

LEE ENTERPRISES, INC  
Form 10-Q  
February 06, 2009  
Table of Contents

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 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 December 28, 2008**

OR

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

Commission File Number 1-6227

# LEE ENTERPRISES, INCORPORATED

(Exact name of Registrant as specified in its Charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)  
42-0823980  
(I.R.S. Employer Identification No.)  
201 N. Harrison Street, Suite 600, Davenport, Iowa 52801

(Address of principal executive offices)

(563) 383-2100

(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

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

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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 Exchange Act). Yes  No

As of December 28, 2008, 39,019,847 shares of Common Stock and 5,912,657 shares of Class B Common Stock of the Registrant were outstanding.

**Table of Contents**

| TABLE OF CONTENTS   | PAGE |
|---|------|
| <u>FORWARD LOOKING STATEMENTS</u>   | 1    |
| PART I <u>FINANCIAL INFORMATION</u>   |      |
| Item 1. <u>Financial Statements (unaudited)</u>   | 2    |
| <u>Consolidated Statements of Operations and Comprehensive Income (Loss) 13 weeks ended December 28, 2008 and December 30, 2007</u> | 2    |
| <u>Consolidated Balance Sheets December 28, 2008 and September 28, 2008</u>   | 3    |
| <u>Consolidated Statements of Cash Flows 13 weeks ended December 28, 2008 and December 30, 2007</u>                                 | 4    |
| <u>Notes to Consolidated Financial Statements</u>   | 5    |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                                | 17   |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>   | 28   |
| Item 4. <u>Controls and Procedures</u>  | 29   |
| PART II <u>OTHER INFORMATION</u>  |      |
| Item 1. <u>Legal Proceedings</u>  | 30   |
| Item 2(c). <u>Issuer Purchases of Equity Securities</u>   | 30   |
| Item 6. <u>Exhibits</u>   | 30   |
| <u>SIGNATURES</u>   | 30   |

**Table of Contents**

**FORWARD-LOOKING STATEMENTS**

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. This report contains information that may be deemed forward-looking, that is based largely on, Lee Enterprises, Incorporated's (the Company) current expectations, and is subject to certain risks, trends and uncertainties that could cause actual results to differ materially from those anticipated. Among such risks, trends and other uncertainties, which in some instances are beyond its control, are the Company's ability to generate cash flows and maintain liquidity sufficient to service its debt, and comply with or obtain amendments or waivers of the financial covenants contained in its credit facilities, if necessary. Other risks and uncertainties include the impact of continuing adverse economic conditions, potential changes in advertising demand, newsprint and other commodity prices, energy costs, interest rates and the availability of credit due to instability in the credit markets, labor costs, legislative and regulatory rulings and other results of operations or financial conditions, difficulties in maintaining employee and customer relationships, increased capital and other costs, competition and other risks detailed from time to time in the Company's publicly filed documents. The words "may", "will", "would", "could", "believes", "expects", "anticipates", "intends", "plans", "projects", "considers" and similar expressions are used in forward-looking statements. Readers are cautioned not to place undue reliance on such forward-looking statements, which are made as of the date of this report. The Company does not undertake to publicly update or revise its forward-looking statements.

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements****LEE ENTERPRISES, INCORPORATED****CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)**

(Unaudited)

|  | 13 Weeks Ended |              |
|--|----------------|--------------|
|  | December 28,   | December 30, |
|  | 2008           | 2007         |
| <i>(Thousands, Except Per Common Share Data)</i>             |                |              |
| Operating revenue:   |                |              |
| Advertising  | \$184,583      | \$217,570    |
| Circulation  | 47,556         | 49,805       |
| Other  | 11,416         | 12,481       |
| Total operating revenue                                      | 243,555        | 279,856      |
| Operating expenses:  |                |              |
| Compensation   | 94,483         | 108,194      |
| Newsprint and ink  | 25,154         | 25,103       |
| Other operating expenses                                     | 69,950         | 74,126       |
| Depreciation   | 8,296          | 8,159        |
| Amortization of intangible assets                            | 12,103         | 14,872       |
| Impairment of goodwill                                       | 67,781         | -            |
| Unrealized losses on property and equipment                  | 2,264          | -            |
| Workforce adjustments  | 838            | -            |
| Total operating expenses                                     | 280,869        | 230,454      |
| Equity in earnings of associated companies                   | 3,064          | 4,301        |
| Operating income (loss)                                      | (34,250)       | 53,703       |
| Non-operating income (expense):                              |                |              |
| Financial income   | 1,271          | 1,796        |
| Financial expense  | (20,008)       | (20,850)     |
| Total non-operating expense, net                             | (18,737)       | (19,054)     |
| Income (loss) before income taxes                            | (52,987)       | 34,649       |
| Income tax expense (benefit)                                 | (5,524)        | 12,254       |
| Minority interest  | 170            | 607          |
| Income (loss) from continuing operations                     | (47,633)       | 21,788       |
| Discontinued operations, net                                 | (5)            | 338          |
| Net income (loss)  | (47,638)       | 22,126       |
| Increase in redeemable minority interest                     | 1,039          | -            |
| Net income (loss) available to common stockholders           | (48,677)       | 22,126       |
| Other comprehensive loss, net                                | (1,746)        | (2,455)      |
| Comprehensive income (loss) available to common stockholders | \$ (50,423)    | \$ 19,671    |
| Earnings (loss) per common share:                            |                |              |
| Basic:   |                |              |
| Continuing operations  | \$(1.10)       | \$0.48       |
| Discontinued operations                                      | -              | 0.01         |
|  | \$(1.10)       | \$0.48       |
| Diluted:   |                |              |

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|                            |          |        |
|----------------------------|----------|--------|
| Continuing operations      | \$(1.10) | \$0.48 |
| Discontinued operations    | -        | 0.01   |
|                            | \$(1.10) | \$0.48 |
| Dividends per common share | \$ -     | \$0.19 |

The accompanying Notes are an integral part of the Consolidated Financial Statements.

**Table of Contents****LEE ENTERPRISES, INCORPORATED****CONSOLIDATED BALANCE SHEETS**

(Unaudited)

|  | 13 Weeks Ended |                      |
|--|----------------|----------------------|
|  | December 28,   | September 28,        |
|  | 2008           | 2008                 |
|  |                | Revised - See Note 2 |
| <i>(Thousands, Except Per Share Data)</i>  |                |                      |
| <b>ASSETS</b>  |                |                      |
| Current assets:  |                |                      |
| Cash and cash equivalents  | \$ 26,177      | \$ 23,459            |
| Accounts receivable, net   | 110,308        | 100,380              |
| Inventories  | 15,197         | 18,952               |
| Other  | 11,845         | 10,988               |
| Total current assets   | 163,527        | 153,779              |
| Investments  | 98,022         | 97,643               |
| Restricted cash and investments  | 129,810        | 126,060              |
| Property and equipment, net  | 286,199        | 292,828              |
| Goodwill   | 559,242        | 627,023              |
| Other intangible assets, net   | 689,081        | 701,184              |
| Other  | 23,662         | 17,850               |
| Total assets   | \$1,949,543    | \$2,016,367          |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>   |                |                      |
| Current liabilities:   |                |                      |
| Current maturities of long-term debt   | \$1,362,576    | \$1,337,640          |
| Accounts payable   | 36,922         | 53,827               |
| Compensation and other accrued liabilities   | 50,631         | 60,416               |
| Income taxes payable   | 6,189          | 5,431                |
| Dividends payable  | -              | 8,539                |
| Unearned revenue   | 38,920         | 38,871               |
| Total current liabilities  | 1,495,238      | 1,504,724            |
| Pension obligations  | 2,778          | 2,803                |
| Postretirement and postemployment benefit obligations                                  | 58,972         | 58,767               |
| Deferred income taxes  | 176,147        | 187,869              |
| Other  | 36,759         | 34,442               |
| Redeemable and other minority interest   | 73,452         | 72,244               |
| Total liabilities  | 1,843,346      | 1,860,849            |
| Stockholders equity:   |                |                      |
| Serial convertible preferred stock, no par value; authorized 500 shares; none issued   | -              | -                    |
| Common Stock, \$2 par value; authorized 120,000 shares; issued and outstanding:        | 78,040         | 78,222               |
| December 28, 2008: 39,020 shares;  |                |                      |
| September 28, 2008: 39,111 shares  |                |                      |
| Class B Common Stock, \$2 par value; authorized 30,000 shares; issued and outstanding: | 11,826         | 11,958               |
| December 28, 2008: 5,913 shares;   |                |                      |
| September 28, 2008: 5,979 shares   |                |                      |
| Additional paid-in capital   | 135,704        | 134,289              |
| Accumulated deficit  | (160,820)      | (112,144)            |
| Accumulated other comprehensive income   | 41,447         | 43,193               |
| Total stockholders equity  | 106,197        | 155,518              |
| Total liabilities and stockholders equity  | \$1,949,543    | \$2,016,367          |

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The accompanying Notes are an integral part of the Consolidated Financial Statements.



**Table of Contents**

**LEE ENTERPRISES, INCORPORATED**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Unaudited)

| <i>(Thousands)</i>   | 13 Weeks Ended       |                      |
|--|----------------------|----------------------|
|  | December 28,<br>2008 | December 30,<br>2007 |
| <b>Cash provided by operating activities:</b>  |                      |                      |
| Net income (loss)  | \$(47,638)           | \$ 22,126            |
| Results of discontinued operations   | (5)                  | 338                  |
| Income (loss) from continuing operations   | (47,633)             | 21,788               |
| Adjustments to reconcile income (loss) from continuing operations to net cash provided by operating activities of continuing operations: |                      |                      |
| Depreciation and amortization  | 20,399               | 23,031               |
| Impairment of goodwill   | 67,781               | -                    |
| Unrealized losses on property and equipment  | 2,264                | -                    |
| Stock compensation expense   | 1,052                | 1,514                |
| Accretion of debt fair value adjustment  | (2,064)              | (1,959)              |
| Distributions greater than current earnings of associated companies  | 5                    | 798                  |
| Decrease in deferred income taxes  | (10,699)             | (1,551)              |
| Changes in operating assets and liabilities, net of acquisitions:  |                      |                      |
| Increase in receivables  | (9,928)              | (10,184)             |
| Decrease (increase) in inventories and other   | 3,809                | (1,235)              |
| Increase (decrease) in accounts payable, accrued expenses and unearned revenue   | (25,298)             | (17,714)             |
| Change in income taxes receivable or payable   | 758                  | 17,647               |
| Other, net   | 367                  | (189)                |
| Net cash provided by operating activities of continuing operations   | 813                  | 31,946               |
| <b>Cash provided by (required for) investing activities of continuing operations:</b>  |                      |                      |
| Purchases of property and equipment  | (5,301)              | (8,976)              |
| Purchases of marketable securities   | (26,635)             | (39,469)             |
| Sales or maturities of marketable securities   | 21,375               | 23,457               |
| Increase in restricted cash  | 3,292                | 13,186               |
| Acquisitions   | -                    | (1,224)              |
| Other, net   | 370                  | 2,103                |
| Net cash required for investing activities of continuing operations  | (6,899)              | (10,923)             |
| <b>Cash provided by (required for) financing activities of continuing operations:</b>  |                      |                      |
| Proceeds from long-term debt   | 76,625               | 35,000               |
| Payments on long-term debt   | (49,625)             | (56,000)             |
| Financing costs  | (9,702)              | -                    |
| Common stock transactions, net   | 50                   | (424)                |
| Cash dividends paid  | (8,539)              | (6,703)              |
| Net cash provided by (required for) financing activities of continuing operations  | 8,809                | (28,127)             |
| <b>Net cash provided by (required for) discontinued operations:</b>  |                      |                      |
| Operating activities   | (5)                  | (9,075)              |
| Investing activities   | -                    | 23,911               |
| Net increase in cash and cash equivalents  | 2,718                | 7,732                |
| <b>Cash and cash equivalents:</b>  |                      |                      |
| Beginning of period  | 23,459               | -                    |
| End of period  | \$ 26,177            | \$ 7,732             |

The accompanying Notes are an integral part of the Consolidated Financial Statements.



**Table of Contents**

**LEE ENTERPRISES, INCORPORATED**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**1 BASIS OF PRESENTATION**

The Consolidated Financial Statements included herein are unaudited. In the opinion of management, these financial statements contain all adjustments (consisting of only normal recurring items) necessary to present fairly the financial position of Lee Enterprises, Incorporated and subsidiaries (the Company) as of December 28, 2008 and its results of operations and cash flows for the periods presented. The Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and Notes thereto included in the Company's 2008 Annual Report on Form 10-K.

Because of acquisitions, divestitures, seasonal and other factors, the results of operations for the 13 weeks ended December 28, 2008 are not necessarily indicative of the results to be expected for the full year.

The Consolidated Financial Statements include the accounts of the Company and its subsidiaries, all of which are wholly owned, except for its 95% interest in St. Louis Post-Dispatch LLC (PD LLC) and STL Distribution Services LLC (DS LLC), 50% interest in TNI Partners (TNI), 50% interest in Madison Newspapers, Inc. (MNI), and 82.5% interest in INN Partners, L.C. (INN).

Certain amounts as previously reported have been reclassified to conform with the current period presentation. See Note 3.

References to 2009, 2008 and the like mean the fiscal year ended the last Sunday in September.

**Debt and Liquidity**

As discussed more fully in Note 6 (and capitalized terms used below defined), the Company does not have sufficient cash flows to meet both its requirements for 2009 operations and the scheduled April 28, 2009 repayment of the Pulitzer Notes. The Company's ability to extend or refinance the Pulitzer Notes as they become due, to delay the acceleration of debt maturities upon the expiration of existing waivers of default under both the Credit Agreement and Pulitzer Notes, and to avoid future events of default, are factors that raise significant uncertainty about the Company's ability to continue as a going concern. The Company is actively engaged in discussions with the Noteholders of the Pulitzer Notes, and to the extent their approval may also be required, the Lenders under the Credit Agreement, to extend or refinance the Pulitzer Notes. However, the timing and ultimate outcome of such discussions cannot be determined at this time.

The Consolidated Financial Statements do not include all adjustments relating to the recoverability or classification of recorded asset amounts or the amounts or classification of liabilities should the Company be unable to continue as a going concern.

**2 CORRECTION OF AN ERROR**

The Company recorded a \$30,019,000 increase in the valuation allowance for deferred tax assets in the 13 weeks ended September 28, 2008. In the 13 weeks ended December 28, 2008, the Company determined that it had not considered the benefit of net operating loss carrybacks in its determination of the 2008 valuation allowance for deferred tax assets. The correction of this error results in a decrease of \$8,431,000 in the valuation allowance included in net deferred income tax liabilities recorded as of September 28, 2008, a corresponding increase in income tax benefit in the 13 weeks ended September 28, 2008, and a decrease in diluted loss per common share of \$0.19. The Company determined that the impact of this error on previously issued Consolidated Financial Statements is not material. The September 28, 2008 Consolidated Balance Sheet included herein has been revised to reflect the corrected amounts. The corrected amounts related to the 2008 Consolidated Statement of Operations and Comprehensive Income (Loss) will be reflected in subsequent filings on Form 10-K.

### **3 ACQUISITIONS AND DIVESTITURES**

All acquisitions are accounted for as purchases and, accordingly, the results of operations since the respective dates of acquisition are included in the Consolidated Financial Statements.

#### **Acquisitions**

In 2008, the Company purchased a specialty publication at a cost of \$400,000 and a newspaper distribution business at a cost of \$240,000 and made final cash payments totaling \$984,000 related to newspaper distribution businesses purchased in 2007.

#### **Divestitures**

In 2008, the Company sold its daily newspaper in DeKalb, Illinois for \$24,000,000, before income taxes. The transaction resulted in an after tax gain of \$219,000, which is recorded in discontinued operations. Results of DeKalb have been classified as discontinued operations for all periods presented.

**Table of Contents**

Results of discontinued operations consist of the following:

| (Thousands)   | 13 Weeks Ended       |                      |
|---|----------------------|----------------------|
|   | December 28,<br>2008 | December 30,<br>2007 |
| Operating revenue   | \$ -                 | \$1,376              |
| Income from discontinued operations                                 | \$ -                 | \$ 128               |
| Gain (loss) on sale of discontinued operations, before income taxes | (8)                  | 5,867                |
| Income tax expense (benefit)  | (3)                  | 5,657                |
|   | \$ (5)               | \$ 338               |

Tax expense of \$3,382,000 recorded in results of discontinued operations in 2008 is related to goodwill basis differences recognized as a result of the sale of DeKalb operations.

**4 INVESTMENTS IN ASSOCIATED COMPANIES****TNI Partners**

In Tucson, Arizona, TNI, acting as agent for the Company's subsidiary, Star Publishing Company (Star Publishing), and Citizen Publishing Company (Citizen), a subsidiary of Gannett Co. Inc., is responsible for printing, delivery, advertising, and circulation of the *Arizona Daily Star* and *Tucson Citizen* as well as their related online operations and specialty publications. TNI collects all receipts and income and pays substantially all operating expenses incident to the partnership's operations and publication of the newspapers and other media.

Each newspaper is solely responsible for its own news and editorial content. Income or loss of TNI (before income taxes) is allocated equally to Star Publishing and Citizen.

Summarized results of TNI are as follows:

| (Thousands)  | 13 Weeks Ended       |                      |
|--|----------------------|----------------------|
|  | December 28,<br>2008 | December 30,<br>2007 |
| Operating revenue  | \$21,998             | \$27,914             |
| Operating expenses, excluding curtailment gain, workforce adjustments, depreciation and amortization | 18,732               | 19,673               |
| Curtailment gain   | (1,332)              | -                    |
| Workforce adjustments  | 102                  | 247                  |
| Operating income   | \$ 4,496             | \$ 7,994             |
| Company's 50% share of operating income  | \$ 2,248             | \$ 3,997             |
| Less amortization of intangible assets   | 379                  | 1,585                |
| Equity in earnings of TNI  | \$ 1,869             | \$ 2,412             |

Star Publishing's 50% share of TNI depreciation and certain general and administrative expenses associated with its share of the operation and administration of TNI are reported as operating expenses in the Company's Consolidated Statements of Operations and Comprehensive Income (Loss). These amounts totaled \$591,000 and \$221,000 in the 13 weeks ended December 28, 2008 and 13 weeks ended December 30, 2007, respectively.

Annual amortization of intangible assets of TNI is estimated to be \$1,517,000 in each of the 52 week periods ending December 2009 through December 2012 and \$1,340,000 in the 52 week period ending December 2013.

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In January 2009, Citizen announced its intention to sell the assets of, or discontinue publication of, the *Tucson Citizen* by March 21, 2009.

### **Madison Newspapers, Inc.**

The Company has a 50% ownership interest in MNI, which publishes daily and Sunday newspapers, and other publications in Madison, Wisconsin, and other Wisconsin locations, as well as their related online operations. Net income or loss of MNI (after income taxes) is allocated equally to the Company and The Capital Times Company. MNI conducts its business under the trade name Capital Newspapers.

**Table of Contents**

Summarized results of MNI are as follows:

| (Thousands)  | 13 Weeks Ended       |                      |
|--|----------------------|----------------------|
|  | December 28,<br>2008 | December 30,<br>2007 |
| Operating revenue  | \$ 23,384            | \$ 27,860            |
| Operating expenses, excluding transition costs,<br>depreciation and amortization | 18,946               | 20,750               |
| Depreciation and amortization  | 824                  | 1,101                |
| Operating income   | \$ 3,614             | \$ 6,009             |
| Net income   | \$ 2,390             | \$ 3,778             |
| Company's 50% share of net income  | \$ 1,195             | \$ 1,889             |

Debt of MNI totaled \$555,000 and \$2,285,000 at December 28, 2008 and September 28, 2008, respectively.

In 2008, one of MNI's daily newspapers, *The Capital Times*, decreased print publication from six days per week to one day. The change resulted in severance and other transition costs of \$2,578,000 in 2008.

**5 GOODWILL AND OTHER INTANGIBLE ASSETS**

Changes in the carrying value of goodwill are as follows:

| (Thousands)                   | 13 Weeks Ended    |
|-------------------------------|-------------------|
|                               | December 28, 2008 |
| Goodwill, beginning of period | \$627,023         |
| Goodwill impairment           | 67,781            |
| Goodwill, end of period       | \$559,242         |

Identified intangible assets consist of the following:

| (Thousands)                             | December 28, | September 28, |
|---|--------------|---------------|
|   | 2008         | 2008          |
| <b>Nonamortized intangible assets:</b>  |              |               |
| Mastheads                               | \$ 59,869    | \$ 59,869     |
| <b>Amortizable intangible assets:</b>   |              |               |
| Customer and newspaper subscriber lists | 921,642      | 921,642       |
| Less accumulated amortization           | 292,451      | 280,359       |
|   | 629,191      | 641,283       |
| Noncompete and consulting agreements    | 28,658       | 28,658        |
| Less accumulated amortization           | 28,637       | 28,626        |
|   | 21           | 32            |
|   | \$689,081    | \$701,184     |

In assessing the recoverability of its goodwill and other nonamortized intangible assets, the Company makes a determination of the fair value of its business. Fair value is determined using a combination of an income approach, which estimates fair value based upon future revenue, expenses and cash flows discounted to their present value, and a market approach, which estimates fair

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value using market multiples of various financial measures compared to a set of comparable public companies in the publishing industry. An impairment charge will generally be recognized when the carrying amount of the net assets of the business exceeds its estimated fair value.

The required valuation methodology and underlying financial information that are used to determine fair value require significant judgments to be made by management. These judgments include, but are not limited to, long-term projections of future financial performance and the selection of appropriate discount rates used to determine the present value of future cash flows. Changes in such estimates or the application of alternative assumptions could produce significantly different results.

The Company analyzes its goodwill and other nonamortized intangible assets for impairment on an annual basis at the end of its fiscal year, or more frequently if impairment indicators are present. Such indicators of impairment include, but are not limited to, changes in business climate and operating or cash flow losses related to such assets.



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## **Table of Contents**

Due primarily to the continuing and increasing difference between its stock price and the per share carrying value of its net assets, the Company analyzed the carrying value of its net assets as of December 28, 2008. Recent deterioration in the Company's revenue and the overall recessionary operating environment for the Company and other publishing companies were also factors in the timing of the analysis. The Company concluded the fair value of its business did not exceed the carrying value of its net assets as of December 28, 2008.

The Company recorded a pretax, non-cash charge in the 13 weeks ended December 28, 2008 to reduce the carrying value of goodwill by \$67,781,000. The Company recorded \$13,460,000 of income tax benefit related to this charge.

The Company reviews its amortizable intangible assets for impairment when indicators of impairment are present. The Company assesses recovery of these assets by comparing the estimated undiscounted cash flows associated with the asset or asset group with their carrying amount. The impairment amount, if any, is calculated based on the excess of the carrying amount over the fair value of those assets.

The Company also periodically evaluates its determination of the useful lives of amortizable intangible assets. Any resulting changes in the useful lives of such intangible assets will not impact the cash flows of the Company. However, a decrease in the useful lives of such intangible assets would increase future amortization expense and decrease future reported operating results and earnings per common share. The Company tested such assets for impairment as of December 28, 2008, as noted above, and concluded no adjustments to the useful lives of such assets were required.

Annual amortization of intangible assets for each of the 52 week periods ending December 2013 is estimated to be \$48,351,000, \$48,241,000, \$47,385,000, \$44,493,000 and \$42,034,000, respectively.

## **6 DEBT**

### **Credit Agreement**

In 2006, the Company entered into an amended and restated credit agreement (Credit Agreement) with a syndicate of financial institutions (the Lenders). The Credit Agreement provided for aggregate borrowing of up to \$1,435,000,000 and consisted of a \$950,000,000 A Term Loan, \$35,000,000 B Term Loan and \$450,000,000 revolving credit facility. The Credit Agreement matures in June 2012 and amended and replaced a \$1,550,000,000 credit agreement consummated in 2005.

The Credit Agreement is fully and unconditionally guaranteed on a joint and several basis by substantially all of the Company's existing and future, direct and indirect subsidiaries in which the Company holds a direct or indirect interest of more than 50% (the Credit Parties); provided however, that Pulitzer and its subsidiaries will not become Credit Parties for so long as their doing so would violate the terms of the Pulitzer Notes discussed more fully below. The Credit Agreement was secured by first priority security interests in the stock and other equity interests owned by the Credit Parties in their respective subsidiaries.

Debt under the A Term Loan and revolving credit facility bore interest, at the Company's option, at either a base rate or an adjusted Eurodollar rate (LIBOR), plus an applicable margin. The base rate for the facility was the greater of the prime lending rate of Deutsche Bank Trust Company Americas at such time and 0.5% in excess of the overnight federal funds rate at such time. The margin applicable was a percentage determined according to the following: For revolving loans and A Term Loans, maintained as base rate loans: 0%, and maintained as Eurodollar loans: 0.625% to 1.0% depending, in each instance, upon the Company's leverage ratio at such time.

The Company may voluntarily prepay principal amounts outstanding or reduce commitments under the Credit Agreement at any time, in whole or in part, without premium or penalty, upon proper notice and subject to certain limitations as to minimum amounts of prepayments. The Company is required to repay principal amounts, on a quarterly basis until maturity, under the A Term Loan. In addition to the scheduled payments, the Company is required to make mandatory prepayments under the A Term Loan under certain other conditions. Total A Term Loan payments in the 13 weeks ended December 28, 2008 and 2008 were \$35,625,000 and \$62,250,000 respectively.

The Credit Agreement contains customary affirmative and negative covenants for financing of its type. These financial covenants include a maximum total leverage ratio. The total leverage ratio is based primarily on the principal amount of debt, net of cash, which equals \$1,217,787,000 at December 28, 2008, divided by a measure of trailing 12 month operating results which includes

several factors, including distributions from TNI and MNI. The

## **Table of Contents**

Company's total leverage ratio at December 28, 2008 was 5.90:1. The Credit Agreement also includes a minimum interest expense coverage ratio. The Company's interest expense coverage ratio at December 28, 2008 was 2.9:1. At December 28, 2008, the Company was in compliance with such covenants, as waived or amended from time to time.

The Credit Agreement required the Company to apply the net proceeds from asset sales to repayment of the A Term Loan to the extent such proceeds exceed the amount used to purchase assets (other than inventory and working capital) within one year of the asset sales. Repayments in 2008 met required repayments related to its sales transactions.

The Credit Agreement requires the Company to accelerate future payments under the A Term Loan in the amount of 75% of its Excess Cash Flow, as defined, beginning in 2008. The Company had Excess Cash Flow of approximately \$62,000,000 in 2008 and, as a result, paid \$46,325,000 originally due under the A Term Loan in March and June 2009, in December 2008 subsequent to the end of the quarter. The acceleration of such payments due to Excess Cash Flow does not change the due dates of other A Term Loan payments.

## **Amendments to Credit Agreement**

In 2009, the Credit Agreement was amended (the 2009 Amendments).

Under the 2009 Amendments, the Credit Parties pledged substantially all of their tangible and intangible assets, and granted mortgages covering certain real estate, as collateral for the payment and performance of their obligations under the Credit Agreement. Assets of Pulitzer Inc. (Pulitzer), an indirect wholly-owned subsidiary of the Company, the Company's ownership interest in MNI and certain employee benefit plan assets are excluded.

The 2009 Amendments reduce the amount available under the revolving credit facility to \$375,000,000 and eliminate an unused incremental term loan facility. The 2009 Amendments require the Company to suspend stockholder dividends and share repurchases until its total leverage ratio is less than 4.5:1. The 2009 Amendments also limit capital expenditures to \$20,000,000 per year, with a provision for carryover of unused amounts from the prior year. Other covenants ensure that substantially all future cash flows of the Company are required to be directed for debt reduction.

Further, the 2009 Amendments modify other covenants, including restricting the Company's ability to make additional investments and acquisitions without the consent of its Lenders, limiting additional debt beyond that permitted under the Credit Agreement, and limiting the amount of unrestricted cash and cash equivalents the Company may hold to \$15,000,000.

Under the 2009 Amendments, the Company's credit spreads generally increase 200 basis points from the original pricing grid. The maximum rate (for leverage greater than 6.25:1) increased to LIBOR plus 400 basis points. At the December 2008 leverage level, the Company's debt under the Credit Agreement will be priced at LIBOR plus 350 basis points. The base rate margin was changed to 250 basis points.

Under the 2009 Amendments, the Company's total leverage ratio limit will increase from 6.5:1 in December 2008 to 6.75:1 in March 2009, decrease to 6.5:1 in December 2009, decrease to 6.25:1 in September 2010 and decrease to 4.5:1 in December 2010. Each change in the leverage ratio limit noted above is effective on the last day of the fiscal quarter.

The interest expense coverage ratio limit will be 2.0:1 through March 2009, decrease thereafter to 1.7:1 through September 2009, increase thereafter to 1.8:1 through December 2009, increase thereafter to 1.9:1 through March 2010, increase thereafter to 2.0:1 through September 2010, and increase thereafter to 2.5:1.

The Company paid a fee of 0.5% to consenting lenders, which along with the related expenses, totals \$6,478,000. The fees were capitalized and are being expensed over the respective periods of the 2009 Amendments.

## **Pulitzer Notes**

In conjunction with its formation in 2000, PD LLC borrowed \$306,000,000 (Pulitzer Notes) from a group of institutional lenders (the Noteholders). The aggregate principal amount of the Pulitzer Notes is payable in April 2009 and bears interest at an annual rate of 8.05%. The Pulitzer Notes are guaranteed by Pulitzer pursuant to a Guaranty Agreement dated May 1, 2000 (Guaranty Agreement) with the Noteholders. In turn, pursuant to an Indemnity Agreement dated May 1, 2000 (Indemnity Agreement) between The Herald Company, Inc. (Herald, Inc.) and Pulitzer, Herald, Inc. agreed to indemnify Pulitzer for any payments that Pulitzer may make under

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the Guaranty Agreement. In December 2006, Herald Inc. assigned its assets and liabilities to the Herald Publishing Company, LLC (Herald).

## **Table of Contents**

The terms of the Pulitzer Notes, as amended, contain certain covenants and conditions including the maintenance, by Pulitzer, of the ratio of debt to EBITDA, as defined in the Guaranty Agreement, minimum net worth and limitations on the incurrence of other debt. At December 28, 2008, Pulitzer was in compliance with such covenants, as waived or amended from time to time. In addition, the Pulitzer Notes and the Operating Agreement with Herald (Operating Agreement) require that PD LLC maintain a reserve, consisting of cash and investments in U.S. government securities, totaling approximately \$129,810,000 at December 28, 2008 (Reserve). The Pulitzer Notes and the Operating Agreement provide for a \$3,750,000 quarterly increase in the minimum Reserve balance through May 1, 2010, when the amount will total \$150,000,000. See Note 13.

The Credit Agreement contains a cross-default provision tied to the terms of the Pulitzer Notes.

The purchase price allocation of Pulitzer resulted in an increase in the value of the Pulitzer Notes in the amount of \$31,512,000, which is recorded as debt in the Consolidated Balance Sheets. This amount will be accreted over the remaining life of the Pulitzer Notes, until April 2009, as a reduction in interest expense using the interest method. This accretion will not increase the principal amount due to, or reduce the amount of interest to be paid to, the Noteholders.

The Company is required to refinance the Pulitzer Notes from time to time, as they become due, until May 1, 2015, unless Herald exercises its rights under the Operating Agreement to require Pulitzer to redeem its 5% interest in PD LLC on May 1, 2010 (2010 Redemption). See Note 13.

## **2009 Waivers**

In December 2008, certain covenant violations related to the Credit Agreement and Pulitzer Notes, as applicable, were waived (the 2009 Waivers). The 2009 Waivers relate to the going concern modification of the auditors' reports on the Consolidated Financial Statements of the Company, and the separate financial statements of Pulitzer and PD LLC for 2008, and a delay in the timing of delivery of 2008 year end covenant compliance information related to the Credit Agreement and the Pulitzer Notes. Waivers were also obtained related to a violation of the Consolidated Net Worth (as defined) covenant as of September 28, 2008 and as of December 28, 2008 under the Pulitzer Notes. The waiver under the Credit Agreement expires March 30, 2009. The waiver under the Pulitzer Notes, which was initially scheduled to expire January 16, 2009, was extended through February 13, 2009. As of December 28, 2008, the Company was also in violation of the maximum debt to EBITDA covenant related to the Pulitzer Notes. A waiver of the covenant violation was obtained through February 13, 2009 under the Pulitzer Notes and through March 30, 2009 under the Credit Agreement. The waiver under the Pulitzer Notes contains a provision which allows it to be revoked upon 48 hours notice.

The Company paid fees and expenses related to the 2009 Waivers totaling \$1,599,000. The fees were capitalized and are being expensed over the respective waiver periods.

## **Liquidity**

The Company's ability to operate as a going concern is dependent on its ability to refinance or amend its debt agreements as they become due, or earlier if available liquidity is consumed.

The Company's indebtedness could adversely affect its financial health in any or all of the following ways:

- Substantially all of the cash flows of the Company are required to be applied to payment of debt interest and principal, reducing funds available for investment, capital expenditures and other purposes;
- The Company reported significant net losses in 2008 and the 13 weeks ended December 28, 2008, due to impairment of goodwill and other assets resulting from the continuing and increasing difference between its stock price and the per share carrying value of its net assets. Reduced expectations of future cash flows were also an important factor in the determination of such impairment charges;
- The Company's flexibility to react to changes in economic and industry conditions may be more limited;
- Increasing leverage could make the Company more vulnerable in the event of additional deterioration of general economic conditions or other adverse events; and
- Continuation of current business trends may result in additional violations of debt covenants in future periods.

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There could be a material impact on the Company's business if it is unable to meet the conditions of its debt agreements or obtain replacement financing.

The Company generated cash flows in 2008 sufficient to reduce net debt by \$102,225,000, pay dividends totaling \$32,573,000 and acquire shares of its Common Stock in the amount of \$19,483,000. The Company does not have sufficient cash flows to meet both its requirements for 2009 operations and repayment of the Pulitzer Notes.

**Table of Contents**

Remaining 2009 principal payments required under the Credit Agreement at January 31, 2009 totaling \$60,550,000 are expected to exceed the Company's cash flows available for such payments. As a result, the Company expects to utilize a portion of its capacity under its revolving credit facility to fund a portion of the 2009 principal payments required. At January 31, 2009, the Company had \$302,950,000 outstanding under the revolving credit facility, and after consideration of the 2009 Amendments and letters of credit, has approximately \$61,217,000 available for future use.

Principal payments under the Credit Agreement totaling \$166,250,000 are due in 2010. The Company expects to utilize the remainder of its capacity under its revolving credit facility to fund a portion of the 2010 principal payments required.

The Pulitzer Notes mature in April 2009. The Company is actively engaged in discussions with the Noteholders, and to the extent their approval may also be required, the Lenders, to extend or refinance the Pulitzer Notes. The Company has also initiated discussions with the Lenders related to changes to the Credit Agreement to maintain sufficient long-term liquidity. However, the timing and ultimate outcome of such discussions cannot be determined at this time due, in part, to the abnormal condition of the domestic credit markets and the overall recessionary operating environment in which the Company, Pulitzer, and other publishing companies are currently operating. Continuing instability or further disruptions of these markets could prohibit or make it more difficult for the Company to access new capital, increase the cost of capital or limit its ability to refinance existing indebtedness.

There are numerous potential consequences under the Credit Agreement, and Guaranty Agreement and Note Agreement related to the Pulitzer Notes, if an Event of Default, including those arising upon expiration of existing waivers occurs and is not remedied. Many of those consequences are beyond the control of the Company, Pulitzer, and PD LLC, respectively. The occurrence of one or more Events of Default would give rise to the right of the Lenders or the Noteholders, or both of them, to exercise their remedies under the Credit Agreement and the Note and Guaranty Agreements, respectively, including, without limitation, the right to accelerate all outstanding debt and take actions authorized in such circumstances under applicable collateral security documents, any of which would impair the ability of the Company to operate its business as a going concern.

Debt consists of the following:

| <i>(Thousands)</i>               | December 28,<br>2008 | September 28,<br>2008 | Interest Rate(s)<br>December 28, 2008 |
|----------------------------------|----------------------|-----------------------|---------------------------------------|
| <b>Credit Agreement:</b>         |                      |                       |                                       |
| A Term Loan                      | \$ 783,750           | \$ 819,375            | 4.44-5.20%                            |
| Revolving credit facility        | 269,625              | 207,000               | 4.04-5.25                             |
| <b>Pulitzer Notes:</b>           |                      |                       |                                       |
| Principal amount                 | 306,000              | 306,000               | 8.05                                  |
| Unaccreted fair value adjustment | 3,201                | 5,265                 |                                       |
|                                  | <b>\$ 1,362,576</b>  | <b>\$ 1,337,640</b>   |                                       |

At December 28, 2008, the Company's weighted average cost of debt (including the effect of interest rate swaps and collars) was 5.79%.

Aggregate maturities of debt for each of the 52 week periods ending December 2012 are \$448,500,000, \$190,000,000, \$285,000,000, and \$435,875,000, respectively. Because the timing and ultimate outcome of discussions to extend or refinance the Pulitzer Notes cannot be determined at this time, and because of the potential for a cross-default under the Credit Agreement related to expiration of waivers of current covenant violations and/or potential future covenant violations under the Pulitzer Notes, the Company has classified all amounts outstanding under the Credit Agreement as a current liability in the Consolidated Balance Sheets.

**7 INTEREST RATE EXCHANGE AGREEMENTS**

At December 28, 2008, the Company has outstanding interest rate swaps in the notional amount of \$125,000,000. The interest rate swaps have original terms of four to five years, carry interest rates from 4.3% to 4.4% (plus the applicable LIBOR margin) and

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effectively fix the Company's interest rate on debt in the amounts, and for the time periods, of such instruments. During the 13 weeks ended December 28, 2008 interest rate swaps with a notional amount of \$75,000,000 expired.



**Table of Contents**

In 2008, the Company executed interest rate collars in the notional amount of \$150,000,000. The collars have a two year term and limit LIBOR to an average floor of 3.57% and a cap of 5.0%. Such collars effectively limit the range of the Company's exposure to interest rates to LIBOR greater than the floor and less than the cap (in either case plus the applicable LIBOR margin) for the time period of such instruments.

At December 28, 2008 and September 28, 2008, the Company recorded a liability of \$6,971,000 and \$3,337,000, respectively, related to the fair value of such instruments. The change in this fair value is recorded in other comprehensive income, net of income taxes.

At December 28, 2008, after consideration of the interest rate swaps described above, approximately 68% of the principal amount of the Company's debt is subject to floating interest rates. The interest rate collars described above limit the Company's exposure to interest rates on an additional 11% of the principal amount of its debt.

The Company's interest rate exchange agreements at December 28, 2008 consist of the following:

| (Thousands)<br>Notional Amount      | Start Date        | Maturity Date     | Rate(s)    | Fair Value       |
|-------------------------------------|-------------------|-------------------|------------|------------------|
| <b>VARIABLE TO FIXED RATE SWAPS</b> |                   |                   |            |                  |
| \$ 50,000                           | November 30, 2005 | November 30, 2009 | 4.315%     | \$(1,345)        |
| 50,000                              | November 30, 2005 | November 30, 2009 | 4.325      | (1,350)          |
| 25,000                              | November 30, 2005 | November 30, 2010 | 4.395      | (1,301)          |
| <b>\$125,000</b>                    |                   |                   |            | <b>\$(3,996)</b> |
| <b>COLLARS</b>                      |                   |                   |            |                  |
| \$ 75,000                           | November 30, 2007 | November 30, 2009 | 3.53-5.00% | \$(1,451)        |
| 75,000                              | November 30, 2007 | November 30, 2009 | 3.61-5.00  | (1,524)          |
| <b>\$150,000</b>                    |                   |                   |            | <b>\$(2,975)</b> |

**8 PENSION, POSTRETIREMENT AND POSTEMPLOYMENT DEFINED BENEFIT PLANS**

The Company and its subsidiaries have several noncontributory defined benefit pension plans that together cover a significant number of *St. Louis Post-Dispatch* and selected other employees. Benefits under the plans are generally based on salary and years of service. The Company's liability and related expense for benefits under the plans are recorded over the service period of active employees based upon annual actuarial calculations. Plan funding strategies are influenced by tax regulations. Plan assets consist primarily of domestic and foreign corporate equity securities, government and corporate bonds, and cash.

In addition, the Company provides retiree medical and life insurance benefits under postretirement plans at several of its operating locations. The level and adjustment of participant contributions vary depending on the specific plan. In addition, PD LLC provides postemployment disability benefits to certain employee groups prior to retirement at the *St. Louis Post-Dispatch*. The Company's liability and related expense for benefits under the postretirement plans are recorded over the service period of active employees based upon annual actuarial calculations. The Company accrues postemployment disability benefits when it becomes probable that such benefits will be paid and when sufficient information exists to make reasonable estimates of the amounts to be paid.

The Company uses a June 30 measurement date for all of its pension and postretirement medical plan obligations.

**Table of Contents**

The net periodic cost (benefit) components of the Company's pension and postretirement medical plans are as follows:

## Pension Plans

| (Thousands)  | 13 Weeks Ended       |                      |
|--|----------------------|----------------------|
|  | December 28,<br>2008 | December 30,<br>2007 |
| Service cost for benefits earned during the period | \$ 269               | \$ 375               |
| Interest cost on projected benefit obligation      | 2,388                | 2,334                |
| Expected return on plan assets                     | (2,917)              | (3,436)              |
| Amortization of net gain                           | (295)                | (424)                |
| Amortization of prior service cost                 | (34)                 | (33)                 |
|  | \$ (589)             | \$(1,184)            |

## Postretirement Medical Plans

| (Thousands)  | 13 Weeks Ended       |                      |
|--|----------------------|----------------------|
|  | December 28,<br>2008 | December 30,<br>2007 |
| Service cost for benefits earned during the period | \$ 349               | \$ 525               |
| Interest cost on projected benefit obligation      | 1,682                | 1,653                |
| Expected return on plan assets                     | (601)                | (549)                |
| Amortization of net gain                           | (514)                | (158)                |
| Amortization of prior service cost                 | (58)                 | (58)                 |
|  | \$ 858               | \$1,413              |

\$30,000 and \$46,000, of net periodic pension benefit for the 13 weeks ended December 28, 2008, and December 31, 2007, respectively, was allocated to TNI.

Based on its forecast at December 28, 2008, the Company expects to contribute \$4,307,000 to its postretirement medical plans in 2009.

**2009 Changes to Plans**

In October and December 2008, the Company notified certain participants in its postretirement medical plans of administrative changes to be made to the plans, effective in January 2009, including increases in employee premiums, changes in the plans reimbursement of medical expenses covered by Medicare, elimination of certain coverage options and the establishment of an account-based structure. The changes are expected to reduce annual net periodic postretirement medical cost by approximately \$5,400,000, beginning in January 2009, and will reduce the benefit obligation by approximately \$27,500,000, effective in January 2009.

**9 INCOME TAXES**

The provision for income taxes includes deferred taxes and is based upon estimated annual effective tax rates in the tax jurisdictions in which the Company operates.

The effective tax rate for the 13 weeks ended December 28, 2008, differs from the statutory rate primarily due to the impairment of goodwill that was partially non-deductible.

The Company estimates that it is reasonably possible that up to \$3,168,000 of uncertain tax benefits associated with state income tax return issues could be recognized in the 52 weeks ending December 2009 as a result of the expiration of various state statutes of limitations.



**Table of Contents**

The Company files income tax returns with the IRS and various state tax jurisdictions. From time to time, the Company is subject to routine audits by those agencies, and those audits may result in proposed adjustments. The Company has considered the alternative interpretations that may be assumed by the various taxing agencies, believes its positions taken regarding its filings are valid, and that adequate tax liabilities have been recorded to resolve such matters. However, the actual outcome cannot be determined with certainty and the difference could be material, either positively or negatively, to the Consolidated Statements of Operations and Comprehensive Income (Loss) in the periods in which such matters are ultimately determined. The Company does not believe the final resolution of such matters will be material to its consolidated financial position or cash flows.

The IRS has completed its review of the Company's income tax returns through 2004 and is presently examining income tax returns of Pulitzer for 2003, 2004 and 2005. The Company has various state income tax examinations ongoing and at various stages of completion, but generally the state income tax returns have been audited or closed to audit through 2002.

**10 EARNINGS (LOSS) PER COMMON SHARE**

The following table sets forth the computation of basic and diluted earnings (loss) per common share. Per share amounts may not add due to rounding.

| <i>(Thousands, Except Per Share Data)</i>          | 13 Weeks Ended    |                   |
|--|-------------------|-------------------|
|  | December 28, 2008 | December 30, 2007 |
| Income (loss) applicable to Common Stock:          |                   |                   |
| Continuing operations                              | \$ (48,672)       | \$ 21,788         |
| Discontinued operations                            | (5)               | 338               |
|  | \$ (48,677)       | \$ 22,126         |
| Weighted average common shares                     | 45,045            | 46,224            |
| Less non-vested restricted Common Stock            | 640               | 478               |
| Basic average common shares                        | 44,405            | 45,746            |
| Dilutive stock options and restricted Common Stock | -                 | 23                |
| Diluted average common shares                      | 44,405            | 45,769            |
| Earnings (loss) per common share:                  |                   |                   |
| Basic:   |                   |                   |
| Continuing operations                              | \$ (1.10)         | \$ 0.48           |
| Discontinued operations                            | -                 | 0.01              |
|  | \$ (1.10)         | \$ 0.48           |
| Diluted:   |                   |                   |
| Continuing operations                              | \$ (1.10)         | \$ 0.48           |
| Discontinued operations                            | -                 | 0.01              |
|  | \$ (1.10)         | \$ 0.48           |

For the 13 weeks ended December 28, 2008 and December 30, 2007, the Company has 259,000 and 1,153,000 weighted average shares, respectively, subject to issuance under its stock option plan that have no intrinsic value and are not considered in the computation of diluted earnings per common share.

**11 STOCK OWNERSHIP PLANS****Stock Options**

A summary of activity related to the Company's stock option plan is as follows:

| <i>(Thousands, Except Per Share Data)</i> | Shares | Weighted | Weighted | Aggregate |
|---|--------|----------|----------|-----------|
|---|--------|----------|----------|-----------|

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|                                 |     | Average<br>Exercise Price | Average<br>Remaining<br>Contractual<br>Term (Years) | Intrinsic<br>Value |
|---------------------------------|-----|---------------------------|---|--------------------|
| Outstanding, September 28, 2008 | 263 | \$ 34.69                  |   |                    |
| Cancelled                       | (4) | 29.63                     |   |                    |
| Outstanding, December 28, 2008  | 259 | \$ 34.77                  | 6.1   | -                  |
| Exercisable, December 28, 2008  | 216 | \$ 35.96                  | 5.8   | -                  |

Total unrecognized compensation expense for unvested stock options as of December 28, 2008 is \$180,000, which will be recognized over a weighted average period of 0.9 years.

**Table of Contents****Restricted Common Stock**

The following table summarizes restricted Common Stock activity during the 13 weeks ended December 28, 2008:

| <i>(Thousands, Except Per Share Data)</i> | Shares | Weighted<br>Average Grant Date<br>Fair Value |
|---|--------|--|
| Outstanding, September 28, 2008           | 746    | \$21.60                                      |
| Vested                                    | (112)  | 39.60  |
| Forfeited                                 | (150)  | 15.24  |
| Outstanding, December 28, 2008            | 484    | \$19.39                                      |

The fair value of restricted Common Stock vested during the 13 weeks ended December 28, 2008 totals \$170,000.

Total unrecognized compensation expense for unvested restricted Common Stock as of December 28, 2008 is \$4,485,000, which will be recognized over a weighted average period of 1.6 years.

**12 FAIR VALUE MEASUREMENTS**

The Company adopted FASB Statement 157 *Fair Value Measurements* (Statement 157) in 2009. Statement 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. Statement 157 establishes a three-level hierarchy of fair value measurements based on whether the inputs to those measurements are observable or unobservable and consists of the following levels:

Level 1 Quoted prices for identical instruments in active markets;

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets; and

Level 3 Valuations derived from valuation techniques in which one or more significant inputs are unobservable.

The following table summarizes the financial instruments measured at fair value in the accompanying Consolidated Financial Statements as of December 28, 2008:

| <i>(Thousands)</i>              | Level 1   | Level 2 | Level 3 | Total     |
|---------------------------------|-----------|---------|---------|-----------|
| Marketable securities           | \$133,780 | \$ -    | \$ -    | \$133,780 |
| Interest rate swaps and collars | -         | (6,971) | -       | (6,971)   |

In the 13 weeks ended December 28, 2008 the Company reduced the carrying value of property and equipment no longer in use by \$2,264,000, based on estimates of the related fair value in the current market.

**13 COMMITMENTS AND CONTINGENT LIABILITIES****Capital Expenditures**

At December 28, 2008, the Company has construction and equipment purchase commitments totaling approximately \$5,083,000.

**PD LLC Operating Agreement**

In 2000, Pulitzer and Herald Inc. completed the transfer of their respective interests in the assets and operations of the *St. Louis Post-Dispatch* and certain related businesses to a new joint venture (the Venture), known as PD LLC. Pulitzer is the managing member of PD LLC. Under the terms of the Operating Agreement, Pulitzer and another subsidiary hold a 95% interest in the results of operations of PD LLC and Herald, as successor to Herald Inc., holds a 5% interest. Until 2008, Herald's 5% interest was reported as minority interest in the Consolidated Statements of Operations and Comprehensive Income (Loss) at historical cost, plus accumulated earnings since the acquisition of Pulitzer.

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## **Table of Contents**

Also, under the terms of the Operating Agreement, Herald Inc. received on May 1, 2000 a cash distribution of \$306,000,000 from PD LLC (the Initial Distribution). This distribution was financed by the Pulitzer Notes. Pulitzer's entry into the Venture was treated as a purchase for accounting purposes and a leveraged partnership for income tax purposes.

On May 1, 2010, the 2010 Redemption will provide Herald a one-time right to require PD LLC to redeem its interest in PD LLC, together with its interest, if any, in DS LLC. The May 1, 2010 redemption price for Herald's interest will be determined pursuant to a formula yielding an amount which will result in the present value to May 1, 2000 of the after tax cash flows to Herald (based on certain assumptions) from PD LLC, including the Initial Distribution and the special distribution described below, if any, and from DS LLC, being equal to \$275,000,000. Based on this formula, the present value of the 2010 Redemption at December 28, 2008, is approximately \$73,210,000. The Company recorded the present value of the remaining amount of this potential liability in its Consolidated Balance Sheet in 2008, with the offset primarily to goodwill in the amount of \$55,594,000, and the remainder recorded as a reduction of retained earnings.

Recording of the liability for the 2010 Redemption in 2008 also resulted in an increase in loss available to common stockholders and loss per common share of \$1,039,000 and \$0.02 respectively in the 13 weeks ended December 28, 2008, which accounts primarily for the time value of the increase in the liability.

During the first ten years of its term, PD LLC is restricted from making distributions (except under specified circumstances), capital expenditures and member loan repayments unless it has set aside out of its cash flow the Reserve in an amount equal to the product of \$15,000,000 and the number of years since May 1, 2000, but not in excess of \$150,000,000. PD LLC is not required to maintain the Reserve after May 1, 2010.

Upon termination of PD LLC and DS LLC, which will be on May 1, 2015 (unless Herald exercises the 2010 Redemption described above), Herald will be entitled to the liquidating value of its interests in PD LLC and DS LLC, to be paid in cash by Pulitzer (the 2015 Liquidation). That amount would be equal to the amount of Herald's capital accounts, after allocating the gain or loss that would result from a cash sale of PD LLC and DS LLC's assets for their fair market value at that time. Herald's share of such gain or loss generally will be 5%, but will be reduced (but not below 1%) to the extent that the present value to May 1, 2000 of the after tax cash flows to Herald from PD LLC and from DS LLC, including the Initial Distribution, the special distribution described below, if any, and the liquidation amount (based on certain assumptions), exceeds \$325,000,000.

The actual amount payable to Herald upon the termination of PD LLC and DS LLC on May 1, 2015 will depend on such variables as future cash flows, the amounts of any distributions to Herald prior to such payment, PD LLC's and DS LLC's rate of growth and market valuations of newspaper properties.

The redemption of Herald's interest in PD LLC and DS LLC either on May 1, 2010 or upon termination of PD LLC and DS LLC in 2015 is expected to generate significant tax benefits to the Company as a consequence of the resulting increase in the tax basis of the assets owned by PD LLC and DS LLC and the related depreciation and amortization deductions. The increase in basis, which will be amortized for income tax purposes over a 15 year period, approximates the sum of the Initial Distribution and either the 2010 Redemption or the 2015 Liquidation.

In the event the transactions effectuated in connection with either the formation of the Venture and the Initial Distribution or the organization of DS LLC are recharacterized by the Internal Revenue Service (IRS) as a taxable sale by Herald, with the result in either case that the tax basis of PD LLC's assets increases and Herald is required to recognize taxable income as a result of such recharacterization, Herald generally will be entitled to receive a special distribution from PD LLC in an amount that corresponds, approximately, to the present value of the after tax benefit to the members of PD LLC of the tax basis increase. The adverse financial effect of any such special distribution to Herald on PD LLC (and thus Pulitzer and the Company) will be partially offset by the current and deferred tax benefits arising as a consequence of the treatment of the transactions effectuated in connection with the formation of the Venture and the Initial Distribution or the organization of DS LLC as a taxable sale by Herald. In 2006, the IRS concluded an examination of Herald without adjustment related to the Venture or the Initial Distribution.

## **Legal Proceedings**

The Company is involved in a variety of legal actions that arise in the normal course of business. Insurance coverage mitigates potential loss for certain of these matters. While the Company is unable to predict the ultimate outcome of these legal actions, it is the opinion of management that the disposition of these matters will not have a material adverse effect on the Company's Consolidated Financial Statements, taken as a whole.





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## **Table of Contents**

In April 2008, a group of newspaper carriers filed suit against the Company in the United States District Court for the Southern District of California, claiming to be employees and not independent contractors of the Company. The plaintiffs seek relief related to violation of various employment based statutes, and request punitive damages and attorneys' fees. Since the suit is in the earliest of phases, the Company is unable to predict whether the ultimate economic outcome, if any, could have a material effect on the Company's Consolidated Financial Statements, taken as a whole. The Company denies the allegations of employee status, consistent with past practices of the Company and the industry, and intends to vigorously contest the action, which is not covered by insurance.

### **14 IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS**

In 2006, the FASB issued Statement 158, *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans*, which amends Statements 87, 88, 106 and 132(R). The Company adopted the recognition and disclosure provision of Statement 158 as of September 30, 2007.

Statement 158 will also require the Company to change its measurement date to the last day of the fiscal year from a date three months prior to the end of the fiscal year, beginning in 2009. The change in measurement date will require a one-time adjustment to retained earnings, the effect of which cannot be determined at this time. None of the changes required will impact the Company's results of operations or cash flows.

In 2008, the FASB issued Statement 141(R), *Business Combinations* and Statement 160, *Noncontrolling Interests in Consolidated Financial Statements, an amendment of Accounting Research Bulletin No. 51*. Statement 141(R) establishes requirements for how an acquirer in a business combination recognizes and measures the assets acquired, liabilities assumed, and any noncontrolling interests. For the Company, the provisions of Statement 141(R) are effective for business combinations occurring in 2010. Statement 160 will change the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests and classified as a component of stockholders' equity. Statement 160 is effective for the Company in 2010. The Company has not completed its evaluation of the effects of Statements 141(R) and 160 on its Consolidated Financial Statements.

In 2008, the FASB issued Statement 161, *Disclosures About Derivative Instruments and Hedging Activities*, an amendment of FASB Statement 133. Statement 161 requires disclosure regarding the objectives and strategies for using derivative instruments and the credit-risk-related features. Statement 161 also requires disclosure of the fair value amounts and the gains and losses on derivative instruments in tabular form. Statement 161 is effective for the Company in 2010.

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

The following discussion includes comments and analysis relating to the Company's results of operations and financial condition as of and for the 13 weeks ended December 28, 2008. This discussion should be read in conjunction with the Consolidated Financial Statements and related Notes thereto and the Company's 2008 Annual Report on Form 10-K.

### **NON-GAAP FINANCIAL MEASURES**

No non-GAAP financial measure should be considered as a substitute for any related financial measure under accounting principles generally accepted in the United States of America (GAAP). However, the Company believes the use of non-GAAP financial measures provides meaningful supplemental information with which to evaluate its financial performance, or assist in forecasting and analyzing future periods. The Company also believes such non-GAAP financial measures are alternative indicators of performance used by investors, lenders, rating agencies and financial analysts to estimate the value of a publishing business or its ability to meet debt service requirements.

#### **Operating Cash Flow and Operating Cash Flow Margin**

Operating cash flow, which is defined as operating income before depreciation, amortization, impairment of goodwill and other assets, and equity in earnings of associated companies, and operating cash flow margin (operating cash flow divided by operating revenue) represent non-GAAP financial measures that are used in the analysis below. The Company believes these measures provide meaningful supplemental information because of their focus on the Company's results from operations before depreciation, amortization and earnings from equity investments.



**Table of Contents**

Reconciliations of operating cash flow and operating cash flow margin to operating income (loss) and operating income (loss) margin, the most directly comparable measures under GAAP, are included in the tables below:

| <i>(Thousands)</i>  | 13 Weeks Ended    | Percent of | 13 Weeks Ended    | Percent of |
|---|-------------------|------------|-------------------|------------|
|   | December 28, 2008 | Revenue    | December 30, 2007 | Revenue    |
| Operating cash flow   | \$ 53,130         | 21.8%      | \$72,433          | 25.9%      |
| Less depreciation and amortization                                | 20,399            | 8.4        | 23,031            | 8.2        |
| Unrealized losses of property and equipment                       | 2,264             | 0.9        | -                 | -          |
| Impairment of goodwill  | 67,781            | NM         | -                 | -          |
| Equity in earnings of associated companies                        | 3,064             | 1.3        | 4,301             | 1.5        |
| Operating income (loss)   | \$(34,250)        | NM         | \$53,703          | 19.2%      |
| <b>Adjusted Net Income and Adjusted Earnings Per Common Share</b> |                   |            |                   |            |

Adjusted net income and adjusted earnings per common share, which are defined as net income (loss) available to common stockholders and earnings (loss) per common share adjusted to exclude unusual matters and those of a substantially non-recurring nature, are non-GAAP financial measures that are used in the analysis below. The Company believes these measures provide meaningful supplemental information by identifying matters that are not indicative of core business operating results or are of a substantially non-recurring nature.

Reconciliations of adjusted net income and adjusted earnings per common share to net income (loss) available to common stockholders and earnings (loss) per common share, respectively, the most directly comparable measures under GAAP, are set forth below under the caption Overall Results .

**SAME PROPERTY COMPARISONS**

Certain information below, as noted, is presented on a same property basis, which is exclusive of acquisitions and divestitures consummated in the current or prior year. The Company believes such comparisons provide meaningful supplemental information for an understanding of changes in its revenue and operating expenses. Same property comparisons exclude TNI and MNI. The Company owns 50% of TNI and also owns 50% of the capital stock of MNI, both of which are reported using the equity method of accounting. Same property comparisons also exclude corporate office costs.

**CRITICAL ACCOUNTING POLICIES**

The Company's discussion and analysis of its results of operations and financial condition are based upon the Company's Consolidated Financial Statements, which have been prepared in accordance with GAAP. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, the Company evaluates its estimates. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The Company's critical accounting policies include the following:

- Goodwill and other intangible assets
- Pension, postretirement and postemployment benefit plans
- Income taxes
- Revenue recognition
- Uninsured risks

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The Company recorded a pretax, non-cash charge in the 13 weeks ended December 28, 2008 to reduce the carrying value of goodwill by \$67,781,000. The Company recorded \$13,460,000 of income tax benefit related to this charge. See Note 5 of the Notes to Consolidated Financial Statements, included herein.

Additional information regarding these critical accounting policies can be found under the caption Management's Discussion and Analysis of Financial Condition and Results of Operations in the Company's 2008 Annual Report on Form 10-K and the Notes to Consolidated Financial Statements, included herein.

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**Table of Contents**

**IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS**

In 2006, the FASB issued Statement 158, *Employer's Accounting for Defined Benefit Pension and Other Postretirement Plans*, which amends Statements 87, 88, 106 and 132(R). The Company adopted the recognition and disclosure provision of Statement 158 as of September 30, 2007.

Statement 158 will also require the Company to change its measurement date to the last day of the fiscal year from a date three months prior to the end of the fiscal year, beginning in 2009. The change in measurement date will require a one-time adjustment to retained earnings, the effect of which cannot be determined at this time. None of the changes required will impact the Company's results of operations or cash flows.

In 2008, the FASB issued Statement 141(R), *Business Combinations* and Statement 160, *Noncontrolling Interests in Consolidated Financial Statements, an amendment of Accounting Research Bulletin No. 51*. Statement 141(R) establishes requirements for how an acquirer in a business combination recognizes and measures the assets acquired, liabilities assumed, and any noncontrolling interests. For the Company, the provisions of Statement 141(R) are effective for business combinations occurring in 2010. Statement 160 will change the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests and classified as a component of stockholders' equity. Statement 160 is effective for the Company in 2010. The Company has not completed its evaluation of the effects of Statements 141(R) and 160 on its Consolidated Financial Statements.

In 2008, the FASB issued Statement 161, *Disclosures About Derivative Instruments and Hedging Activities*, an amendment of FASB Statement 133. Statement 161 requires disclosure regarding the objectives and strategies for using derivative instruments and the credit-risk-related features. Statement 161 also requires disclosure of the fair value amounts and the gains and losses on derivative instruments in tabular form. Statement 161 is effective for the Company in 2010.

**EXECUTIVE OVERVIEW**

The Company is a premier provider of local news, information and advertising in primarily midsize markets, with 49 daily newspapers and a joint interest in four others, rapidly growing online sites and more than 300 weekly newspapers and specialty publications in 23 states.

In 2005, the Company acquired Pulitzer. Pulitzer published 14 daily newspapers, including the *St. Louis Post-Dispatch*, and more than 100 weekly newspapers and specialty publications. Pulitzer also owned a 50% interest in TNI. The acquisition of Pulitzer increased the Company's circulation by more than 50% to more than 1.6 million daily and 1.9 million Sunday, and revenue, on an annualized basis, by more than 60% at that time. In 2006, the Company sold the assets of *The Daily News* in Rhinelander, Wisconsin, the smallest of these newspapers. In 2008, the Company sold the assets of *The Daily Chronicle* in DeKalb, Illinois.

The Company is focused on six key strategic priorities. They are to:

- Grow revenue creatively and rapidly;
- Deliver strong local news and information;
- Maximize its local online strength;
- Continue expanding its print and online audiences;
- Nurture employee development and achievement; and
- Exercise careful cost control.

Certain aspects of these priorities are discussed below.

Approximately 76% of the Company's revenue is derived from advertising. The Company's strategies are to increase its share of local advertising through increased sales activities in its existing markets and, over time, to increase its print and online audiences through internal expansion into existing and contiguous markets and enhancement of online offerings, augmented by selective acquisitions.



**Table of Contents**

**ECONOMIC CONDITIONS**

The United States economy has been in a recession since December 2007, according to the National Bureau of Economic Research, and it is widely believed that certain elements of the economy, such as housing, were in decline before that time. 2008 and 2009 revenue, operating results and cash flows were significantly impacted by the recession. The duration and depth of an economic recession in markets in which the Company operates may further reduce its future advertising and circulation revenue, operating results and cash flows.

**IMPAIRMENT OF GOODWILL**

In the 13 weeks ended December 28, 2008, the Company, based on its most recent analysis and in conjunction with its ongoing requirement to assess the carrying value and estimated useful lives of goodwill and identified intangible assets, concluded that the carrying value of goodwill exceeded its fair value. As a result, the Company recorded a pretax, non-cash charge to reduce the carrying value of goodwill by \$67,781,000. This charge resulted in recognition of a significant loss per share for the 13 weeks ended December 28, 2008, and may result in a loss for the 52 weeks ending September 27, 2009.

**DEBT AND LIQUIDITY**

The Company has a substantial amount of debt, as more fully discussed (and capitalized terms used below defined) under Item 2, Liquidity and Capital Resources and Note 6 of the Notes to Consolidated Financial Statements, included herein. In 2009, the Company amended the terms of its Credit Agreement, which, among other changes, increases the Company's future borrowing costs in relation to LIBOR, and reduces the amount available under the Company's revolving credit facility. In December 2008 and February 2009, certain covenant violations related to the Credit Agreement and Pulitzer Notes were waived until March 30, 2009 and February 13, 2009, respectively.

The Company's ability to operate as a going concern is dependent on its ability to refinance or amend its debt agreements as they become due, or earlier if available liquidity is consumed.



**Table of Contents****13 WEEKS ENDED DECEMBER 28, 2008**

Results, as reported in the Consolidated Financial Statements, are summarized below:

| <i>(Thousands, Except Per Share Data)</i>                         | 13 Weeks Ended       |                      | Percent Change |               |
|---|----------------------|----------------------|----------------|---------------|
|   | December 28,<br>2008 | December 30,<br>2007 | Total          | Same Property |
| Advertising revenue:  |                      |                      |                |               |
| Retail  | \$112,934            | \$127,602            | (11.5)%        | (11.4)%       |
| Classified:   |                      |                      |                |               |
| Daily newspapers:   |                      |                      |                |               |
| Employment  | 8,686                | 15,367               | (43.5)         | (43.5)        |
| Automotive  | 8,643                | 11,729               | (26.3)         | (26.3)        |
| Real estate   | 8,126                | 11,543               | (29.6)         | (29.6)        |
| All other   | 10,046               | 9,988                | 0.6            | 0.6           |
| Other publications  | 8,357                | 10,640               | (21.5)         | (22.8)        |
| Total classified  | 43,858               | 59,267               | (26.0)         | (26.2)        |
| Online  | 11,621               | 13,475               | (13.8)         | (13.7)        |
| National  | 12,851               | 13,582               | (5.4)          | (5.4)         |
| Niche publications  | 3,319                | 3,644                | (8.9)          | (8.9)         |
| Total advertising revenue   | 184,583              | 217,570              | (15.2)         | (15.2)        |
| Circulation   | 47,556               | 49,805               | (4.5)          | (4.5)         |
| Commercial printing   | 3,469                | 4,175                | (16.9)         | (16.9)        |
| Online services and other   | 7,947                | 8,306                | (4.3)          | (4.3)         |
| Total operating revenue   | 243,555              | 279,856              | (13.0)         | (13.0)        |
| Compensation  | 94,483               | 108,194              | (12.7)         | (12.1)        |
| Newsprint and ink   | 25,154               | 25,103               | 0.2            | 1.5           |
| Other operating expenses  | 69,950               | 74,126               | (5.6)          | (5.7)         |
| Workforce adjustments   | 838                  | -                    | NM             | NM            |
| Total operating expenses, excluding depreciation and amortization | 190,425              | 207,423              | (8.2)          | (7.7)         |
| Operating cash flow   | 53,130               | 72,433               | (26.6)         | (26.2)        |
| Depreciation and amortization                                     | 20,399               | 23,031               | (11.4)         |               |
| Impairment of goodwill  | 67,781               | -                    | NM             |               |
| Unrealized losses on property and equipment                       | 2,264                | -                    | NM             |               |
| Equity in earnings of associated companies                        | 3,064                | 4,301                | (28.8)         |               |
| Operating income (loss)   | (34,250)             | 53,703               | NM             |               |
| Non-operating expense, net  | 18,737               | 19,054               | (1.7)          |               |
| Income (loss) from continuing operations before income taxes      | (52,987)             | 34,649               | NM             |               |
| Income tax expense (benefit)                                      | (5,524)              | 12,254               | NM             |               |
| Minority interest   | 170                  | 607                  | (72.0)         |               |
| Income (loss) from continuing operations                          | (47,633)             | 21,788               | NM             |               |
| Discontinued operations, net                                      | (5)                  | 338                  | NM             |               |
| Net income (loss)   | (47,638)             | 22,126               | NM             |               |
| Increase in redeemable minority interest                          | 1,039                | -                    | NM             |               |
| Net income (loss) available to common stockholders                | \$ (48,677)          | \$ 22,126            | NM             |               |
| Earnings (loss) per common share:                                 |                      |                      |                |               |
| Basic   | \$ (1.10)            | \$ 0.48              | NM             |               |
| Diluted   | (1.10)               | 0.48                 | NM             |               |

For the 13 weeks ended December 28, 2008, total same property operating revenue decreased \$36,267,000, or 13.0%, compared to the 13 weeks ended December 30, 2007.



**Table of Contents****Advertising Revenue**

Same property advertising revenue decreased \$32,958,000, or 15.2%, for the 13 weeks ended December 28, 2008 compared to the prior year.

| (Thousands, Same Property) | 13 Weeks Ended    |                   | Percent Change |
|----------------------------|-------------------|-------------------|----------------|
|                            | December 28, 2008 | December 30, 2007 |                |
| Retail                     | \$115,635         | \$128,011         | (9.7)%         |
| Classified:                |                   |                   |                |
| Employment                 | \$ 13,280         | \$ 23,123         | (42.6)%        |
| Automotive                 | 12,561            | 16,576            | (24.2)         |
| Real estate                | 10,738            | 15,279            | (29.7)         |
| Other                      | 15,848            | 17,134            | (7.5)          |
| Total classified revenue   | \$ 52,427         | \$ 72,112         | (27.3)%        |

On a combined basis, print and online retail advertising revenue decreased 9.8% in the 13 weeks ended December 28, 2008. Same property print retail revenue decreased \$14,507,000, or 11.4%. Same property average retail rate, excluding preprint insertions, decreased 6.0%. Same property daily newspaper retail preprint insertion revenue decreased 8.0%.

On a combined basis, print and online classified revenue decreased 27.1%. Same property print classified advertising revenue decreased \$15,544,000, or 26.2%, for the 13 weeks ended December 28, 2008. Higher rate print employment advertising at the daily newspapers decreased 43.5% for the period on a same property basis. Same property print automotive advertising decreased 26.3% amid an industry-wide decline. Same property print real estate advertising decreased 29.6% in a weak housing market nationally, which also negatively impacted the home improvement, furniture and home electronics categories of retail revenue. Other daily newspaper print classified advertising increased 0.6% on a same property basis. Same property classified advertising rates decreased 12.6%.

Advertising lineage, as reported on a same property basis for the Company's daily newspapers only, consisted of the following:

| (Thousands of Inches) | 13 Weeks Ended    |                   | Percent Change |
|-----------------------|-------------------|-------------------|----------------|
|                       | December 28, 2008 | December 30, 2007 |                |
| Retail                | 3,303             | 3,543             | (6.8)%         |
| National              | 148               | 180               | (17.8)         |
| Classified            | 2,969             | 3,562             | (16.6)         |
|                       | 6,420             | 7,285             | (11.9)%        |

Online advertising revenue decreased 13.7% on a same property basis, due to a 31.5% decrease in online classified revenue, partially offset by a 19.1% increase in retail revenue.

National advertising decreased \$731,000, or 5.4%, on a same property basis due to a 17.8% decline in lineage offset by a 13.7% increase in average national rate. Advertising in niche publications decreased 8.9% on a same property basis.

**Circulation and Other Revenue**

Circulation revenue decreased \$2,249,000, or 4.5%, in the 13 weeks ended December 28, 2008, and same property circulation revenue decreased \$2,245,000, or 4.5%. The Company's unaudited average daily newspaper circulation units, including TNI and MNI, decreased 5.1% and Sunday circulation decreased 3.2% for the 13 weeks ended December 28, 2008, compared to the prior year period. Discontinuation of daily publication of *The Capital Times* in Madison, WI and the *South Idaho Press* in Burley, ID magnified the decrease in daily circulation units. Company research in its larger markets indicates it is reaching an increasingly larger audience in these markets through modest growth in newspaper readership and rapid online growth, as well as through additional specialty and niche publications.

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Same property commercial printing revenue decreased \$706,000, or 16.9%, in the 13 weeks ended December 28, 2008. Same property online services and other revenue decreased \$358,000, or 4.3%, in the 13 weeks ended December 28, 2008.

## Table of Contents

### **Operating Expenses**

Costs other than depreciation, amortization and unusual costs and cost reductions decreased \$17,836,000, or 8.6%, in the 13 weeks ended December 28, 2008, and decreased \$16,275,000, or 8.1%, on a same property basis.

Compensation expense decreased \$13,711,000, or 12.7%, in the 13 weeks ended December 28, 2008 and same property compensation expense decreased 12.1% driven primarily by a decline in same property full time equivalent employees of 10.7%. Bonus programs and employee benefits have also been substantially reduced and stock compensation grants have been suspended.

Newsprint and ink costs increased \$51,000, or 0.2%, in the 13 weeks ended December 28, 2008 due to higher unit prices, offset by decreased usage from lower advertising, reduced page sizes, lighter weight paper and some reduction of content. Costs increased 1.5% on a same property basis and volume decreased 24.0% on a same property basis. See Item 3, *Commodities*, included herein.

Other operating costs, which are comprised of all operating expenses not considered to be compensation, newsprint, depreciation, amortization, or unusual costs or cost reductions decreased \$4,176,000, or 5.6%, in the 13 weeks ended December 28, 2008 and decreased 5.7% on a same property basis.

In October and December 2008, the Company notified certain participants in its postretirement medical plans of administrative changes to be made to the plans, effective in January 2009, including increases in employee premiums, changes in the plans reimbursement of medical expenses covered by Medicare, elimination of certain coverage options and the establishment of an account based structure. The changes are expected to reduce annual net periodic postretirement medical cost by approximately \$5,400,000, beginning in January 2009, and will reduce the benefit obligation by approximately \$27,500,000, effective in January 2009.

The Company is engaged in various efforts to continue to reduce its operating expenses in 2009 and beyond, including staff reductions and newsprint conservation. The Company expects its operating expenses, excluding depreciation, amortization and unusual costs and cost reductions, to decline approximately 10-11% in 2009.

### **Results of Operations**

As a result of the above operating cash flow decreased \$19,303,000, or 26.6%, in the current year period. Operating cash flow margin decreased to 21.8% from 25.9% in the prior year period. Same property operating cash flow margin decreased to 24.1%, from 28.4% in the prior year period.

Depreciation and amortization expense decreased \$2,632,000, or 11.4%, due primarily to impairment charges recorded in 2008.

In the 13 weeks ended December 28, 2008, the Company, based on its most recent analysis and in conjunction with its ongoing requirement to assess the carrying value and estimated useful lives of goodwill and identified intangible assets, concluded that the carrying value of goodwill exceeded its fair value. As a result, the Company recorded a pretax, non-cash charge to reduce the carrying value of goodwill by \$67,781,000. This charge resulted in recognition of a significant loss per share for the 13 weeks ended December 28, 2008, and may result in a loss for the 52 weeks ending September 27, 2009.

Equity in earnings of associated companies decreased to \$3,064,000 in the current year period, compared to \$4,301,000 in the prior year. In April 2008, one of MNI's daily newspapers, *The Capital Times*, decreased print publication from six days per week to one day. MNI expects the change will result in annual cost savings of \$3,500,000 to \$4,000,000.

In January 2009, Citizen announced its intention to sell the assets of, or discontinue publication of, the *Tucson Citizen* by March 21, 2009.

The above resulted in an operating loss of \$34,250,000 in the 13 weeks ended December 28, 2008, compared to operating income of \$53,703,000 in the prior year period.

### **Nonoperating Income and Expense**

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Financial expense decreased \$842,000 due to lower levels of debt and lower interest rates, partially offset by increases from the prior year in LIBOR spreads. LIBOR has decreased substantially from its prior year levels.

**Table of Contents**

Amendments to the Company's Credit Agreement consummated in 2009 will increase financial expense in 2009 in relation to LIBOR. Under the amendments, the Company's credit spreads will generally increase 200 basis points from the original pricing grid. The maximum rate will be increased to LIBOR plus 400 basis points. At the December 2008 leverage level, the Company's debt under the Credit Agreement will be priced at LIBOR plus 350 basis points.

**Overall Results**

Income tax expense (benefit) was 10.4% of loss from continuing operations before income taxes in the current year period and 35.4% of income from continuing operations before income taxes in the prior year. In the current year period, the Company reduced certain deferred income tax assets by an increase in the valuation allowance of \$1,152,000 due to the uncertainty that such assets will be realized.

Recording of the change in the liability for the 2010 Redemption resulted in an increase in net loss available to common stockholders for the 13 weeks ended December 28, 2008, of \$1,039,000 and an increase in loss per common share for the 13 weeks ended December 28, 2008, of \$0.02. The Company estimates the ongoing impact on earnings per common share from accounting for the 2010 Redemption of up to \$0.08 to \$0.10 per year through April 2010. There is no impact on net income based on application of current accounting standards. Also, under such standards, if the 2010 Redemption does not occur, the liability and earnings per common share impact discussed above will be reversed for all periods.

As a result of all of the above, the Company recorded a loss per diluted common share of \$1.10 compared to earnings of \$0.48 per diluted share in the prior year period. As detailed in the table below, diluted earnings per common share, as adjusted, were \$0.21 for the 13 weeks ended December 28, 2008 and \$0.48 for the 13 weeks ended December 30, 2007.

|  | 13 Weeks Ended    |           |                   |           |
|--|-------------------|-----------|-------------------|-----------|
|  | December 28, 2008 |           | December 30, 2007 |           |
|  | Amount            | Per Share | Amount            | Per Share |
| <i>(Thousands, Except Per Share Data)</i>                              |                   |           |                   |           |
| Net income (loss) available to common stockholders, as reported        | \$(48,677)        | \$(1.10)  | \$22,126          | \$0.48    |
| Adjustments:   |                   |           |                   |           |
| Impairment of goodwill   | 67,781            | -         | -                 | -         |
| Unrealized losses on property and equipment                            | 2,264             | -         | -                 | -         |
| Curtailment gain, TNI  | (667)             | -         | -                 | -         |
| Workforce adjustments  | 838               | -         | -                 | -         |
|  | 70,216            | -         | -                 | -         |
| Income tax benefit of adjustments, net and impact on minority interest | (14,315)          | -         | -                 | -         |
| Increase in deferred tax valuation allowance                           | 1,152             | -         | -                 | -         |
|  | 57,053            | 1.28      | -                 | -         |
| Net income available to common stockholders, as adjusted               | 8,376             | 0.19      | 22,126            | 0.48      |
| Change in redeemable minority interest                                 | 1,039             | 0.02      | -                 | -         |
| Net income, as adjusted  | \$ 9,415          | \$ 0.21   | \$22,126          | \$0.48    |

**LIQUIDITY AND CAPITAL RESOURCES****Operating Activities**

Cash provided by operating activities of continuing operations was \$813,000 in the 13 weeks ended December 28, 2008, and was \$31,946,000 in the 13 weeks ended December 30, 2007. An operating loss in the 13 weeks ended December 28, 2008 was caused by non-cash charges for the impairment of goodwill. Changes in operating assets and liabilities and the timing of income tax payments accounted for the bulk of the remainder of the change in both years.

**Investing Activities**

Cash required for investing activities totaled \$6,899,000 in the 13 weeks ended December 28, 2008 and \$10,923,000 in the 13 weeks ended December 30, 2007. Capital spending totaled \$5,301,000 in the 13 weeks ended December 28, 2008, and \$8,976,000 in the 13 weeks ended December 30, 2007 and accounted for substantially all of the net usage of funds in both years.

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The Company anticipates that funds necessary for capital expenditures, which are expected to total approximately \$15,000,000 in 2009, and other requirements, will be available from internally generated funds, or availability under its existing Credit Agreement. The 2009 Amendments to the Credit Agreement, as discussed more fully below, limit capital expenditures to \$20,000,000 in 2009.



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**Table of Contents**

**Financing Activities**

Cash provided by financing activities totaled \$8,809,000 in the 13 weeks ended December 28, 2008. Cash required for financing activities totaled \$28,127,000 in the 13 weeks ended December 30, 2007. An increase in working capital and financing costs related to the 2009 Amendments and 2009 Waivers resulted in a net increase in debt in the current year period. Debt reduction and dividends accounted for the majority of the usage of funds in the prior year period. The annual dividend declared was \$0.76 per share in 2008. The 2009 Amendments require the Company to suspend stockholder dividends and share repurchases until its total leverage ratio is less than 4.5:1.

**Credit Agreement**

In 2006, the Company entered into an amended and restated credit agreement (Credit Agreement) with a syndicate of financial institutions (the Lenders). The Credit Agreement provided for aggregate borrowing of up to \$1,435,000,000 and consisted of a \$950,000,000 A Term Loan, \$35,000,000 B Term Loan and \$450,000,000 revolving credit facility. The Credit Agreement matures in June 2012 and amended and replaced a \$1,550,000,000 credit agreement consummated in 2005.

The Credit Agreement is fully and unconditionally guaranteed on a joint and several basis by substantially all of the Company's existing and future, direct and indirect subsidiaries in which the Company holds a direct or indirect interest of more than 50% (the Credit Parties); provided however, that Pulitzer and its subsidiaries will not become Credit Parties for so long as their doing so would violate the terms of the Pulitzer Notes discussed more fully below. The Credit Agreement was secured by first priority security interests in the stock and other equity interests owned by the Credit Parties in their respective subsidiaries.

Debt under the A Term Loan and revolving credit facility bore interest, at the Company's option, at either a base rate or an adjusted Eurodollar rate (LIBOR), plus an applicable margin. The base rate for the facility was the greater of the prime lending rate of Deutsche Bank Trust Company Americas at such time and 0.5% in excess of the overnight federal funds rate at such time. The margin applicable was a percentage determined according to the following: For revolving loans and A Term Loans, maintained as base rate loans: 0%, and maintained as Eurodollar loans: 0.625% to 1% depending, in each instance, upon the Company's leverage ratio at such time.

The Company may voluntarily prepay principal amounts outstanding or reduce commitments under the Credit Agreement at any time, in whole or in part, without premium or penalty, upon proper notice and subject to certain limitations as to minimum amounts of prepayments. The Company is required to repay principal amounts, on a quarterly basis until maturity, under the A Term Loan. In addition to the scheduled payments, the Company is required to make mandatory prepayments under the A Term Loan under certain other conditions. Total A Term Loan payments in the 13 weeks ended December 28, 2008 and 2007 were \$35,625,000 and \$62,250,000, respectively.

The Credit Agreement contains customary affirmative and negative covenants for financing of its type. These financial covenants include a maximum total leverage ratio. The total leverage ratio is based primarily on the principal amount of debt, net of cash, which equals \$1,217,787,000 at December 28, 2008, divided by a measure of trailing 12 month operating results which includes several factors, including distributions from TNI and MNI. The Company's total leverage ratio at December 28, 2008 was 5.90:1. The Credit Agreement also includes a minimum interest expense coverage ratio. The Company's interest expense coverage ratio at December 28, 2008 was 2.9:1. At December 28, 2008, the Company was in compliance with such covenants, as waived or amended from time to time.

The Credit Agreement required the Company to apply the net proceeds from asset sales to repayment of the A Term Loan to the extent such proceeds exceed the amount used to purchase assets (other than inventory and working capital) within one year of the asset sales. Repayments in 2008 met required repayments related to its sales transactions.

The Credit Agreement requires the Company to accelerate future payments under the A Term Loan in the amount of 75% of its Excess Cash Flow, as defined, beginning in 2008. The Company had Excess Cash Flow of approximately \$62,000,000 in 2008 and, as a result, paid \$46,325,000 originally due under the A Term Loan in March and June 2009, in December 2008, subsequent to the end of the quarter. The acceleration of such payments due to Excess Cash Flow does not change the due dates of other A Term Loan payments.

**Amendments to Credit Agreement**

In 2009, the Credit Agreement was amended (the 2009 Amendments).

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## **Table of Contents**

Under the 2009 Amendments, the Credit Parties pledged substantially all of their tangible and intangible assets, and granted mortgages covering certain real estate, as collateral for the payment and performance of their obligations under the Credit Agreement. Assets of Pulitzer, the Company's ownership interest in MNI and certain employee benefit plan assets are excluded.

The 2009 Amendments reduce the amount available under the revolving credit facility to \$375,000,000 and eliminate an unused incremental term loan facility. The 2009 Amendments require the Company to suspend stockholder dividends and share repurchases until its total leverage ratio is less than 4.5:1. The 2009 Amendments also limit capital expenditures to \$20,000,000 per year, with a provision for carryover of unused amounts from the prior year. Other covenants ensure that substantially all future cash flows of the Company are required to be directed for debt reduction.

Further, the 2009 Amendments modify other covenants, including restricting the Company's ability to make additional investments and acquisitions without the consent of its Lenders, limiting additional debt beyond that permitted under the Credit Agreement, and limiting the amount of unrestricted cash and cash equivalents the Company may hold to \$15,000,000.

Under the 2009 Amendments, the Company's credit spreads generally increase 200 basis points from the original pricing grid. The maximum rate (for leverage greater than 6.25:1) increased to LIBOR plus 400 basis points. At the December 2008 leverage level, the Company's debt under the Credit Agreement will be priced at LIBOR plus 350 basis points. The base rate margin was changed to 250 basis points.

Under the 2009 Amendments, the Company's total leverage ratio limit will increase from 6.5:1 in December 2008, to 6.75:1 in March 2009, decrease to 6.5:1 in December 2009, decrease to 6.25:1 in September 2010 and decrease to 4.5:1 in December 2010. Each change in the leverage ratio limit noted above is effective on the last day of the fiscal quarter.

The interest expense coverage ratio limit will be 2.0:1 through March 2009, decrease thereafter to 1.7:1 through September 2009, increase thereafter to 1.8:1 through December 2009, increase thereafter to 1.9:1 through March 2010, increase thereafter to 2.0:1 through September 2010, and increase thereafter to 2.5:1.

The Company paid a fee of 0.5% to consenting lenders, which along with the related expenses, totals \$6,478,000. The fees were capitalized and are being expensed over the respective periods of the 2009 Amendments.

## **Pulitzer Notes**

In conjunction with its formation in 2000, PD LLC borrowed \$306,000,000 (Pulitzer Notes) from a group of institutional lenders (the Noteholders). The aggregate principal amount of the Pulitzer Notes is payable in April 2009 and bears interest at an annual rate of 8.05%. The Pulitzer Notes are guaranteed by Pulitzer pursuant to a Guaranty Agreement dated May 1, 2000 (Guaranty Agreement) with the Noteholders. In turn, pursuant to an Indemnity Agreement dated May 1, 2000 (Indemnity Agreement) between The Herald Company, Inc. (Herald, Inc.) and Pulitzer, Herald, Inc. agreed to indemnify Pulitzer for any payments that Pulitzer may make under the Guaranty Agreement. In December 2006, Herald Inc. assigned its assets and liabilities to Herald.

The terms of the Pulitzer Notes, as amended, contain certain covenants and conditions including the maintenance, by Pulitzer, of the ratio of debt to EBITDA, as defined in the Guaranty Agreement, minimum net worth and limitations on the incurrence of other debt. At December 28, 2008, Pulitzer was in compliance with such covenants, as waived or amended from time to time. In addition, the Pulitzer Notes and the Operating Agreement with Herald (Operating Agreement) require that PD LLC maintain the Reserve, consisting of cash and investments in U.S. government securities, totaling approximately \$129,810,000 at December 28, 2008 (Reserve). The Pulitzer Notes and the Operating Agreement provide for a \$3,750,000 quarterly increase in the minimum Reserve balance through May 1, 2010, when the amount will total \$150,000,000. See Note 13 of the Notes to Consolidated Financial Statements, included herein.

The Credit Agreement contains a cross-default provision tied to the terms of the Pulitzer Notes.

The purchase price allocation of Pulitzer resulted in an increase in the value of the Pulitzer Notes in the amount of \$31,512,000, which is recorded as debt in the Consolidated Balance Sheets. This amount will be accreted over the remaining life of the Pulitzer Notes, until April 2009, as a reduction in interest expense using the interest method. This accretion will not increase the principal amount due to, or reduce the amount of interest to be paid to, the Noteholders.

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The Company is required to refinance the Pulitzer Notes from time to time, as they become due, until May 1, 2015, unless Herald exercises its rights under the Operating Agreement to require Pulitzer to redeem its 5% interest in PDLLC on May 1, 2010 (2010 Redemption). See Note 13 of the Notes to Consolidated Financial Statements, included herein.

## **Table of Contents**

### **2009 Waivers**

In December 2008, certain covenant violations related to the Credit Agreement and Pulitzer Notes, as applicable, were waived (the 2009 Waivers). The 2009 Waivers relate to the going concern modification of the auditors' reports on the Consolidated Financial Statements of the Company, and the separate financial statements of Pulitzer and PD LLC for 2008, and a delay in the timing of delivery of 2008 year end covenant compliance information related to the Credit Agreement and the Pulitzer Notes. Waivers were also obtained related to a violation of the Consolidated Net Worth (as defined) covenant as of September 28, 2008 and as of December 28, 2008 under the Pulitzer Notes. The waiver under the Credit Agreement expires March 30, 2009. The waiver under the Pulitzer Notes, which was initially scheduled to expire January 16, 2009, was extended through February 13, 2009. As of December 28, 2008, the Company was also in violation of the maximum debt to EBITDA covenant related to the Pulitzer Notes. A waiver of the covenant violation was obtained through February 13, 2009 under the Pulitzer Notes and through March 30, 2009 under the Credit Agreement. The waiver under the Pulitzer Notes contains a provision which allows it to be revoked upon 48 hours notice.

The Company paid fees and expenses related to the 2009 Waivers totaling \$1,599,000. The fees were capitalized and are being expensed over the respective waiver periods.

### **Liquidity**

The Company's ability to operate as a going concern is dependent on its ability to refinance or amend its debt agreements as they become due, or earlier if available liquidity is consumed.

The Company's indebtedness could adversely affect its financial health in any or all of the following ways:

- Substantially all of the cash flows of the Company are required to be applied to payment of debt interest and principal, reducing funds available for investment, capital expenditures and other purposes;
- The Company reported significant net losses in 2008 and the 13 weeks ended December 28, 2008, due to impairment of goodwill and other assets resulting from the continuing and increasing difference between its stock price and the per share carrying value of its net assets. Reduced expectations of future cash flows were also an important factor in the determination of such impairment charges;
- The Company's flexibility to react to changes in economic and industry conditions may be more limited;
- Increasing leverage could make the Company more vulnerable in the event of additional deterioration of general economic conditions or other adverse events; and
- Continuation of current business trends may result in additional violations of debt covenants in future periods.

There could be a material impact on the Company's business if it is unable to meet the conditions of its debt agreements or obtain replacement financing.

The Company generated cash flows in 2008 sufficient to reduce net debt by \$102,225,000, pay dividends totaling \$32,573,000 and acquire shares of its Common Stock in the amount of \$19,483,000. The Company does not have sufficient cash flows to meet both its requirements for 2009 operations and repayment of the Pulitzer Notes.

Remaining 2009 principal payments required under the Credit Agreement at January 31, 2009 totaling \$60,550,000 are expected to exceed the Company's cash flows available for such payments. As a result, the Company expects to utilize a portion of its capacity under its revolving credit facility to fund a portion of the 2009 principal payments required. At January 31, 2009, the Company had \$302,950,000 outstanding under the revolving credit facility, and after consideration of the 2009 Amendments and letters of credit, has approximately \$61,217,000 available for future use.

Principal payments under the Credit Agreement totaling \$166,250,000 are due in 2010. The Company expects to utilize the remainder of its capacity under its revolving credit facility to fund a portion of the 2010 principal payments required.

The Pulitzer Notes mature in April 2009. The Company is actively engaged in discussions with the Noteholders, and to the extent their approval may also be required, the Lenders, to extend or refinance the Pulitzer Notes. The Company has also initiated discussions with the Lenders related to changes to the Credit Agreement to maintain sufficient long-term liquidity. However, the timing and ultimate outcome of such discussions cannot be determined at this time due, in part, to the abnormal condition of the domestic credit markets and the overall recessionary operating environment in which the Company, Pulitzer, and other publishing

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companies are currently operating. Continuing instability or further disruptions of these markets could prohibit or make it more difficult for the Company to access new capital, increase the cost of capital or limit its ability to refinance existing indebtedness.

## **Table of Contents**

There are numerous potential consequences under the Credit Agreement, and Guaranty Agreement and Note Agreement related to the Pulitzer Notes, if an Event of Default, including those arising upon expiration of existing waivers, occurs and is not remedied. Many of those consequences are beyond the control of the Company, Pulitzer, and PD LLC, respectively. The occurrence of one or more Events of Default would give rise to the right of the Lenders or the Noteholders, or both of them, to exercise their remedies under the Credit Agreement and the Note and Guaranty Agreements, respectively, including, without limitation, the right to accelerate all outstanding debt and take actions authorized in such circumstances under applicable collateral security documents, any of which would impair the ability of the Company to operate its business as a going concern.

### **Interest Rate Exchange Agreements**

At December 28, 2008, the Company had outstanding interest rate swaps in the notional amount of \$125,000,000. The interest rate swaps have original terms of four to five years, carry interest rates from 4.3% to 4.4% (plus the applicable LIBOR margin) and effectively fix the Company's interest rate on debt in the amount, and for the time periods, of such instruments. In November 2008, interest rate swaps in the notional amounts of \$75,000,000 expired.

In 2008, the Company executed interest rate collars in the notional amount of \$150,000,000. The collars have a two year term and limit LIBOR to an average floor of 3.57% and a cap of 5.0%. Such collars effectively limit the range of the Company's exposure to interest rates to LIBOR greater than the floor and less than the cap (in either case plus the applicable LIBOR margin) for the time period of such instruments.

### **Discontinued Operations and Other Matters**

Cash required by discontinued operations totaled \$5,000 in the 13 weeks ended December 28, 2008 and provided \$14,836,000 in the 13 weeks ended December 30, 2007. Cash proceeds from the sales of discontinued operations and cash generated from operations were the primary sources of funds in the prior year period.

Cash and cash equivalents increased \$2,718,000 in the 13 weeks ended December 28, 2008, and \$7,732,000 in the 13 weeks ended December 30, 2007.

### **INFLATION**

The Company anticipates that changing costs of newsprint, its basic raw material, may impact future operating costs. Energy costs have also become more volatile. Price increases (or decreases) for the Company's products are implemented when deemed appropriate by management. The Company continuously evaluates price increases, productivity improvements, sourcing efficiencies and other cost reductions to mitigate the impact of inflation.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

The Company is exposed to market risk stemming from changes in interest rates and commodity prices. Changes in these factors could cause fluctuations in earnings and cash flows. In the normal course of business, exposure to certain of these market risks is managed as described below.

### **INTEREST RATES**

#### **Restricted Cash and Investments**

Interest rate risk in the Company's restricted cash and investments is managed by investing only in short-term securities. Only U.S. Government and related securities are permitted.

#### **Debt**

The Company's debt structure and interest rate risk are managed through the use of fixed and floating rate debt. The Company's primary exposure is to LIBOR. A 100 basis point increase to LIBOR would decrease income from continuing operations before income taxes on an annualized basis by approximately \$7,784,000, based on \$778,375,000 of floating rate debt outstanding at

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December 28, 2008, after consideration of the interest rate swaps described below, and excluding debt subject to interest rate collars described below and debt of MNI. Such interest rates may also decrease.

At December 28, 2008, the Company has outstanding interest rate swaps in the notional amount of \$125,000,000. The interest rate swaps have original terms of four to five years, carry interest rates from 4.3% to 4.4% (plus the applicable LIBOR margin) and effectively fix the Company's interest rate on debt in the amount, and for the time periods, of such instruments. In November 2008, interest rate swaps in the notional amounts of \$75,000,000 expired.



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## **Table of Contents**

In 2008, the Company executed interest rate collars in the notional amount of \$150,000,000. The collars have a two year term and limit LIBOR to an average floor of 3.57% and a cap of 5.0%. Such collars effectively limit the range of the Company's exposure to interest rates to LIBOR greater than the floor and less than the cap (in either case plus the applicable LIBOR margin) for the time period of such instruments.

At December 28, 2008, after consideration of the interest rate swaps described above, approximately 68% of the principal amount of the Company's debt is subject to floating interest rates. The interest rate collars described above limit the Company's exposure to interest rates on an additional 11% of the principal amount of its debt.

Certain of the Company's interest-earning assets, including those in employee benefit plans, also function as a natural hedge against fluctuations in interest rates on debt.

## **COMMODITIES**

Certain materials used by the Company are exposed to commodity price changes. The Company manages this risk through instruments such as purchase orders and non-cancelable supply contracts. The Company is a participant in a buying cooperative with other publishing companies, primarily for acquisition of newsprint. The Company is also involved in continuing programs to mitigate the impact of cost increases through identification of sourcing and operating efficiencies. Primary commodity price exposures are newsprint and, to a lesser extent, ink and energy costs.

Between November 2007 and December 2008, North American newsprint manufacturers implemented, or attempted to implement, as many as 13 price increases totaling up to \$265 per metric ton on standard 30 pound newsprint. Beginning in October 2008 several suppliers delayed or rescinded several of such price increases. North American newsprint suppliers took significant steps in 2008 to curtail newsprint production capacity in an effort to balance supply capacity with declining demand trends and additional capacity reductions have been announced for 2009. Curtailment activities include permanent, indefinite, and temporary shutdown of newsprint production facilities. However, the significant decline in North American 2008 newsprint demand and consumption, which is expected to continue in 2009, appears to be greater than the total newsprint production restraints and may favorably impact pricing trends in 2009. In addition, 2007 and 2008 increases in raw material costs, energy costs and the value of the Canadian dollar relative to the U.S. dollar, all of which contributed to recent increases in newsprint prices, have recently reverted to significantly lower levels, which may mitigate future increases in newsprint costs, or lead to a decline in such costs. The final extent of changes in price, if any, is subject to negotiation between such manufacturers and the Company.

A \$10 per metric ton price increase for 30 pound newsprint would result in an annualized reduction in income before income taxes of approximately \$1,000,000 based on anticipated consumption in 2009, excluding consumption of MNI and TNI and the impact of LIFO accounting. Such prices may also decrease.

## **SENSITIVITY TO CHANGES IN VALUE**

The Company's fixed rate debt consists of the Pulitzer Notes, which are not traded on an active market and held by a small group of Noteholders. Coupled with the volatility of substantially all domestic credit markets that exists in the current recession, the Company is unable, as of December 28, 2008, to measure the maximum potential impact on fair value of fixed rate debt of the Company in one year from adverse changes in market interest rates under normal market conditions. The change in value, if determined, would likely be significant.

Changes in the value of interest rate swaps and interest rate collars from movements in interest rates are not determinable, due to the number of variables involved in the pricing of such instruments. However, increases in interest rates would generally result in increases in the fair value of such instruments.

## **Item 4. Controls and Procedures**

In order to ensure that the information that must be disclosed in filings with the Securities and Exchange Commission is recorded, processed, summarized and reported in a timely manner, the Company has disclosure controls and procedures in place. The chief executive officer, Mary E. Junck, and chief financial officer, Carl G. Schmidt, have reviewed and evaluated the disclosure controls and procedures as of December 28, 2008, and have concluded that such controls and procedures are effective.

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There have been no changes in internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, such controls during the 13 weeks ended December 28, 2008.

**Table of Contents****PART II OTHER INFORMATION****Item 1. Legal Proceedings**

In April 2008, a group of newspaper carriers filed suit against the Company in the United States District Court for the Southern District of California, claiming to be employees and not independent contractors of the Company. The plaintiffs seek relief related to violation of various employment based statutes, and request punitive damages and attorneys' fees. Since the suit is in the earliest of phases, the Company is unable to predict whether the ultimate economic outcome, if any, could have a material effect on the Company's Consolidated Financial Statements, taken as a whole. The Company denies the allegations of employee status, consistent with past practices of the Company and the industry, and intends to vigorously contest the action, which is not covered by insurance.

**Item 2(c). Issuer Purchases of Equity Securities**

During the 13 weeks ended December 28, 2008, the Company purchased shares of Common Stock, as noted in the table below, in transactions with participants in its 1990 Long-Term Incentive Plan. The transactions resulted from the withholding of shares to pay the exercise price for taxes related to the restricted stock vesting.

| Month    | Shares Purchased | Average Price Per Share |
|----------|------------------|-------------------------|
| November | 36,426           | \$1.52                  |

**Item 6. Exhibits**

| Number | Description                            |
|--------|--|
| 31.1   | Rule 13a-14(a)/15d-14(a) certification |
| 31.2   | Rule 13a-14(a)/15d-14(a) certification |
| 32     | Section 1350 certification             |

**SIGNATURES**

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

LEE ENTERPRISES, INCORPORATED

/s/ Carl G. Schmidt  
 Carl G. Schmidt  
 Vice President, Chief Financial Officer and Treasurer  
 (Principal Financial and Accounting Officer)

Date: February 6, 2009