

ARBITRON INC  
Form 10-Q  
August 14, 2002

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, DC 20549

**FORM 10-Q**

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

**For the quarterly period ended June 30, 2002**

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: 1-1969

**ARBITRON INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of  
incorporation or organization)

**52-0278528**

(I.R.S. Employer Identification No.)

**142 West 57<sup>th</sup> Street**

**New York, New York 10019**

(Address of principal executive offices) (Zip Code)

**(212) 887-1300**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

The registrant had 29,497,462 shares of common stock, par value \$0.50 per share, outstanding as of July 31, 2002.

ARBITRON INC.

INDEX

	<u>Page No.</u>
PART I FINANCIAL INFORMATION	
Item 1. Financial Statements	
Consolidated Balance Sheets June 30, 2002 and December 31, 2001	3
Consolidated Statements of Income Three Months Ended June 30, 2002 and 2001	4
Consolidated Statements of Income Six Months Ended June 30, 2002 and 2001	5
Consolidated Statements of Cash Flows Six Months Ended June 30, 2002 and 2001	6
Notes to Consolidated Financial Statements June 30, 2002	7
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	12
Item 3. Quantitative and Qualitative Disclosure of Market Risk	20
PART II OTHER INFORMATION	
Item 4. Submission of Matters to a Vote of Security Holders	21
Item 6. Exhibits and Reports on Form 8-K	21
Signature	22

**PART I FINANCIAL INFORMATION**  
**ITEM 1. FINANCIAL STATEMENTS**

**ARBITRON INC.**  
Consolidated Balance Sheets  
(In thousands)

	<b>June 30, 2002</b>	<b>December 31, 2001</b>
	<b>(unaudited)</b>	<b>(audited)</b>
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 24,203	\$ 21,043
Trade accounts receivable, net of allowance for doubtful accounts of \$1,129 in 2002 and \$995 in 2001	16,193	19,393
Deferred tax assets	15,525	24,644
Prepaid expenses and other current assets	3,073	2,578
	<u>58,994</u>	<u>67,658</u>
Total current assets	58,994	67,658
Investments in affiliates	9,438	9,722
Property and equipment, net	12,201	8,850
Goodwill, net	32,937	28,937
Other intangibles, net	2,382	2,961
Deferred tax assets	2,391	3,698
Other noncurrent assets	5,292	5,015
	<u>123,635</u>	<u>126,841</u>
Total assets	\$ 123,635	\$ 126,841
<b>Liabilities and Stockholders Equity (Deficit)</b>		
Current liabilities		
Accounts payable	\$ 4,083	\$ 5,245
Accrued expenses and other current liabilities	14,198	15,597
Due to owners of acquired business		10,621
Deferred revenue	46,177	52,993
	<u>64,458</u>	<u>84,456</u>
Total current liabilities	64,458	84,456
Noncurrent liabilities		
Long-term debt	195,000	205,000
Other noncurrent liabilities	6,470	6,494
	<u>201,470</u>	<u>211,494</u>
Total liabilities	265,928	295,950
Stockholders equity (deficit)		
Common stock, \$0.50 par value, authorized 500,000 shares, issued 32,336 shares and 32,332 shares, respectively	16,168	16,166
Additional paid-in capital	64,980	59,349
Accumulated earnings (net distributions to Ceridian in excess of accumulated earnings) prior to spin-off	(260,146)	(260,146)
Retained earnings subsequent to spin-off	41,027	20,167
Common stock held in treasury, 2,898 shares and 3,130 shares, respectively	(1,449)	(1,565)
Accumulated other comprehensive loss	(2,873)	(3,080)
	<u>(142,293)</u>	<u>(169,109)</u>
Total stockholders equity (deficit)	(142,293)	(169,109)

Edgar Filing: ARBITRON INC - Form 10-Q

Total liabilities and stockholders' equity (deficit)	\$ 123,635	\$ 126,841
--	------------	------------

See notes to consolidated financial statements.

Edgar Filing: ARBITRON INC - Form 10-Q

**ARBITRON INC.**  
 Consolidated Statements of Income  
 (In thousands, except per share data)  
 (unaudited)

	<b>Three Months Ended June 30,</b>	
	<b>2002</b>	<b>2001</b>
Revenue	\$56,509	\$50,264
Costs and expenses		
Cost of revenue	26,046	22,811
Selling, general and administrative	12,986	11,951
Research and development	5,803	5,638
Total costs and expenses	44,835	40,400
Operating income	11,674	9,864
Equity in net income of affiliate	3,312	2,942
Income before interest and income tax expense	14,986	12,806
Interest income	124	354
Interest expense	4,348	5,352
Income before income tax expense	10,762	7,808
Income tax expense	4,144	3,094
Net income	\$ 6,618	\$ 4,714
Net income per weighted average common share		
Basic	0.23	0.16
Diluted	0.22	0.16
Weighted average common shares used in calculations		
Basic	29,368	29,155
Potentially dilutive securities	712	184
Diluted	30,080	29,339

See notes to consolidated financial statements.

**ARBITRON INC.**  
Consolidated Statements of Income  
(In thousands, except per share data)  
(unaudited)

	Six Months Ended June 30,	
	2002	2001
Revenue	\$ 122,411	\$ 110,454
Costs and expenses		
Cost of revenue	44,909	38,684
Selling, general and administrative	25,663	23,165
Research and development	11,315	10,334
Total costs and expenses	81,887	72,183
Operating income	40,524	38,271
Equity in net income of affiliate	2,067	1,819
Income before interest and income tax expense	42,591	40,090
Interest income	262	373
Interest expense	8,934	5,738
Income before income tax expense	33,919	34,725
Income tax expense	13,059	13,716
Net income	\$ 20,860	\$ 21,009
Net income and pro forma net income per weighted average common share		
Basic	0.71	0.72
Diluted	0.70	0.72
Weighted average and pro forma weighted average common shares used in calculations		
Basic	29,292	29,155
Potentially dilutive securities	673	169
Diluted	29,965	29,324

See notes to consolidated financial statements.

Edgar Filing: ARBITRON INC - Form 10-Q

**ARBITRON INC.**  
 Consolidated Statements of Cash Flows  
 (Dollars in thousands)  
 (unaudited)

	<b>Six Months Ended June 30,</b>	
	<b>2002</b>	<b>2001</b>
<b>Cash flows from operating activities</b>		
Net income	\$ 20,860	\$ 21,009
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	1,482	1,018
Other amortization	579	1,197
Loss on disposals of property and equipment		(4)
Deferred income taxes	10,374	13,528
Equity in net income of affiliate	(2,067)	(1,819)
Distributions from affiliate	2,350	1,950
Bad debt expense	198	136
Tax benefit from stock option exercises	1,352	
Changes in operating assets and liabilities		
Trade accounts receivable	3,086	(855)
Prepaid expenses and other assets	(754)	126
Accounts payable	(1,224)	(4,511)
Accrued expenses and other current liabilities	(1,044)	568
Deferred revenue	(6,829)	(4,994)
Other noncurrent liabilities	114	(507)
Net cash provided by operating activities	28,477	26,842
<b>Cash flows from investing activities</b>		
Additions to property and equipment	(4,824)	(3,264)
Payments for business acquisitions	(15,000)	(3,000)
Proceeds from disposals of property and equipment		45
Net cash used in investing activities	(19,824)	(6,219)
<b>Cash flows from financing activities</b>		
Proceeds from stock option exercises and stock purchase plan	4,397	73
Proceeds from issuance of long-term debt		250,000
Repayment of long-term debt	(10,000)	(10,000)
Payment of deferred financing costs		(3,002)
Net cash distributions to Ceridian Corporation		(235,958)
Net cash provided by (used in) financing activities	(5,603)	1,113
Effect of exchange rate changes on cash	110	(3)
Net increase in cash and cash equivalents	3,160	21,733
Cash and cash equivalents at beginning of period	21,043	3,540
Cash and cash equivalents at end of period	\$ 24,203	\$ 25,273



See notes to consolidated financial statements.

**ARBITRON INC.**  
Notes to Consolidated Financial Statements  
June 30, 2002  
(unaudited)

**1. Basis of Presentation and Consolidation**

*Presentation*

Arbitron Inc. ( Arbitron or the Company ) was formerly known as Ceridian Corporation. Prior to March 31, 2001, Ceridian, a publicly traded company, had as its principal lines of business the human resource service businesses, the Comdata business, which provided transaction processing and regulatory compliance services for the transportation industry, and the radio audience measurement business.

On March 30, 2001, Ceridian effected a reverse spin-off, which we refer to as the spin-off. In connection with the spin-off, the assets and liabilities associated with the human resource service businesses and Comdata subsidiaries were transferred to New Ceridian. The radio audience measurement business stayed with Ceridian. Ceridian then distributed the stock of New Ceridian to its existing stockholders. As a result, New Ceridian is now a separate publicly traded corporation. In connection with the spin-off, Ceridian changed its name to Arbitron Inc. and effected a one-for-five reverse stock split, and New Ceridian changed its name to Ceridian Corporation. Because of the relative significance of the businesses transferred to New Ceridian, New Ceridian was considered the accounting successor to Ceridian for financial reporting purposes.

The accompanying unaudited financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (the U.S. ) 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 of the information and footnotes required by accounting principles generally accepted in the U.S. for complete financial statements. In the opinion of management, all adjustments considered for fair presentation have been included. The consolidated balance sheet at December 31, 2001 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the U.S. for complete financial statements. For further information, refer to the consolidated financial statements and footnotes thereto included in the Arbitron Inc. annual report on Form 10-K for the year ended December 31, 2001.

*Consolidation*

The consolidated financial statements of Arbitron reflect the consolidated financial position, results of operations and cash flows of Arbitron Inc. and its subsidiaries: Arbitron Holdings Inc., Ceridian Infotech (India) Private Limited, CSW Research Limited and Euro Fieldwork Limited. In periods ended prior to March 31, 2001, the Company's financial statements reflected the combined financial position and results of operations of Arbitron (The Arbitron Company which was a division of Ceridian and CSW Research Limited, Euro Fieldwork Limited and Ceridian Infotech (India) Private Limited, each of which was a wholly owned subsidiary of Ceridian).

**2. Goodwill and Other Intangible Assets**

Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, was adopted on January 1, 2002, with the exception of a provision for acquisitions occurring after June 30, 2001, which was adopted on July 1, 2001. Under SFAS No. 142, the Company is no longer amortizing goodwill, rather goodwill is measured for impairment on an annual basis under the guidance set forth in the standard. Additionally, SFAS No. 142 requires disclosure of pro forma net income and earnings per share for prior periods as if the standard was in effect for all periods presented.

**ARBITRON INC.**

Notes to Consolidated Financial Statements Continued  
 June 30, 2002  
 (unaudited)

Intangible assets with finite lives are being amortized to expense over their estimated useful lives. As of June 30, 2002, the Company has no other intangible assets with indefinite useful lives.

The following unaudited information presents the results of operations of the Company as if SFAS No. 142 had been adopted on January 1, 2001 (Dollars in thousands, except per share data).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2002	2001	2002	2001
Net income, as reported	\$6,618	\$4,714	\$20,860	\$21,009
Goodwill amortization, net of tax		426		852
Net income, as adjusted	\$6,618	\$5,140	\$20,860	\$21,861
Net income and pro forma net income per weighted average common share				
Basic	\$ 0.23	\$ 0.18	\$ 0.71	\$ 0.75
Diluted	\$ 0.22	\$ 0.18	\$ 0.70	\$ 0.75

The Company has completed its assessment of the carrying value of goodwill as of January 1, 2002 and has determined no impairment existed as of that date.

**3. Purchase Acquisition**

On July 2, 2001, the Company acquired all of the assets and assumed certain liabilities of the radio network audience measurement service business of Statistical Research, Inc. ( SRI ), known as Radio s All Dimension Audience Research ( RADAR ). The RADAR service measures national radio audiences and the audience size of network radio programs and commercials. The primary reason for the acquisition was to gain entry into the network radio measurement business. Arbitron plans to provide larger sample sizes to customers by combining Arbitron s existing diary sampling process with the RADAR network commercial clearance system.

On June 28, 2002, the Company paid the final installment of \$11.0 million, bringing the aggregate consideration paid to \$25.3 million. In connection with the acquisition, the Company entered into several operational agreements with SRI, including a software development agreement pursuant to which SRI adapted RADAR to the Company s diary based ratings measurement method.

**ARBITRON INC.**

Notes to Consolidated Financial Statements Continued  
 June 30, 2002  
 (unaudited)

The following unaudited pro forma information presents the results of operations of the Company as if the RADAR acquisition had occurred as of January 1, 2001 (Dollars in thousands, except per share data).

	<b>Three Months Ended June 30, 2001</b>	<b>Six Months Ended June 30, 2001</b>
Pro forma revenue	\$ 52,691	\$ 115,323
Pro forma net income	\$ 4,975	\$ 21,532
Pro forma diluted net income per weighted average common share	\$ 0.17	\$ 0.73

**4. Long-term Debt**

Long-term debt consists of the following (Dollars in thousands):

	<b>June 30, 2002</b>	<b>December 31, 2001</b>
Senior fixed rate notes	\$ 50,000	\$ 50,000
Long-term revolving credit facility	145,000	155,000
	<b>\$ 195,000</b>	<b>\$ 205,000</b>

On January 31, 2001, the Company entered into a \$225.0 million five-year revolving credit agreement with a consortium of banks ( Credit Facility ). On March 29, 2001, in connection with the spin-off, \$200.0 million was drawn on the facility and distributed to Ceridian.

The Credit Facility has two borrowing options, a Eurodollar rate option or a base rate option, as defined in the agreement. Under the Eurodollar option, the Company may elect interest periods of one, two, three or six months at the inception date and each renewal date. Borrowings under the Eurodollar option bear interest at the London Interbank Offered Rate (LIBOR) plus a margin of 2.00% to 2.75%. Borrowings under the base rate option bear interest at the higher of the lead lender's prime rate or the Federal Funds rate plus 50 basis points, plus a margin of .50% to 1.25%. The specific margins, under both options, will be determined based on the Company's ratio of indebtedness to earnings before interest, taxes, depreciation and amortization (leverage ratio), and will be adjusted every ninety days. The agreement contains a commitment fee provision whereby the Company will be charged a fee based on the unused portion of the facility. Under the terms of the Credit Facility, the Company is required to maintain certain other financial ratios, in addition to the leverage ratio, and meet other financial conditions. The agreement limits, among other things, the Company's ability to sell assets, incur additional indebtedness, grant or incur liens on its assets, repay indebtedness, make investments or acquisitions, repurchase or redeem capital stock and engage in certain mergers or consolidations. The agreement prohibits the payment of cash dividends through the year ending December 31, 2002. The interest rate on the Credit Facility borrowings as of June 30, 2002 was 7.40%.

The commitment under the Credit Facility, which was \$225.0 million at inception, was reduced to \$185.2 million on April 1, 2002 in accordance with the mandatory commitment reduction and excess cash flow provisions. Available borrowings under the Credit Facility were \$40.2 million as of June 30, 2002.

**ARBITRON INC.**

Notes to Consolidated Financial Statements    Continued  
June 30, 2002  
(unaudited)

Upon consummation of the spin-off, the Company issued \$50.0 million of senior secured notes due January 31, 2008. In connection with the spin-off, the Company distributed the \$50.0 million of note proceeds to Ceridian. The notes bear interest at a fixed rate of 9.96%. The senior secured notes agreement contains covenants similar to the Credit Facility. The agreement also contains a make-whole provision that applies in the event of early prepayment of principal.

**5. Interest Rate Swap**

The Company entered into an interest rate swap agreement effective on March 29, 2001 to hedge its exposure to fluctuations in interest rates relating to its outstanding variable rate debt. The contract's notional amount was \$200.0 million at inception, and declines over the life of the contract in proportion to the Company's estimated outstanding balance on its revolving credit agreement. Under the terms of the contract, the Company will pay a fixed rate of 5.02% and receive LIBOR, which resets every 90 days. The contract matures on December 31, 2004. The interest rate swap agreement was designated as a cash flow hedge, and was designed to be entirely effective by matching the terms of the swap agreement with the debt. The base rate for both the variable rate debt and the swap is LIBOR and the instruments have the same renewal dates over the lives of the instruments. The fair value of the cash flow hedge was recorded as a non-current liability and the offsetting unrealized loss was recorded in accumulated other comprehensive loss as of June 30, 2002 and December 31, 2001.

The Company's risk management objective for entering into the interest rate swap was to mitigate its exposure to interest rate risk. The Company's initial strategy was to lock into a fixed rate of interest with a pay-fixed, receive-variable interest rate swap, thereby hedging exposure to the variability in future cash flows.

**6. Net Income and Pro Forma Net Income per Weighted Average Common Share**

The computations of basic and diluted net income per common share for the three months ended June 30, 2001 and 2002, and the six months ended June 30, 2002 are based on Arbitron's weighted average shares of common stock and potentially dilutive securities outstanding, respectively. The pro forma net income per weighted average common share computations for the six months ended June 30, 2001, are based on Ceridian's weighted average number of shares of Ceridian common stock and potentially dilutive securities outstanding through March 30, 2001 (the spin-off date), and Arbitron's weighted average shares of common stock and potentially dilutive securities outstanding thereafter.

Potentially dilutive securities are calculated in accordance with the treasury stock method, which assumes that the proceeds from the exercise of all stock options are used to repurchase the Company's common stock at the average market price for the period.

In November 2000, Ceridian's board of directors approved a one-for-five reverse stock split for Arbitron common stock, which was effective immediately after the spin-off. Pro forma net income per common share and weighted average common shares outstanding included in the accompanying consolidated financial statements and related notes have been adjusted to reflect this reverse stock split.

**7. Comprehensive Income**

The Company's comprehensive income is comprised of net income, foreign currency translation adjustments and changes in unrealized gains and losses on the interest rate swap agreement.

**ARBITRON INC.**  
Notes to Consolidated Financial Statements    Continued  
June 30, 2002  
(unaudited)

The components of comprehensive income are as follows (Dollars in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2002	2001	2002	2001
Net income	\$6,618	\$4,714	\$20,860	\$21,009
Items of other comprehensive income				
Change in foreign currency translation adjustment	161	(53)	121	(3)
Change in unrealized gain (loss) on interest rate swap, net of tax	(919)	(50)	86	(338)
Comprehensive income	<u>\$5,860</u>	<u>\$4,611</u>	<u>\$21,067</u>	<u>\$20,668</u>

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion should be read in conjunction with Arbitron's consolidated financial statements and the notes related to those consolidated financial statements contained elsewhere in this Form 10-Q.

**Forward-Looking Statements**

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The statements regarding Arbitron in this document that are not historical in nature, particularly those that utilize terminology such as may, will, should, likely, expects, anticipates, estimates, believes or plans, or comparable terminology, are forward-looking statements that represent current expectations about future events, which Arbitron has derived from information currently available to it. These forward-looking statements involve known and unknown risks and uncertainties that may cause our results to be materially different from results implied in such forward-looking statements. These risks and uncertainties include whether we will be able to:

renew contracts with large customers as they expire;

successfully execute our business strategies, including timely implementation of our Portable People Meter (PPM) and our webcast ratings services, as well as expansion of international operations;

effectively manage the impact of further consolidation in the radio industry;

keep up with rapidly changing technological needs of our customer base, including creating new products and services that meet those needs; and

realize the benefits we expect to achieve resulting from the completion of the reverse spin-off of Ceridian Corporation.

Additional important factors known to Arbitron that could cause forward-looking statements to turn out to be incorrect are identified and discussed from time to time in Arbitron's filings with the Securities and Exchange Commission, including in particular the risk factors discussed under the caption ITEM 1. BUSINESS - Business Risks in Arbitron's Form 10-K for the year ended December 31, 2001.

The forward-looking statements contained in this document speak only as of the date hereof, and Arbitron undertakes no obligation to correct or update any forward-looking statements, whether as a result of new information, future events or otherwise.

**Overview**

Arbitron Inc. was formerly known as Ceridian Corporation (Ceridian). Prior to March 31, 2001, Ceridian, a publicly traded company, had as its principal lines of business the human resource service businesses, the Comdata business, which provided transaction processing and regulatory compliance services for the transportation industry, and the radio audience measurement business.

On March 30, 2001, Ceridian effected a reverse spin-off, which we refer to as the spin-off. In connection with the spin-off, the assets and liabilities associated with the human resource service businesses and Comdata subsidiaries were transferred to New Ceridian. The radio audience measurement business stayed with Ceridian. Ceridian then distributed the stock of New Ceridian to its existing stockholders. As a result, New Ceridian is now a separate publicly traded corporation. In connection with the spin-off, Ceridian changed its name to Arbitron Inc. and effected a one-for-five reverse stock split, and New Ceridian changed its name to Ceridian Corporation. Because of the relative significance of the businesses transferred to New Ceridian, New Ceridian was considered the accounting successor to Ceridian for financial reporting purposes.

The terms Arbitron or the Company as used in this document shall include Arbitron Inc. and its subsidiaries.

The consolidated financial statements of Arbitron reflect the consolidated financial position, results of operations and cash flows of Arbitron Inc. and its subsidiaries: Arbitron Holdings Inc., Ceridian Infotech (India) Private Limited, CSW Research Limited and Euro Fieldwork Limited. In periods ended prior to March 31, 2001, the Company's financial statements reflected the combined financial position and results of operations of Arbitron (The Arbitron Company which was a division of Ceridian and CSW Research Limited, Euro Fieldwork Limited and Ceridian Infotech (India) Private Limited, each of which was a wholly owned subsidiary of Ceridian).

Arbitron's radio audience measurement business has generally accounted for a majority of its revenue. In recent years, significant consolidation of radio station ownership has tended to intensify competition within the radio industry and between radio and other forms of media for advertising dollars. At the same time, audiences have become more fragmented as a result of the greatly increased programming choices and entertainment and media options. Consequently, the increased competition together with the desire for more complex information have driven demand by radio broadcasters, advertising agencies and advertisers for Arbitron's audience measurement information. In addition, although radio industry consolidation has led to the increased concentration of Arbitron's customer base, it has also contributed to an increase in the number of stations subscribing for the ratings service as well as increases in sales of Arbitron's analytical software applications and other services.

Infinity Broadcasting is Arbitron's second largest customer and represented approximately 11% of Arbitron's revenue in 2001. Certain contracts with Infinity Broadcasting, which collectively accounted for nine percent of Arbitron's revenue in 2001, expired at the end of 2001 and renewal negotiations commenced during the fourth quarter of 2001. In July 2002, Arbitron entered into an extension of the radio ratings license agreement with Infinity Broadcasting, which gives their stations access to our quarterly radio ratings up to the release of the Spring 2003 radio survey as well as access to additional services currently provided. In addition, in July 2002, Arbitron also entered into an extension of the radio ratings license agreement with ABC Radio up to the release of the Spring 2003 radio survey. The one year extensions with Infinity Broadcasting and ABC Radio are for significantly shorter terms than the typical four to five year agreements between Arbitron and its customers. Arbitron believes that this is a result of customers currently waiting for a more detailed analysis of the PPM Philadelphia test market and a rollout plan for other major markets. Additionally, future contracts with other customers may be of a shorter than normal term until the PPM data analysis is available and the PPM rollout plan is established. Arbitron cannot give any assurances that it could replace the revenue that could be lost if a key customer failed to renew its agreement with Arbitron. The loss of a key customer would materially harm Arbitron's business and operating results.

#### **Critical Accounting Policies**

Critical accounting policies are those that are both important to the presentation of our financial condition and results of operations and require management's most difficult, complex or subjective judgments. The Company's most critical accounting policies relate to the capitalization of software development costs and impairments of assets.

The Company capitalizes software development costs with respect to major product initiatives or enhancements, which are incurred during the period from the time of technological feasibility until the time that the software is ready for use. To the extent that software is being developed for use by customers or to support data collection activities, the Company also considers the recovery of such costs through future revenue streams in its decision to capitalize software development costs. Once the software is placed in service, the capitalized costs are generally amortized over periods of three to five years. If events or changes in circumstances indicate that the carrying value of software may not be recovered, a recoverability analysis is performed based on estimated undiscounted cash flows to be generated from the software in the future. If the analysis indicates that the carrying value is not recoverable from future cash flows, the software cost is written down to estimated fair value and an impairment loss is recognized. The Company's estimates are subject to revision as market conditions and the Company's assessments of them change.

In 2002, and annually thereafter, the Company will assess the fair value of goodwill. To the extent that information indicates that the carrying value of the assets exceeds their estimated fair values, the Company will recognize an impairment charge. The Company's estimates of fair value will be subject to revision as market conditions and the Company's assessments of them change.



**New Accounting Pronouncements**

Statement of Financial Accounting Standards (SFAS) No. 142 was adopted on January 1, 2002, with the exception of a provision for acquisitions occurring after June 30, 2001 which was adopted on July 1, 2001. Under SFAS No. 142, the Company's goodwill is no longer amortized to expense, rather goodwill is measured for impairment on an annual basis under the guidance set forth in the standard. Additionally, SFAS No. 142 requires disclosure of pro forma net income and earnings per share for prior periods as if the standard was in effect for all periods presented. For the year ending December 31, 2002, the Company expects that the reduction in amortization expense will increase net income by approximately \$1.7 million. If the Company had adopted the provisions of SFAS No. 142 on January 1, 2001, net income and diluted net income per weighted average share would have been \$5,140 and \$0.18, respectively, for the three months ended June 30, 2001, and \$21,861 and \$0.75, respectively, for the six months ended June 30, 2001.

**Results of Operations****Comparison of the Three Months Ended June 30, 2002 to the Three Months Ended June 30, 2001.**

The following table sets forth information with respect to the consolidated statements of income of Arbitron.

**Consolidated Statements of Income**  
(Dollars in thousands, except per share amounts)

	Three Months Ended		Increase (Decrease)		Percentage of Revenue	
	June 30,		Dollar	Percent	2002	2001
	2002	2001				
Revenue	\$56,509	\$50,264	\$ 6,245	12.4%	100.0%	100.0%
Costs and expenses						
Cost of revenue	26,046	22,811	3,235	14.2%	46.1%	45.4%
Selling, general and administrative	12,986	11,951	1,035	8.7%	23.0%	23.8%
Research and development	5,803	5,638	165	2.9%	10.3%	11.2%
Total costs and expenses	44,835	40,400	4,435	11.0%	79.4%	80.4%
Operating income	11,674	9,864	1,810	18.3%	20.6%	19.6%
Equity in net income of affiliate	3,312	2,942	370	12.6%	5.9%	5.9%
Income before interest and income tax expense	14,986	12,806	2,180	17.0%	26.5%	25.5%
Interest income	124	354	(230)	(65.0%)	0.2%	0.7%
Interest expense	4,348	5,352	(1,004)	(18.8%)	7.7%	10.6%
Income before income tax expense	10,762	7,808	2,954	37.8%	19.0%	15.5%
Income tax expense	4,144	3,094	1,050	33.9%	7.3%	6.2%
Net income	\$ 6,618	\$ 4,714	\$ 1,904	40.4%	11.7%	9.3%
Net income per weighted average common share						
Basic	\$ 0.23	\$ 0.16	\$ 0.07	43.8%		
Diluted	\$ 0.22	\$ 0.16	\$ 0.06	37.5%		
Other data:						
EBITDA	\$16,065	\$13,946	\$ 2,119	15.2%	28.4%	27.7%



## Edgar Filing: ARBITRON INC - Form 10-Q

**Revenue.** Revenue increased 12.4% from \$50.3 million for the three months ended June 30, 2001 to \$56.5 million for the same period in 2002. RADAR accounted for \$2.3 million or 4.6% out of the 12.4% growth. Increases in the ratings subscriber base, analytical software applications, escalations in multi-year customer contracts and contract renewals accounted for most of the remaining \$3.9 million increase.

**Cost of Revenue.** Cost of revenue increased 14.2% from \$22.8 million for the three months ended June 30, 2001 to \$26.0 million for the same period in 2002, and increased as a percentage of revenue from 45.4% in 2001 to 46.1% in 2002. RADAR accounted for \$0.2 million of the dollar increase. The remaining dollar increase of \$3.0 million is mainly attributed to increases in diary and data collection costs (\$1.0 million), computer center costs (\$0.4 million), royalties (\$0.6 million), and PPM costs (\$0.6 million).

**Selling, General and Administrative.** Selling, general and administrative expenses increased 8.7% from \$12.0 million for the three months ended June 30, 2001 to \$13.0 million for the same period in 2002 but decreased as a percentage of revenue from 23.8% in 2001 to 23.0% in 2002. RADAR expenses accounted for \$0.3 million of the dollar increase. The remaining dollar increase of \$0.7 million is attributed to increases in certain variable costs, including marketing expenses related to PPM (\$0.6 million) and overall increases in selling expenses (\$0.5 million). These increases were partially offset by the elimination of goodwill amortization, in accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, which was \$0.4 million in 2001.

**Research and Development.** Research and development increased 2.9% from \$5.6 million during the three months ended June 30, 2001 to \$5.8 million for the same period in 2002 but decreased as a percentage of revenue from 11.2% in 2001 to 10.3% in 2002. RADAR costs and core services costs increased by \$0.4 million and \$0.6 million, respectively. These increases were offset by decreases in webcast ratings and PPM costs of \$0.9 million.

**Operating Income.** Operating income increased 18.3% from \$9.9 million for the three months ended June 30, 2001 to \$11.7 million for the same period in 2002. Operating margin increased from 19.6% in 2001 to 20.6% in 2002.

**Equity in Net Income of Affiliate.** Equity in net income of affiliate increased 12.6% from \$2.9 million for the three months ended June 30, 2001 to \$3.3 million for the same period in 2002.

**Interest Expense.** Interest expense decreased 18.8% from \$5.4 million for the three months ended June 30, 2001 to \$4.3 million for the same period in 2002. The decrease is the result of a lower debt principal balance outstanding under the Company's revolving credit facility in 2002.

**Income Tax Expense.** Arbitron's effective tax rate was 39.5% and 38.5% for the three months ended June 30, 2001 and 2002, respectively. The 1.0% decrease in the Company's effective income tax rate resulted from the discontinuance of goodwill amortization in accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, and a change in certain state tax apportionment factors following the spin-off from Ceridian.

**Net Income.** Net income increased 40.4% from \$4.7 million for the three months ended June 30, 2001 to \$6.6 million for the same period in 2002.

**EBITDA.** EBITDA increased 15.2% from \$13.9 million for the three months ended June 30, 2001 to \$16.1 million for the same period in 2002.

Edgar Filing: ARBITRON INC - Form 10-Q

*Comparison of the Six Months Ended June 30, 2002 to the Six Months Ended June 30, 2001*

The following table sets forth information with respect to the consolidated statements of income of Arbitron.

**Consolidated Statements of Income**  
(Dollars in thousands, except per share amounts)

	Six Months Ended		Increase (Decrease)		Percentage of Revenue	
	June 30,		Dollar	Percent	2002	2001
	2002	2001				
Revenue	\$ 122,411	\$ 110,454	\$ 11,957	10.8%	100.0%	100.0%
Costs and expenses						
Cost of revenue	44,909	38,684	6,225	16.1%	36.7%	35.0%
Selling, general and administrative	25,663	23,165	2,498	10.8%	21.0%	21.0%
Research and development	11,315	10,334	981	9.5%	9.2%	9.4%
Total costs and expenses	81,887	72,183	9,704	13.4%	66.9%	65.4%
Operating income	40,524	38,271	2,253	5.9%	33.1%	34.6%
Equity in net income of affiliate	2,067	1,819	248	13.6%	1.7%	1.7%
Income before interest and income tax expense	42,591	40,090	2,501	6.2%	34.8%	36.3%
Interest income	262	373	(111)	(29.8%)	0.2%	0.3%
Interest expense	8,934	5,738	3,196	55.7%	7.3%	5.2%
Income before income tax expense	33,919	34,725	(806)	(2.3%)	27.7%	31.4%
Income tax expense	13,059	13,716	(657)	(4.8%)	10.7%	12.4%
Net income	\$ 20,860	\$ 21,009	\$ (149)	(0.7%)	17.0%	19.0%
Net income and pro forma net income per weighted average common share						
Basic	\$ 0.71	\$ 0.72	\$ (0.01)	(1.4%)		
Diluted	\$ 0.70	\$ 0.72	\$ (0.02)	(2.8%)		
Other data:						
EBITDA	\$ 44,653	\$ 42,305	\$ 2,348	5.6%	36.5%	38.3%

**Revenue.** Revenue increased 10.8% from \$110.5 million during the six months ended June 30, 2001 to \$122.4 million for the same period in 2002. RADAR accounted for \$4.5 million or 4.1% out of the 10.8% growth. Increases in the ratings subscriber base, analytical software applications, escalations in multi-year customer contracts and contract renewals accounted for the remaining \$7.5 million increase.

**Cost of Revenue.** Cost of revenue increased 16.1% from \$38.7 million for the six months ended June 30, 2001 to \$44.9 million for the same period in 2002, and increased as a percentage of revenue from 35.0% in 2001 to 36.7% in 2002. RADAR accounted for \$1.1 million of the dollar increase. The remaining dollar increase of \$5.1 million is mainly attributed to increases in diary and data collection costs (\$1.7 million), computer center costs (\$0.6 million), royalties (\$1.0 million) and PPM costs (\$1.6 million).

**Selling, General and Administrative.** Selling, general and administrative expenses increased 10.8% from \$23.2 million for the six months ended June 30, 2001 to \$25.7 million for the same period in 2002 and remained consistent at 21.0% of revenue. RADAR accounted for \$0.5 million of the dollar increase. The remaining dollar increase of \$2.0 million is mainly attributed to increases in certain variable costs,

## Edgar Filing: ARBITRON INC - Form 10-Q

including marketing expenses related to PPM (\$0.9 million), higher overall administrative costs (\$0.9 million), and overall increases in selling expenses (\$1.3 million). These increases were offset by the elimination of goodwill amortization, in accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, which was \$0.8 million in 2001.

## Edgar Filing: ARBITRON INC - Form 10-Q

**Research and Development.** Research and development increased 9.5% from \$10.3 million during the six months ended June 30, 2001 to \$11.3 million for the same period in 2002 but decreased as a percentage of revenue from 9.4% in 2001 to 9.2% in 2002. RADAR costs and core services costs increased by \$0.8 million and \$2.0 million, respectively. These increases were partially offset by decreases in webcast ratings and PPM costs of \$1.9 million.

**Operating Income.** Operating income increased 5.9% from \$38.3 million for the six months ended June 30, 2001 to \$40.5 million for the same period in 2002. Operating margin decreased from 34.6% in 2000 to 33.1% in 2002.

**Equity in Net Income of Affiliate.** Equity in net income of affiliate increased 13.6% from \$1.8 million for the six months ended June 30, 2001 to \$2.1 million for the same period in 2002.

**Interest Expense.** Interest expense increased 55.7% from \$5.7 million for the six months ended June 30, 2001 to \$8.9 million for the same period in 2002. The increase is the result of having debt outstanding for approximately three months in 2001 compared to six months in 2002.

**Income Tax Expense.** Arbitron's effective tax rate was 39.5% and 38.5% for the three months ended March 31, 2001 and 2002, respectively. The 1.0% decrease in the Company's effective income tax rate resulted from the discontinuance of goodwill amortization in accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, and a change in certain state tax apportionment factors following the spin-off from Ceridian.

**Net Income.** Net income decreased 0.7% from \$21.0 million for the six months ended June 30, 2001 to \$20.9 million for the same period in 2002.

**EBITDA.** EBITDA increased 5.6% from \$42.3 million for the six months ended June 30, 2001 to \$44.7 million for the same period in 2002.

### Liquidity and Capital Resources

Prior to the spin-off, Arbitron participated in Ceridian's centralized cash management system to finance its operations. Cash deposits from the majority of Arbitron's operations were transferred to Ceridian on a daily basis and Ceridian funded Arbitron's cash disbursements from the centralized cash management system. Accordingly, Arbitron's net change in cash in periods prior to the spin-off on March 30, 2001 is not indicative of its liquidity or cash flow as a stand-alone company.

As of June 30, 2002, the Company had \$24.2 million in available cash and cash equivalents. In addition, the Company had \$40.2 million in available borrowings under its bank credit facility. Although Arbitron has a limited history as a stand-alone company, management expects that cash flow generated from operations, as well as available borrowings from its bank credit facility, if necessary, will be sufficient to support the Company's operations, including research and development costs, for the foreseeable future.

Net cash provided by operating activities was \$28.5 million and \$26.8 million for the six months ended June 30, 2002 and 2001, respectively, an increase of \$1.7 million. The increase is mainly attributed to better efficiency in collections of accounts receivable and the Company's tax benefit from stock option exercises, partially offset by lower utilization of deferred tax assets.

Net cash used in investing activities was \$19.8 million and \$6.2 million for the six months ended June 30, 2002 and 2001, respectively, an increase of \$13.6 million. The increase is primarily attributed to payments of \$15.0 million to the former owners of RADAR during the six months ended June 30, 2002, compared to \$3.0 million of business acquisition payments during the same period in 2001. Additionally, the Company acquired \$4.8 million of property and equipment during the six month period ended June 30, 2002, compared to \$3.3 million during the same period in 2001. The increase in property and equipment additions is largely related to hardware and internally developed software related to PPM.

Net cash provided by (used in) financing activities was (\$5.6) million and \$1.1 million for the six month periods ended June 30, 2002 and 2001, respectively, a decrease of \$6.7 million. The decrease is mainly attributed to cash flow related to the spin-off distribution in 2001. During the six months ended June 30, 2001, the Company had proceeds of \$250.0 million from debt issuance and distributed cash of \$236.0 million to Ceridian and paid financing costs of \$3.0 million, resulting in \$11.0 million of cash provided by investing activities after payment of debt issue costs. There were no such debt issuance and distribution activities during the same period in 2002. Partly offsetting the \$11.0 million decrease related to the spin-off distribution was \$4.4 million of cash received from stock option exercises and stock purchase plans for the six months ended June 30, 2002, compared to \$0.1 million for the six months ended June 30, 2001.

Arbitron's credit facility and senior secured notes ( borrowings ) contain non-investment grade financial terms, covenants and operating restrictions that increase the cost of financing and restrict financial flexibility. Under the terms of the borrowings, Arbitron is required to maintain certain leverage and coverage ratios and meet other financial conditions. The agreements limit, among other things, Arbitron's ability to sell assets, incur additional indebtedness, grant or incur liens on its assets, repay senior indebtedness, pay cash dividends, make certain investments or acquisitions, repurchase or redeem capital stock and engage in certain mergers or consolidations. Although Arbitron does not believe that the terms of its borrowings limit the operation of its business in any material respect, the terms may restrict or prohibit Arbitron's ability to raise additional capital when needed or could prevent Arbitron from making acquisitions or investing in other growth initiatives. Arbitron holds a derivative instrument as a hedge of its variable interest rate debt as indicated below under Item 3. Quantitative and Qualitative Disclosures About Market Risk.

In 2001, Clear Channel Communications, Inc. and Infinity Broadcasting Corp. represented approximately 23.0% and 11.0%, respectively, of Arbitron's revenue. Arbitron's agreements with these customers are not exclusive and contain no renewal obligations. Certain contracts with Infinity Broadcasting, which collectively accounted for nine percent of Arbitron's revenue in 2001, expired at the end of 2001 and renewal negotiations commenced during the fourth quarter of 2001. In July 2002, Arbitron entered into an extension of the radio ratings license agreement with Infinity Broadcasting which gives their stations access to our quarterly radio ratings up to the release of the Spring 2003 radio survey as well as access to additional services currently provided. In addition, in July 2002, Arbitron also entered into an extension of the radio ratings license agreement with ABC Radio up to the release of the Spring 2003 radio survey. The one year extensions with Infinity Broadcasting and ABC Radio are for significantly shorter terms than the typical four to five year agreements between Arbitron and its customers. Arbitron believes that this is a result of customers currently waiting for a more detailed analysis of the PPM Philadelphia test market and a rollout plan for other major markets. Arbitron cannot give any assurances that it could replace the revenue that could be lost if a key customer failed to renew its agreement with Arbitron. The loss of a key customer would adversely affect Arbitron's results of operations and liquidity.

The continuing development and anticipated rollout of the PPM service will require significant capital resources and will increase our operating costs over the next several years. The introduction of the PPM could be delayed if Arbitron does not form a joint venture. In that event, Arbitron would need to revise its plans and assumptions relating to the timing of the PPM rollout. Additionally, agreements with customers may continue to be of a shorter than normal term until a more detailed analysis of the Philadelphia test market is completed and a rollout plan into other markets is established. It is expected that within the next year this additional analysis will have been completed so that Arbitron's customers will have a fuller understanding of the value of the PPM service, which will then serve as the basis for longer-term renewal contract negotiations.

**Seasonality**

Arbitron recognizes revenue for products and services over the terms of license agreements as products and services are delivered, and expenses are recognized as incurred. Arbitron gathers radio-listening data in approximately 283 United States local markets. All markets are measured at least twice per year (April, May, June, Spring Survey, and October, November, December, Fall Survey ). In addition, major markets are measured two additional times per year (January, February, March, Winter Survey, and July, August, September Summer Survey ). Arbitron's revenue is generally higher in the first and third quarters as the result of the delivery of the Fall Survey and Spring Survey, respectively, to all markets compared to revenue in the second and fourth quarters when delivery of the Winter Survey and Summer Survey, respectively, is only delivered to major markets. Arbitron's expenses are generally higher in the second and fourth quarters as the Spring Survey and Fall Survey are being conducted.



**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE OF MARKET RISK**

***Interest Risk***

The Company currently has no exposure to market risk with respect to changes in interest rates because the variable portion of the Company's long-term obligations is fully hedged with a derivative instrument. The Company does not use derivatives for speculative or trading purposes.

The Company has two long-term obligations: senior notes that bear interest at a fixed rate of 9.96%, and a revolving credit facility which bears interest at LIBOR plus a margin of 2.00% to 2.75%. The variable portion of the interest rate, LIBOR, is hedged with an interest rate swap, which has a fixed rate of 5.02%.

Due to the variable rate debt being fully hedged, a hypothetical market interest rate change of 1% would have no effect on the Company's results of operations. However, changes in market interest rates would impact the fair values of the Company's long-term obligations.

***Foreign Currency Risk***

Arbitron's foreign operations are not significant at this time, and, therefore, Arbitron's exposure to foreign currency risk is minimal.

**PART II OTHER INFORMATION**

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

Arbitron's annual meeting of stockholders was held on May 30, 2002. There were 29,252,346 shares of Arbitron common stock outstanding and entitled to vote at the annual meeting. Of the 29,252,346 shares of Arbitron common stock entitled to vote at the annual meeting, a total of 26,740,919 shares were present in person or by proxy at the annual meeting.

The following eight people designated by Arbitron's Board of Directors as nominees for director were elected at the annual meeting, with the voting as follows:

Nominee	Votes For	Votes Withheld
Erica Farber	26,731,829	9,090
Kenneth F. Gorman	26,629,535	111,384
Philip Guarascio	26,731,192	9,727
Larry E. Kittelberger	26,629,092	111,827
Stephen B. Morris	26,730,955	9,964
Luis G. Nogales	26,731,121	9,798
Lawrence Perlman	26,728,703	12,216
Richard A. Post	26,629,612	111,307

No additional items were on the agenda of the annual meeting of stockholders and no items were brought to a vote during the meeting.

**ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K**

(a) Exhibits

Exhibit No.	Description
99.1	Certifications of Chief Executive Officer and Chief Financial Officer

(b) Reports on Form 8-K

Arbitron filed a Current Report on Form 8-K on April 18, 2002 reporting 2002 first quarter financial results.

Edgar Filing: ARBITRON INC - Form 10-Q

SIGNATURE

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, we have duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ARBITRON INC

By: /s/ WILLIAM J. WALSH

---

William J. Walsh  
Executive Vice President of Finance and Planning and  
Chief Financial Officer, authorized signatory and  
principal financial officer

Date: August 14, 2002