

GRAY TELEVISION INC
Form 10-K
February 26, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 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 1-13796

GRAY TELEVISION, INC.

(Exact Name of Registrant as Specified in its Charter)

Georgia **58-0285030**
(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)

4370 Peachtree Road, NE Atlanta, GA 30319
(Address of Principal Executive Offices) (Zip Code)

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

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Class A Common Stock (no par value)	New York Stock Exchange

Common Stock (no par value)	New York Stock Exchange
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Securities registered pursuant to Section 12(g) of the Act: **NONE**

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

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

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 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 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.

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. (Check one).

Large accelerated filer

Accelerated filer

Non-accelerated filer (do not check if a smaller reporting company)

Smaller Reporting Company

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

The aggregate market value of the voting stock (based upon the closing sales prices quoted on the New York Stock Exchange) held by non-affiliates of the registrant (solely for purposes of this calculation, all directors, executive officers and 10% or greater stockholders of the registrant are considered to be "affiliates") as of June 30, 2015: **Class A Common Stock and Common Stock; no par value - \$1,006,138,318.**

The number of shares outstanding of the registrant's classes of common stock as of February 19, 2016: **Class A Common Stock; no par value –6,396,033 shares; Common Stock, no par value –66,304,805 shares.**

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement for the annual meeting of stockholders, to be filed within 120 days of the registrant's fiscal year end, pursuant to Regulation 14A are incorporated by reference into Part III hereof.

Gray Television Inc.**INDEX**

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PART 1

Item 1. Business.

In this annual report on Form 10-K (the “Annual Report”), unless otherwise indicated or the context otherwise requires, the words “Gray,” the “Company,” “we,” “us,” and “our” refer to Gray Television, Inc. and its consolidated subsidiaries. For more information on variable interest entities, see Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations.” The discussion herein of the television (or “TV”) stations that we own and operate does not include our interest in the television and radio stations owned by Sarkes Tarzian, Inc.

Our common stock and our Class A common stock have been listed and traded on The New York Stock Exchange (the “NYSE”) under the symbols “GTN” and “GTN.A” since 1996 and 1995, respectively.

Unless otherwise indicated, all station rank, in-market share and television household data herein are derived from reports prepared by Nielsen Media Research Company (“Nielsen”), a national audience measuring service. While we believe this data to be accurate and reliable, we have not independently verified such data.

General

We are a television broadcast company headquartered in Atlanta, Georgia, that owns and operates television stations and leading digital assets in markets throughout the United States. As of February 19, 2016, we owned and/or operated television stations in 50 television markets broadcasting approximately 180 separate programming streams, including 35 affiliates of the CBS Network (“CBS”), 26 affiliates of the NBC Network (“NBC”), 19 affiliates of the ABC Network (“ABC”) and 13 affiliates of the FOX Network (“FOX”). We refer to these major broadcast networks CBS, NBC, ABC and FOX collectively as the “Big Four” networks.

In addition to our primary broadcast channels, we can also broadcast secondary digital channels within a market. Our secondary digital channels are generally affiliated with networks different from those affiliated with our primary broadcast channels, and they are operated by us to make better use of our broadcast spectrum by providing supplemental and/or alternative programming in addition to our primary channels. Certain of our secondary digital channels are affiliated with more than one network simultaneously. In addition to affiliations with ABC, CBS and FOX, our secondary channels are affiliated with numerous smaller networks and program services including, among others, the CW Network or the CW Plus Network (collectively, “CW”), MY Network (“MY” or “My Network”), the MeTV

Network (“MeTV”), This TV Network (“This TV”), Antenna TV (“Ant.”), Telemundo (“Tel.”), Heroes and Icons (“H&I”) and MOVIES! Network (“Movies”). We also broadcast local news/weather channels in certain of our existing markets (“News”). Our combined TV station group reaches approximately 9.4% of total United States television households.

Our operating revenues are derived primarily from broadcast and internet advertising, retransmission consent fees and, to a lesser extent, from other sources such as production of commercials and tower rentals. For the years ended December 31, 2015, 2014 and 2013, we generated revenue of \$597.4 million, \$508.1 million and \$346.3 million, respectively.

Television Industry Background

The Federal Communications Commission (the “FCC”) grants broadcast licenses to television stations. There are only a limited number of broadcast licenses available in any one geographic area.

Each commercial television station in the United States is assigned by Nielsen to one of 210 geographic television markets or designated market areas (“DMAs”). These markets are ranked in size according to their number of television households, with the market having the largest number of television households (New York City) ranked first. Each DMA is an exclusive geographic area consisting of all counties (and in some cases, portions of counties) in which the home-market commercial television stations receive the greatest percentage of total viewing hours. Nielsen periodically publishes data on estimated audiences for the television stations in each DMA.

Television station revenue is derived primarily from local, regional and national advertising and retransmission consent fees. Television station revenue is derived to a much lesser extent from studio and tower space rental fees and commercial production activities. “Advertising” refers primarily to advertisements broadcast by television stations, but it also includes advertisements placed on a television station’s website and sponsorships of television programming and off-line content (such as email messages, mobile applications, and other electronic content distributed by stations). Advertising rates are based upon: (i) the size of a station’s market, (ii) a station’s overall ratings, (iii) a program’s popularity among targeted viewers, (iv) the number of advertisers competing for available time, (v) the demographic makeup of the station’s market, (vi) the availability of alternative advertising media in the market, (vii) the presence of effective sales forces and (viii) the development of projects, features and programs that tie advertiser messages to programming and/or digital content on a station’s website or mobile applications. Advertising rates can also be determined in part by a station’s overall ratings and in-market share, as well as the station’s ratings and market share among particular demographic groups that an advertiser may be targeting. Because broadcast stations rely on advertising revenues, they are sensitive to cyclical changes in the economy. The sizes of advertisers’ budgets, which can be affected by broad economic trends, can affect the broadcast industry in general and the revenues of individual broadcast television stations.

Strategy

Our success is based on the following strategies for growing our revenues and operating cash flows:

Grow by Leveraging our Diverse National Footprint

We have a diverse and national footprint of television stations in 50 television markets that comprise approximately 9.4% of United States television households. We currently operate in DMAs ranked between 62 and 209 and primarily focus our operations on university towns and state capitals. We believe university towns and state capitals provide significant advantages as they generally offer more favorable advertising demographics, more stable economics and a stronger affinity between local stations and university sports teams than other markets. We also seek to operate in markets that we believe have the potential for significant political advertising revenue in periods leading up to elections. We are also diversified across our programming, broadcasting approximately 180 separate programming streams, including 35 affiliates of CBS, 26 affiliates of NBC, 19 affiliates of ABC and 13 affiliates of FOX.

Continue to Pursue Strategic Growth and Accretive Acquisition Opportunities

The television broadcasting industry has been characterized recently by a high level of acquisition activity. We believe that there continue to be a number of television stations, and a few station groups, that have attractive operating profiles and characteristics, and that share our commitment to local news coverage in the communities in which they operate and to creating high-quality and locally-driven content. We intend to continue to selectively pursue opportunities for the acquisition of television stations or station groups, primarily in markets below the Top 50 DMAs that fit our strategic and operational objectives, and where we believe that we can improve revenue, efficiencies and cash flow through active management and cost controls. As we consider potential acquisitions, we primarily evaluate potential station audience and revenue shares and the extent to which the target would positively impact our existing station operations.

Consistent with this strategy, between October 31, 2013 and December 31, 2015, we completed 16 acquisition transactions and two divestiture transactions. These transactions added a net total of 31 television stations in 20 television markets to our operations, including 15 new television markets. During the year ended December 31, 2015, we completed the following acquisitions:

the November 1, 2015 acquisition of KCRG-TV, which is affiliated with ABC and serves the Cedar Rapids, Iowa television market (“KCRG-TV”) for \$100.0 million (the “Cedar Rapids Acquisition”);

the July 1, 2015 acquisition of KOSA-TV, whose digital channels are affiliated with the CBS and MY networks and serves the Odessa-Midland, Texas television market (“KOSA-TV”) for \$33.6 million (the “Odessa Acquisition”);

the July 1, 2015 acquisition of KMVT-TV, whose digital channels are affiliated with the CBS and CW Networks, as well as KSVT-LD, whose digital channel is affiliated jointly with the FOX and MY Networks (together, “KMTV-TV”), which station serves the Twin Falls, Idaho television market, for \$17.5 million (the “Twin Falls Acquisition”);

the July 1, 2015 acquisition of certain non-license assets, including programming streams, of WFXS-TV, which had served as the FOX affiliate for the Wausau-Rhineland, Wisconsin television market, whose programming streams are now broadcast on our digital low power television station in Wausau, WZAW-LD (“WZAW-LD” or) for \$14.0 million (the “Wausau Acquisition”);

the July 1, 2015 acquisition of WAGM-TV, whose digital channels are affiliated with the CBS and FOX networks (“WAGM-TV”), and which station serves the Presque Isle, Maine television market, for \$10.3 million (the “Presque Isle Acquisition”); and

the July 1, 2015 acquisition of certain non-license assets, including programming streams, of KVTM-TV, which had served as the CBS affiliate for the Laredo, Texas television market, whose programming streams are now broadcast on our digital low power television station in Laredo, KYLX-TV (“KYLX-LD”) for \$9.0 million (the “Laredo Acquisition”).

We refer to the stations acquired in 2015 collectively as the “2015 Acquired Stations.” During 2014, we completed seven acquisitions, which transactions collectively added a total of 22 television stations and 12 markets (10 new markets) to our operations at various times during that year, and we refer to the stations acquired in those acquisitions as the “2014 Acquired Stations.” During 2013, we completed two acquisition transactions that together added five television stations in four markets (three in new markets) to our operations, and we refer to the stations acquired in those acquisitions as the “2013 Acquired Stations.” Unless the context of the discussion of these transactions requires otherwise, we refer to the 2015 Acquired Stations, the 2014 Acquired Stations and the 2013 Acquired Stations, collectively, as the “Acquired Stations.”

In addition, on September 14, 2015, we announced that we agreed to acquire all of the television and radio stations of Schurz Communications, Inc. (“Schurz”) for approximately \$442.5 million inclusive of working capital (the “Schurz Acquisition”). On October 1, 2015, we announced the sale of certain television stations to facilitate regulatory approvals for the Schurz Acquisition, and we simultaneously announced the acquisition of two television stations through swap transactions as part of those divestitures. On November 2, 2015, we announced that we had reached agreements with three radio broadcasters to divest the Schurz radio stations to those third-parties upon the closing of the Schurz Acquisition (the transactions announced on October 1, 2015 and November 2, 2015 together with the Schurz Acquisition, the “Schurz Acquisition and Related Transactions”). On October 1, 2015, we also announced the acquisition of KYES-TV, which would be our second station in the Anchorage, Alaska television market. The KYES-TV acquisition, which remains pending, is excluded from the foregoing definition.

On February 1, 2016, to facilitate regulatory approval of the Schurz Acquisition, we completed one swap transaction, the disposition of the assets of KAKE-TV in the Wichita, Kansas television market in exchange for the assets of WBXX-TV in the Knoxville, Tennessee television market. On February 16, 2016 we completed the remaining portions of the Schurz Acquisition and Related Transactions. The Schurz Acquisition and Related Transactions added the following television stations to our portfolio:

Station	Primary Network Affiliation	Market
WBXX-TV	CW	Knoxville, TN
KWCH-TV ⁽¹⁾	CBS	Wichita-Hutchinson, KS
WDBJ-TV	CBS	Roanoke, VA
KYTV-DT	NBC	Springfield, MO
KCZ	CW	Springfield, MO
KSPR-TV ⁽²⁾	ABC	Springfield, MO
WAGT-TV	NBC	Augusta, GA
KTUU-TV	NBC	Anchorage, AK
KOTA-TV ⁽³⁾	ABC	Rapid City, SD
WLUC-TV	NBC/FOX	Marquette, MI

(1) The acquired station includes one or more satellite stations, either re-broadcasting the programming associated with the primary network affiliation or programming associated with smaller networks and/or program services.

(2) Gray provides certain non-sales, back-office services to KSPR-TV, which Schurz acquired from Perkin Media, LLC, on February 16, 2016.

(3) We have acquired the indicated program stream in this market and are broadcasting this program stream on our previously existing station in this market, which has changed its call letters to KOTA-TV.

Refer to our Markets and Stations table later in this Item 1 and Note 2 “Acquisitions and Dispositions” and Note 11 “Subsequent Events” of our audited consolidated financial statements as of and for the year ended December 31, 2015 included in Item 8, for more information.

Maintain and Grow our Market Leadership Position

Based on the consolidated results of the four Nielsen “sweeps” periods in 2015, our television stations (including those acquired in February 2016) achieved the #1 ranking in overall audience in 39 of our 50 markets and the #1 ranking in local news audience in 36 of our markets. In addition, our stations achieved the #1 or #2 ranking in both overall audience and news audience in 49 of our 50 markets.

We believe there are significant advantages in operating the #1 or #2 television broadcasting stations in a local market. Strong audience and market share allows us to enhance our advertising revenue through price discipline and leadership. We believe a top-rated news platform is critical to capturing incremental sponsorship and political advertising revenue. Our high-quality station group allows us to generate high operating margins, which allows us additional opportunities to reinvest in our business to further strengthen our network and news ratings. Furthermore, we believe operating the top ranked stations in our various markets allows us to attract and retain top talent.

We also believe our local leadership positions help us in negotiating more beneficial terms in our network affiliation agreements, which expire on various dates through December 2020, and in our syndicated programming agreements.

We also believe that our leadership position in the markets in which we operate gives us additional leverage to negotiate retransmission contracts with cable system operators, telephone video distributors, direct broadcast satellite (“DBS”) operators, and other multichannel video programming distributors (collectively, “MVPDs”). These MVPDs pay us for the right to retransmit our television stations’ program content.

We intend to maintain our market leadership position through continued prudent investment in our news and syndicated programs, as well as continued technological advances and workflow improvements. We expect to continue to invest in technological upgrades over the next few years. We believe the foregoing will help us maintain and grow our market leadership; thereby enhancing our ability to grow and further diversify our revenues and cash flows.

Continue to Monetize Digital Spectrum

We currently broadcast over 80 secondary channels. Our secondary channels are affiliated with networks different from those affiliated with our primary channels and are operated by us to make better use of our broadcast spectrum by providing supplemental and/or alternative programming to our primary channels. Certain of our channels are affiliated with more than one network simultaneously.

Our strategy includes expanding upon our digital offerings, and we evaluate potential opportunities from time to time either on our own and/or in partnership with other companies. We also evaluate opportunities to use spectrum for future delivery of television broadcasts to handheld and other mobile devices. For example, in 2015, we were one of the first affiliate groups to launch CBS All Access service, and we have implemented the service in each of our markets. We also have an agreement with the NBC Network to launch our NBC-affiliated channels through NBCUniversal’s TV Everywhere platform for mobile and online devices.

Maintain Prudent Cost Management

Historically, we have closely managed our costs to maintain and improve our margins. We believe that our market leadership position also gives us additional negotiating leverage to enable us to lower our syndicated programming costs. We have increased the efficiency of our stations by automating video production and back office processes. We believe that we will be able to further benefit from our cost and operational efficiencies as we continue to grow our Company.

Cyclical, Seasonality and Revenue Concentrations

Because broadcast stations like ours rely on advertising revenue, they are sensitive to cyclical changes in the economy. As a result, our non-political advertising revenue has improved along with the general economic environment since 2010. Our political advertising revenue is generally not as significantly affected by economic slowdowns or recessions as our non-political advertising revenue.

Broadcast advertising revenue is generally highest in the second and fourth quarters each year. This seasonality results partly from increases in consumer advertising in the spring and retail advertising in the period leading up to and including the Christmas holiday season. Broadcast advertising revenue is also typically higher in even-numbered years due to spending by political candidates, political parties and special interest groups during the “on year” of the two-year political advertising cycle. This political advertising spending typically is heaviest during the fourth quarter. In addition, the broadcast of Olympic Games by our NBC-affiliated stations during even-numbered years generally leads to increased viewership and revenue during those years.

Our broadcast advertising revenue is earned from the sale of advertisements broadcast by our stations. Although no single customer represented more than 5% of our broadcast advertising revenue for the years ended December 31, 2015, 2014 or 2013, we derived a material portion of our non-political broadcast advertising revenue from advertisers in a limited number of industries, particularly the automotive industry. For the years ended December 31, 2015, 2014 and 2013, we derived approximately 24%, 21% and 25%, respectively, of our total broadcast advertising revenue from our customers in the automotive industry. Revenue from this industry represents a higher percentage of total revenue in odd-numbered years due to, among other things, the increased availability of advertising time, as a result of such years being the “off year” of the two year political advertising cycle. Our results of operations and financial condition could be materially adversely affected if broadcast advertising revenue from the automotive industry, or certain other industries, such as the medical, restaurant, communications and furniture and appliance industries were to decline.

Markets and Stations

We operate in markets below the top 50 DMAs and have significant operations in university towns and state capitals. Our markets include 27 university towns, representing enrollment of approximately 634,000 students, and 11 state capitals. We believe university towns and state capitals provide significant advantages, as they generally offer more favorable advertising demographics, more stable economics and a stronger affinity between local stations and university sports teams.

We have strong, market leading positions in our markets. We believe a key driver for our strong market position is the strength of our local news and information programs. We believe that our market position and our strong local revenue streams have enabled us to maintain more stable revenues compared to many of our peers.

We are diversified across our markets and network affiliations. In 2015 and 2014, our largest market by company revenue was Charleston/Huntington, WV, which contributed approximately 6% and 7% of our revenue for each of those years, respectively. Our top 10 markets by Company revenue contributed approximately 38% and 35% of our revenue for each of the years ended December 31, 2015 and 2014, respectively. For the years ended December 31, 2015 and 2014, our CBS-affiliated channels accounted for 36% and 42%, respectively, of our revenue; our NBC-affiliated channels accounted for 34% and 38%, respectively, of our revenue; our ABC-affiliated channels accounted for 20% and 15%, respectively, of our revenue; and our FOX-affiliated channels accounted for

approximately 2% of our revenue.

All but four of our stations broadcast a primary channel affiliated with one of the four major broadcast networks. In addition to the primary channels, the majority of our stations also broadcast secondary digital channels that are affiliated with various networks. The terms of our affiliations with these networks are governed by network affiliation agreements. Each network affiliation agreement provides the affiliated station with the right to broadcast all programs transmitted by the affiliated network. Our network affiliation agreements currently expire at various dates through December 31, 2020.

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The following table provides information about our owned and/or operated television stations, as of February 19, 2016:

DMA Rank (a)	Designated Market Area ("DMA")	Station	Network	Primary Broadcast License	Primary Channel	
		Call Letters	Affiliation (b)	Expiration Date (c)	Station Rank in DMA (d)	News Rank in DMA (e)
62	Knoxville, TN	WVLT	CBS	8/1/2021	2	3
62	Knoxville, TN	WBXX	CW	8/1/2021	5	5
63	Lexington, KY	WKYT	CBS	8/1/2021	1	1
(f)	Hazard, KY	WYMT	CBS	8/1/2021	6	5
65	Wichita-Hutchinson, KS	KWCH	CBS	6/1/2022	1	1
65	Wichita-Hutchinson, KS	KSCW	CW	6/1/2022	5	5
65	Wichita-Hutchinson, KS	KDCU	(g) UNI	6/1/2022	7	7
65	(Ensign, KS)	KBSD	(h)			