2015	1,715,252	$ 4.84	$ 3.36	4.8 years	$ 3,102
Exercisable at March 31, 2015	962,327	$ 5.13	$ 3.63	3.7 years	$ 1,559
Expected to Vest	714,905	$ 4.47	$ 3.01	6.3 years	$ 1,466

Non-employee directors of the company have been awarded restricted stock awards that vest one year from the date of issuance. These restricted stock awards contained transfer restrictions under which they could not be sold, pledged, transferred or assigned until the sooner of the fifth anniversary from the grant date or the day after the non-employee director is no longer a member of the company's board. The restricted stock awards were independent of option grants and were granted at no cost to the recipient other than applicable taxes owed by the recipient. The awards were considered issued and outstanding from the date of grant.

The fair values of shares of restricted stock awards are determined based on the closing price of the company common stock on the grant dates. Information regarding the company's restricted stock awards during the three months ended March 31, 2015 is as follows:

Restricted Stock Awards	Shares	Weighted Average Grant Date Fair Value	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
	(Dollars in thousands, except weighted average exercise price and weighted average grant date fair value)			
Outstanding at January 1, 2015	—	$ —		$ —
Granted	10,000	5.83	1.0 years	62
Vested	—	—		
Forfeited	—	—		
Unvested outstanding at March 31, 2015	10,000	$ **5.83**	1.0 years	$ 62

The aggregate intrinsic value represents the difference between the company's closing stock price on March 31, 2015 of $6.16 and the option exercise price of the shares for stock options that were in the money, multiplied by the number of shares underlying such options. The total fair value of options vested during the three months ended March 31, 2014 and 2015 was $1.5 million and $1.3 million, respectively.

As of March 31, 2015, there was $0.7 million of total unrecognized compensation cost related to non-vested awards of stock.

NOTE 7. RECENT ACCOUNTING PRONOUNCEMENTS

Changes to accounting principles are established by the FASB in the form of accounting standards updates ("ASU's") to the FASB's Accounting Standards Codification. We consider the applicability and impact of all ASU's. ASU's that are not listed below were assessed and determined to be not applicable to our financial position, results of operations, cash flows, or presentation thereof.

In April 2015, the FASB issued ASU 2015-03, *Simplifying the Presentation of Debt Issuance Costs*, which requires debt issuance costs to be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The new standard is effective for fiscal years beginning after December 15, 2015, and for interim reporting periods within those fiscal years, with early adoption permitted. The new guidance is to be applied on a retrospective basis and reported as a change in accounting principle. The adoption of ASC Update 2015-03 will affect our balance sheet presentation only and will have no impact on our financial position, results of operations or cash flows.

14

In February 2015, the FASB issued ASU 2015-02, Consolidation (Topic 810): *Amendments to the Consolidation Analysis*, which modifies existing consolidation guidance related to (i) limited partnerships and similar legal entities, (ii) the evaluation of variable interests for fees paid to decision makers or service providers, (iii) the effect of fee arrangements and related parties on the primary beneficiary determination, and (iv) certain investment funds. These changes reduce the number of consolidation models from four to two and place more emphasis on the risk of loss when determining a controlling financial interest. This guidance is effective for fiscal years beginning after December 15, 2015. We are in the process of evaluating the adoption of this ASU, and do not expect this to have a material effect on our financial position, results of operations or cash flows.

In August 2014, the FASB issued ASU 2014-15, *Disclosure of Uncertainties About an Entities Ability to Continue as a Going Concern*, which requires management to assess a company's ability to continue as a going concern and to provide related footnote disclosures. The new standard provides management with specific guidance on the assessments and related disclosures as well as provides a longer look-forward period as one year from the financial statement issuance date. The new standard is effective for the annual period ending after December 15, 2016, with early adoption permitted. The adoption of ASU 2014-15 is not expected to have a material impact on our financial position, results of operations, cash flows, or presentation thereof.

In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers,* which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The new standard is effective as of the first interim period within annual reporting periods beginning on or after December 15, 2016, and will replace most existing revenue recognition guidance in U.S. GAAP. Early adoption is not permitted. The standard permits the use of either the retrospective or cumulative effect transition method. We are evaluating the effect that ASU 2014-09 will have on our consolidated financial statements and related disclosures. We have not yet selected a transition method nor have we determined the effect of ASU 2014-09 on our financial position, results of operations, cash flows, or presentation thereof.

In April 2014, the FASB issued ASU 2014-08, *Presentation of Financial Statements and Property, Plant, and Equipment: Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*. ASU 2014-08 limits the requirement to report discontinued operations to disposals of components of an entity that represent strategic shifts that have (or will have) a major effect on an entity's operations and financial results. The amendments also require expanded disclosures concerning discontinued operations and disclosures of certain financial results attributable to a disposal of a significant component of an entity that does not qualify for discontinued operations reporting. These amendments are effective prospectively for reporting periods beginning on or after December 15, 2014, with early adoption permitted. We elected early adoption of the provisions of ASU 2014-08 as of the annual period ending December 31, 2014. The adoption of this ASU did not have a material impact on our financial position, results of operations, cash flows, or presentation thereof.

NOTE 8. EQUITY TRANSACTIONS

We account for stock-based compensation expense in accordance with FASB ASC Topic 718, *Compensation-Stock Compensation*. As a result, $0.6 million and $0.3 million of non-cash stock-based compensation expense has been recorded to additional paid-in capital for the three months ended March 31, 2014 and 2015, respectively.

While we intend to pay regular quarterly distributions, the actual declaration of such future distributions and the establishment of the per share amount, record dates, and payment dates are subject to final determination by our Board of Directors and dependent upon future earnings, cash flows, financial requirements, and other factors. The current policy of the Board of Directors is to review each of these factors on a quarterly basis to determine the appropriate amount, if any, to allocate toward a cash distribution with the general principle of using approximately 20% of free cash flow. Free cash flow is a non-GAAP measure defined in Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations included with this quarterly report.

The following table shows distributions that have been declared and paid since January 1, 2014:

Announcement Date	Payment Date	Amount Per Share	Cash Distributed (*in thousands*)
March 5, 2015	March 31, 2015	$0.0650	$ 1,647
December 2, 2014	December 29, 2014	$0.0650	1,646
September 2, 2014	September 30, 2014	$0.0625	1,579
May 27, 2014	June 30, 2014	$0.0600	1,514
March 6, 2014	March 31, 2014	$0.0575	1,444

Based on the number of shares of Class A and Class B currently outstanding, and the currently approved distribution amount, we expect to pay total annual distributions of approximately $6.6 million for the year ending December 31, 2015.

NOTE 9. NOTES PAYABLE AND LONG-TERM DEBT

Salem Media Group, Inc. has no independent assets or operations, the subsidiary guarantees are full and unconditional and joint and several, and any subsidiaries of Salem Media Group, Inc. other than the subsidiary guarantors are minor.

Term Loan B and Revolving Credit Facility

On March 14, 2013, we entered into a senior secured credit facility, consisting of the Term Loan B of $300.0 million and a revolving credit facility of $25.0 million (“Revolver”). The Term Loan B was issued at a discount for total net proceeds of $298.5 million. The discount is being amortized to non-cash interest expense over the life of the loan using the effective interest method. For each of the three months ended March 31, 2014 and 2015, approximately $46,000 of the discount has been recognized as interest expense including approximately $27,000 of bank loan fees.

The Term Loan B has a term of seven years, maturing in March 2020. During this term, the principal amount may be increased by up to an additional $60.0 million, subject to the terms and conditions of the credit agreement. We are required to make principal payments of $750,000 per quarter which began on September 30, 2013 for the Term Loan B. Prepayments may be made against the outstanding balance of our Term Loan B. Each repayment of the outstanding Term Loan B is applied ratably to each of the next four principal installments thereof in the direct order of maturity and thereafter to the remaining principal balance in reverse order of maturity.

We have made prepayments on our Term Loan B, including interest through the date of the as follows:

Date	Principal Paid	Unamortized Discount
	(Dollars in Thousands)	
January 30, 2015	$2,000	$ 15
December 31, 2014	4,000	16
November 28, 2014	4,000	15
September 29, 2014	5,000	18
March 31, 2014	2,250	8
December 30, 2013	750	3
September 30, 2013	4,000	16
June 28, 2013	4,000	14

The Revolver has a term of five years, maturing in March 2018. We report outstanding balances on our Revolver as short-term based on use of the Revolver to fund ordinary and customary operating cash needs with repayments made frequently. We believe that the borrowing capacity under our Term Loan B and Revolver allows us to meet our ongoing operating requirements, fund capital expenditures and satisfy our debt service requirements for at least the next twelve months.

Borrowings under the Term Loan B may be made at LIBOR (subject to a floor of 1.00%) plus a spread of 3.50% or Wells Fargo’s base rate plus a spread of 2.50%. Borrowings under the Revolver may be made at LIBOR or Wells Fargo’s base rate plus a spread determined by reference to our leverage ratio, as set forth in the pricing grid below. If an event of default occurs under the credit agreement, the applicable interest rate may increase by 2.00% per annum. At March 31, 2015, the blended interest rate on amounts outstanding under the Term Loan B and Revolver was 5.06%.

		Revolver Pricing	
Pricing Level	Consolidated Leverage Ratio	Base Rate Loans	LIBOR Loans
1	Less than 3.00 to 1.00	1.250%	2.250 %
2	Greater than or equal to 3.00 to 1.00 but less than 4.00 to 1.00	1.500%	2.500 %
3	Greater than or equal to 4.00 to 1.00 but less than 5.00 to 1.00	1.750%	2.750 %
4	Greater than or equal to 5.00 to 1.00 but less than 6.00 to 1.00	2.000%	3.000 %
5	Greater than or equal to 6.00 to 1.00	2.500%	3.500 %

The obligations under the credit agreement and the related loan documents are secured by liens on substantially all of the assets of Salem and its subsidiaries, other than certain exceptions set forth in the Security Agreement, dated as of March 14, 2013, among Salem, the subsidiary guarantors party thereto, and Wells Fargo Bank, National Association, as Administrative Agent (the “Security Agreement”) and such other related loan documents.

With respect to financial covenants, the credit agreement includes a minimum interest coverage ratio, which started at 1.50 to 1.0 and steps up to 2.50 to 1.0 by 2016 and a maximum leverage ratio, which started at 6.75 to 1.0 and steps down to 5.75 to 1.0 by 2017. The credit agreement also includes other negative covenants that are customary for credit facilities of this type, including covenants that, subject to exceptions described in the credit agreement, restrict the ability of Salem and its subsidiary guarantors: (i) to incur additional indebtedness; (ii) to make investments; (iii) to make distributions, loans or transfers of assets; (iv) to enter into, create, incur, assume or suffer to exist any liens; (v) to sell assets; (vi) to enter into transactions with affiliates; or (vii) to merge or consolidate with, or dispose of all or substantially all assets to, a third party. As of March 31, 2015, our leverage ratio was 5.35 to 1 compared to our compliance covenant of 6.25 and our interest coverage ratio was 3.25 compared to our compliance ratio of 2.25. We were in compliance with our debt covenants under the credit facility at March 31, 2015.

Other Debt

We have several capital leases related to office equipment. The obligation recorded at December 31, 2014 and March 31, 2015 represents the present value of future commitments under the capital lease agreements.

Summary of long-term debt obligations

Long-term debt consisted of the following:

	As of December 31, 2014	As of March 31, 2015
	(Dollars in thousands)	
Term Loan B	$274,933	$272,994
Revolver	1,784	483
Capital leases and other loans	788	758
	277,505	274,235
Less current portion	(1,898)	(593)
	$275,607	$273,642

In addition to the outstanding amounts listed above, we also have interest payments related to our long-term debt as follows as of March 31, 2015:

- Outstanding borrowings of $274.0 million under the Term Loan B with interest payments due at LIBOR (subject to a floor of 1.00%) plus 3.50% or prime rate plus 2.50%; and
- Outstanding borrowings of $0.5 million under the Revolver, with interest payments due at LIBOR plus 3.00% or at prime rate plus 2.00%.
- Commitment fees of 0.50% on any unused portion of the revolver.

Maturities of Long-Term Debt

Principal repayment requirements under all long-term debt agreements outstanding at March 31, 2015 for each of the next five years and thereafter are as follows:

For the Twelve Months Ended March 31,	Amount (Dollars in thousands)
2016	$ 593
2017	3,108
2018	3,116
2019	3,100
2020	3,103
Thereafter	261,215
	$ 274,235

NOTE 10. DEFERRED FINANCING COSTS

Deferred financing costs consist of bank loan fees incurred upon entering our Term Loan B and Revolver as of September 30, 2013. The costs are being amortized over the seven year term of the Term Loan B and the five year term of the Revolver as an adjustment to interest expense. During the three months ended March 31, 2015, approximately $27,000 of bank loan fees were written off in conjunction with the early retirement of the Term Loan B. Deferred financing costs were $3.2 million at December 31, 2014 and $3.0 million at March 31, 2015.

NOTE 11. AMORTIZABLE INTANGIBLE ASSETS

The following tables provide details, by major category, of the significant classes of amortizable intangible assets:

	As of March 31, 2015		
	Cost	Accumulated Amortization	Net
	(Dollars in thousands)		
Customer lists and contracts	$19,910	$ (17,205)	$2,705
Domain and brand names	15,657	(10,098)	5,559
Favorable and assigned leases	2,379	(1,819)	560
Subscriber base and lists	4,824	(2,893)	1,931
Author relationships	2,245	(1,415)	830
Non-compete agreements	888	(693)	195
Other amortizable intangible assets	1,336	(1,336)	—
	$47,239	$ (35,459)	$11,780

	As of December 31, 2014		
	Cost	Accumulated Amortization	Net
	(Dollars in thousands)		
Customer lists and contracts	$19,910	$ (16,558)	$3,352
Domain and brand names	15,465	(9,722)	5,743
Favorable and assigned leases	2,379	(1,795)	584
Subscriber base and lists	4,302	(2,671)	1,631
Author relationships	2,245	(1,379)	866
Non-compete agreements	888	(669)	219
Other amortizable intangible assets	1,336	(1,336)	—
	$46,525	$ (34,130)	$12,395

Based on the amortizable intangible assets as of March 31, 2015, we estimate amortization expense for the next five years to be as follows:

Year Ending December 31,	Amortization Expense
	(Dollars in thousands)
2015 (April – Dec)	$ 3,658
2016	3,084
2017	1,680

2018	1,461
2019	1,062
Thereafter	835
Total	$ 11,780

NOTE 12. BASIC AND DILUTED NET EARNINGS PER SHARE

Basic net earnings per share is computed using the weighted average number of Class A and Class B shares of common stock outstanding during the period. Diluted net earnings per share is computed using the weighted average number of shares of Class A and Class B common stock outstanding during the period plus the dilutive effects of stock options.

Options to purchase 2,030,459 and 1,715,252 shares of Class A common stock were outstanding at March 31, 2014 and 2015, respectively. Diluted weighted average shares outstanding exclude outstanding stock options whose exercise price is in excess of the average price of the company’s stock price. These options are excluded from the respective computations of diluted net income or loss per share because their effect would be anti-dilutive. As of March 31, 2014 and 2015 there were 816,829 and 574,620 dilutive shares, respectively.

NOTE 13. DERIVATIVE INSTRUMENTS

We are exposed to fluctuations in interest rates. We actively monitor these fluctuations and use derivative instruments from time to time to manage the related risk. In accordance with our risk management strategy, we may use derivative instruments only for the purpose of managing risk associated with an asset, liability, committed transaction, or probable forecasted transaction that is identified by management. Our use of derivative instruments may result in short-term gains or losses that may increase the volatility of our earnings.

Under FASB ASC Topic 815, *Derivatives and Hedging,* the effective portion of the gain or loss on a derivative instrument designated and qualifying as a cash flow hedging instrument shall be reported as a component of other comprehensive income (outside earnings) and reclassified into earnings in the same period or periods during which the hedged forecasted transaction affects earnings. The remaining gain or loss on the derivative instrument, if any, shall be recognized currently in earnings.

On March 27, 2013, we entered into an interest rate swap agreement with Wells Fargo Bank, N.A. that began on March 28, 2014 with a notional principal amount of $150.0 million. The agreement was entered to offset risks associated with the variable interest rate on our Term Loan B. Payments on the swap are due on a quarterly basis with a LIBOR floor of 0.625%. The swap expires on March 28, 2019 at a fixed rate of 1.645%. The interest rate swap agreement was not designated as a cash flow hedge. Changes in the fair value of this non-cash flow hedge are recognized in the current period statement of operations rather than through other comprehensive income. We recorded a long-term liability of $0.9 million as of March 31, 2015, representing the fair value of the interest rate swap agreement. The swap was valued based on observable inputs for similar assets and liabilities and other observable inputs for interest rates and yield curves, which are classified within Level 2 inputs in the fair value hierarchy described in Note 14.

	As of December 31, 2014	As of March 31, 2015
	(Dollars in thousands)	
Fair value of interest rate swap	$ —	$ 945

NOTE 14. FAIR VALUE MEASUREMENTS

FASB ASC Topic 820, *Fair Value Measurements and Disclosures,* established a single definition of fair value in generally accepted accounting principles and expanded disclosure requirements about fair value measurements. The provision applies to other accounting pronouncements that require or permit fair value measurements. We adopted the fair value provisions for financial assets and financial liabilities effective January 1, 2008. The adoption had a material impact on our consolidated financial position, results of operations or cash flows. We adopted fair value provisions for nonfinancial assets and nonfinancial liabilities effective January 1, 2009. This includes applying the fair value concept to (i) nonfinancial assets and liabilities initially measured at fair value in business combinations; (ii) reporting units or nonfinancial assets and liabilities measured at fair value in conjunction with goodwill impairment testing; (iii) other nonfinancial assets measured at fair value in conjunction with impairment assessments; and (iv) asset retirement obligations initially measured at fair value. The adoption of the fair value provisions of FASB ASC Topic 820 to nonfinancial assets and nonfinancial liabilities did not have a material impact on our consolidated financial position, results of operations or cash flows.

The fair value provisions include guidance on how to estimate the fair value of assets and liabilities in the current economic environment and reemphasizes that the objective of a fair value measurement remains an exit price. If we were to conclude that there has been a significant decrease in the volume and level of activity of the asset or liability in relation to normal market activities, quoted market values may not be representative of fair value and we may conclude that a change in valuation technique or the use of multiple valuation techniques may be appropriate.

The degree of judgment utilized in measuring the fair value of financial instruments generally correlates to the level of pricing observability. Pricing observability is affected by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market, and the characteristics specific to the transaction. Financial instruments with readily available active quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of pricing observability and a lesser degree of judgment utilized in measuring fair value. Conversely, financial instruments rarely traded or not quoted will generally have less (or no) pricing observability and a higher degree of judgment utilized in measuring fair value.

FASB ASC Topic 820 established a hierarchal disclosure framework associated with the level of pricing observability utilized in measuring fair value. This framework defined three levels of inputs to the fair value measurement process and requires that each fair value measurement be assigned to a level corresponding to the lowest level input that is significant to the fair value measurement in its entirety. The three broad levels of inputs defined by the FASB ASC Topic 820 hierarchy are as follows:

- Level 1 Inputs—quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date;

- Level 2 Inputs—inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. If the asset or liability has a specified (contractual) term, a Level 2 input must be observable for substantially the full term of the asset or liability; and

- Level 3 Inputs—unobservable inputs for the asset or liability. These unobservable inputs reflect the entity’s own assumptions about the assumptions that market participants would use in pricing the asset or liability, and are developed based on the best information available in the circumstances (which might include the reporting entity’s own data).

As of March 31, 2015, the carrying value of cash and cash equivalents, trade accounts receivables, accounts payable, accrued expenses and accrued interest approximates fair value due to the short-term nature of such instruments. The carrying value of other long-term liabilities approximates fair value as the related interest rates approximate rates currently available to the company. The following table summarizes the fair value of our financial assets and liabilities that are measured at fair value:

	March 31, 2015			
	Total Fair Value and Carrying Value on Balance Sheet	Fair Value Measurement Category		
		Level 1	Level 2	Level 3
	(Dollars in thousands)			
Assets:				
Cash and cash equivalents	**$182**	$182	$—	$—
Trade accounts receivable, net	**33,520**	33,520	—	—
Liabilities:				
Accounts payable	**5,801**	5,801	—	—
Accrued expenses including estimated fair value of contingent earn-out consideration	**15,104**	12,853	—	2,251
Accrued interest	**43**	43	—	—
Long term liabilities including estimated fair value of contingent earn-out consideration	**1,059**	24	—	1,035
Long-term debt	**274,235**	274,235	—	—
Fair value of interest rate swap	**945**	—	945	—

NOTE 15. INCOME TAXES

We account for income taxes in accordance with FASB ASC Topic 740, *Income Taxes*. We recorded no adjustments to our unrecognized tax benefits as of March 31, 2015 and 2014. At December 31, 2014, we had $0.5 million in liabilities for unrecognized tax benefits. Included in this liability amount were $0.02 million accrued for the related interest, net of federal income tax benefits, and $0.02 million for the related penalty recorded in income tax expense on our Condensed Consolidated Statements of Operations. We expect to reduce the reserve balance by $0.4 million over the next twelve months due to statute expirations.

Valuation Allowance (Deferred Taxes)

For financial reporting purposes, we recorded a valuation allowance of $3.0 million as of March 31, 2015 to offset a portion of the deferred tax assets related to the state net operating loss carryforwards. We regularly review our financial forecasts in an effort to determine our ability to utilize the net operating loss carryforwards for tax purposes. Accordingly, the valuation allowance is adjusted periodically based on our estimate of the benefit the company will receive from such carryforwards.

NOTE 16. COMMITMENTS AND CONTINGENCIES

The company enters into various agreements in the normal course of business that contain minimum guarantees. These minimum guarantees are often tied to future events, such as future revenue earned in excess of the contractual level. Accordingly, the fair value of these arrangements is zero. The company also records contingent earn-out consideration representing the estimated fair value of future liabilities associated with acquisitions that may have additional payments due upon the achievement of certain performance targets. The fair value of the contingent earn-out consideration is estimated as of the acquisition date as the present value of the expected contingent payments as determined using weighted probabilities of the expected payment amounts.

The company and its subsidiaries, incident to its business activities, are parties to a number of legal proceedings, lawsuits, arbitration and other claims. Such matters are subject to many uncertainties and outcomes that are not predictable with assurance. The company maintains insurance that may provide coverage for such matters. Consequently, the company is unable to ascertain the ultimate aggregate amount of monetary liability or the financial impact with respect to these matters. The company believes, at this time, that the final resolution of these matters, individually and in the aggregate, will not have a material adverse effect upon the company's annual consolidated financial position, results of operations or cash flows.

NOTE 17. SEGMENT DATA

FASB ASC Topic 280, *Segment Reporting*, requires companies to provide certain information about their operating segments. We have two reportable segments, radio broadcasting and digital media. Digital media (formerly "Internet and e-commerce") became a reportable segment as of the first quarter of 2011 upon the realization of organic and acquisition-related revenue growth. Our acquisition of Eagle Publishing on January 10, 2014, which included Regnery Publishing, Eagle Financial Publications, Eagle Wellness, Human Events and Red State, resulted in operational changes in our business and a realignment of our operating segments. We now have three operating segments: (1) Broadcast, (2) Digital Media, and (3) Publishing.

We changed the composition of our operating segments to reflect management's view of the operating results for each segment during the fourth quarter of 2014. Under our new composition, digital revenue generated by our broadcast stations is now reported under broadcast operating revenue as the station sales team and general manager are responsible for this digital revenue under their bonus and commission structure. Digital revenue from our broadcast stations was previously reported as Internet and e-Commerce revenue. E-book revenue is now reported under Publishing revenue as sales goals and bonuses for Eagle Regnery Publishing are inclusive of sales of e-books. The sale of e-Books was previously reported as Internet & e-commerce revenue. Additionally, we have allocated specific corporate departments, such as engineering, broadcast operations, digital and publishing within their respective operating segments. Corporate expenses as revised include unallocated expenses, such as accounting and finance, human resources, and other shared functions.

Our operating segments reflect how our chief operating decision makers, which we define as a collective group of senior executives, assesses the performance of each operating segment and determines the appropriate allocations of resources to each segment. Our operating segments do not all meet the quantitative thresholds to qualify as reportable segments; however, we have elected to disclose the results of these non-reportable operating segments as we believe this information is useful to readers of our financial statements. We continue to review our operating segment classifications to align with operational changes in our business and may make future changes as necessary.

We measure and evaluate our operating segments based on operating income and operating expenses that do not include allocations of costs related to corporate functions, such as accounting and finance, human resources, legal, tax and treasury; nor do they include costs such as amortization, depreciation, taxes or interest expense. Changes to our operating segments did not impact the reporting units used to test non-amortizable assets for impairment. All prior periods presented have been updated to reflect the new composition of our operating segments.

Segment performance, as we define it in accordance with the FASB's guidance relating to segment reporting, is not necessarily comparable to other similarly titled captions of other companies. The table below presents financial information for each operating segment as of March 31, 2014 and 2015 based on the new composition of our operating segments:

	Broadcast	Digital Media	Publishing	Unallocated Corporate	Consolidated
	(Dollars in thousands)				
Three Months Ended March 31, 2015					
Net revenue	$46,539	$10,791	$ 4,526	$ —	$ 61,856
Operating expenses	33,917	9,000	4,497	3,991	51,405
Net operating income (loss) before depreciation, amortization, change in the estimated fair value of contingent earn-out consideration and (gain) loss on disposal of assets	$12,622	$1,791	$ 29	$ (3,991)	$ 10,451
Depreciation	1,951	776	168	277	3,172

Amortization	23	1,170	136	—	1,329
Change in the estimated fair value of contingent earn-out consideration	—	33	85	—	118
(Gain) loss on disposal of assets	129	—	(1)	1	129
Net operating income (loss)	$10,519	$(188)	$ (359)	$ (4,269)	$ 5,703
Three Months Ended March 31, 2014					
Net revenue	$46,769	$11,312	$ 4,263	$ —	