ARBITRON INC
Form 10-Q
November 03, 2005

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

þ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended September 30, 2005
Or

o **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the transition period from _______ to ______
Commission file number: 1-1969
ARBITRON INC.
(Exact name of registrant as specified in its charter)

Delaware	**52-0278528**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

142 West 57th Street
New York, New York 10019
(Address of principal executive offices) (Zip Code)
(212) 887-1300
(Registrant s telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes þ No o

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

The registrant had 30,866,553 shares of common stock, par value $0.50 per share, outstanding as of October 28, 2005.

ARBITRON INC.
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Arbitron owns or has the rights to various trademarks, trade names or service marks used in its radio audience measurement business and subsidiaries, including the following: the Arbitron name and logo, *RetailDirect®*, *RADAR®*, *Tapscan®*, *Tapscan WorldWide®*, *Integrated Radio Systems*(IRS) SM, *LocalMotion®, Maximi$er®, Maximi$er® Plus*, *Arbitron PD Advantage®*, *SmartPlus®*, *Arbitron Portable People Meter*™, *Marketing Resources Plus™, MRP™, PrintPlus™, MapMAKER Direct*SM, *Media Professional*SM*, Media Professional Plus*SM, *Qualitap*SM, *MediaMaster*SM, *Prospector*SM, and *Schedule-It*SM.
The trademark *Windows®* is the registered trademark of Microsoft Corporation.
Media Rating Council® is a registered trademark of the Media Rating Council.

PART I FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

ARBITRON INC.
Consolidated Balance Sheets
(In thousands, except par value data)

	September 30, 2005 (unaudited)	December 31, 2004 (audited)
Assets		
Current assets		
Cash and cash equivalents	$ 106,215	$ 86,901
Trade accounts receivable, net of allowance for doubtful accounts of $1,160 in 2005 and $1,124 in 2004	25,150	23,369
Deferred tax assets	3,274	4,362
Prepaid expenses and other current assets	5,072	5,529
Total current assets	139,711	120,161
Investment in affiliate	8,717	12,130
Property and equipment, net of accumulated depreciation of $22,172 in 2005 and $19,456 in 2004	23,700	18,536
Goodwill, net	40,558	37,773
Other intangibles, net	4,049	3,381
Noncurrent deferred tax assets	2,774	3,025
Other noncurrent assets	1,515	1,115
Total assets	$ 221,024	$ 196,121
Liabilities and Stockholders Equity		
Current liabilities		
Accounts payable	$ 7,039	$ 5,444
Accrued expenses and other current liabilities	25,582	30,955
Deferred revenue	54,568	59,608
Total current liabilities	87,189	96,007
Noncurrent liabilities		
Long-term debt	50,000	50,000
Other noncurrent liabilities	4,541	4,734
Total liabilities	141,730	150,741
Stockholders equity		

Common stock, $0.50 par value, authorized 500,000 shares, issued 32,336 shares in 2005 and 2004		16,168		16,168
Additional paid-in capital		89,277		101,914
Accumulated earnings (net distributions to Ceridian in excess of accumulated earnings) prior to spin-off		(242,870)		(242,870)
Retained earnings subsequent to spin-off		220,134		173,360
Common stock held in treasury, 1,478 shares in 2005 and 1,376 shares in 2004		(739)		(688)
Accumulated other comprehensive loss		(2,676)		(2,504)
Total stockholders equity		79,294		45,380
Total liabilities and stockholders equity	$	221,024	$	196,121

See notes to consolidated financial statements.

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

	Three Months Ended September 30, 2005	Three Months Ended September 30, 2004
Revenue	$ 85,615	$ 81,965
Costs and expenses		
Cost of revenue	25,643	23,531
Selling, general and administrative	16,802	14,994
Research and development	10,246	8,604
Total costs and expenses	52,691	47,129
Operating income	32,924	34,836
Equity in net income (loss) of affiliate	193	(1,118)
Income before interest and income tax expense	33,117	33,718
Interest income	797	309
Interest expense	986	1,842
Income before income tax expense	32,928	32,185
Income tax expense	12,027	7,957
Net income	$ 20,901	$ 24,228
Net income per weighted-average common share		
Basic	$ 0.67	$ 0.78
Diluted	$ 0.66	$ 0.77
Dividends declared per share	$ 0.10	$
Weighted-average common shares used in calculations		
Basic	31,198	31,174
Potentially dilutive securities	321	388
Diluted	31,519	31,562

See notes to consolidated financial statements.

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

	Nine Months Ended September 30, 2005	Nine Months Ended September 30, 2004
Revenue	$ 234,626	$ 223,634
Costs and expenses		
Cost of revenue	75,531	74,789
Selling, general and administrative	50,063	45,285
Research and development	26,942	23,471
Total costs and expenses	152,536	143,545
Operating income	82,090	80,089
Equity in net income of affiliate	2,337	1,411
Income before interest and income tax expense	84,427	81,500
Interest income	2,225	707
Interest expense	3,053	6,220
Income before income tax expense	83,599	75,987
Income tax expense	27,467	25,040
Net income	$ 56,132	$ 50,947
Net income per weighted-average common share		
Basic	$ 1.80	$ 1.64
Diluted	$ 1.77	$ 1.62
Dividends declared per share	$ 0.30	$
Weighted-average common shares used in calculations		
Basic	31,265	30,982
Potentially dilutive securities	359	539
Diluted	31,624	31,521

See notes to consolidated financial statements.

ARBITRON INC.
Consolidated Statements of Cash Flows
(In thousands)
(unaudited)

	Nine Months Ended September 30,	
	2005	**2004**
Cash flows from operating activities		
Net income	$ 56,132	$ 50,947
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	3,024	3,216
Other amortization	1,186	996
Loss on asset disposals	237	458
Asset impairment charge		328
Deferred income taxes	1,424	23,109
Equity in net income of affiliate	(2,337)	(1,411)
Distributions from affiliate	5,750	5,374
Bad debt expense	370	346
Tax benefit from stock option exercises	5,053	4,297
Noncash compensation	296	141
Changes in operating assets and liabilities, excluding effects of business acquisitions		
Trade accounts receivable	(2,243)	(7,956)
Prepaid expenses and other assets	(1,858)	(1,935)
Accounts payable	1,663	(739)
Accrued expenses and other current liabilities	(8,437)	(3,782)
Deferred revenue	(5,065)	(7,159)
Other noncurrent liabilities	(643)	219
Net cash provided by operating activities	54,552	66,449
Cash flows from investing activities		
Additions to property and equipment	(8,401)	(7,149)
Payment for business acquisition	(4,176)	(8,928)
Net cash used by investing activities	(12,577)	(16,077)
Cash flows from financing activities		
Proceeds from stock option exercises and stock purchase plan	23,802	14,810
Dividends paid to stockholders	(6,275)	
Stock repurchases	(39,976)	(9,927)
Payment of long-term debt		(55,000)
Net cash used by financing activities	(22,449)	(50,117)
Effect of exchange rate changes on cash	(212)	41

Net increase in cash and cash equivalents	19,314	296
Cash and cash equivalents at beginning of period	86,901	68,433
Cash and cash equivalents at end of period	$ 106,215	$ 68,729

See notes to consolidated financial statements.

ARBITRON INC.
Notes to Consolidated Financial Statements
September 30, 2005
(unaudited)

1. Basis of Presentation and Consolidation

Presentation

The accompanying unaudited consolidated financial statements of Arbitron Inc. (the Company or Arbitron) have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments considered necessary for fair presentation have been included. The consolidated balance sheet as of December 31, 2004 was audited at that date, but all of the information and footnotes as of December 31, 2004 required by U.S. generally accepted accounting principles have not been included in this Form 10-Q. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2004.

Consolidation

The consolidated financial statements of Arbitron reflect the consolidated financial position, results of operations and cash flows of Arbitron Inc. and its subsidiaries: Arbitron Holdings Inc., Audience Research Bureau S.A. de C.V., Ceridian Infotech (India) Private Limited, CSW Research Limited and Euro Fieldwork Limited.

2. Pro Forma Disclosures of Stock-Based Compensation

The Company applies the intrinsic-value-based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations including Financial Accounting Standards Board (FASB) Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation*, an interpretation of APB Opinion No. 25, to account for its fixed-plan stock options. Under this method, compensation expense is recorded on the date of option grant only if the current market price of the underlying stock exceeded the exercise price of the options. In the case of issuances of stock awards, compensation expense is recorded based upon the quoted market value of shares of common stock on the date of grant. Any resulting compensation expense is recognized ratably over the vesting period. Statement of Financial Accounting Standards (SFAS) No. 123 (SFAS No. 123), *Accounting for Stock-Based Compensation* (as amended by SFAS No. 148, *Accounting for Stock-Based Compensation Transitions and Disclosures*), established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic-value-based method of accounting described above and has adopted only the disclosure requirements of SFAS No. 123. The following table illustrates the effect on net income if the fair-value-based method had been applied to all outstanding and unvested awards in each period (dollars in thousands, except per share data):

	Three Months Ended September 30, 2005	2004	Nine Months Ended September 30, 2005	2004
Net income, as reported	$ 20,901	$ 24,228	$ 56,132	$ 50,947
Add: Stock-based compensation expense, net of tax	62		183	
Less: Stock-based compensation expense determined under fair value method, net of tax	1,327	501	4,155	2,110
Pro forma net income	$ 19,636	$ 23,727	$ 52,160	$ 48,837
Basic net income per weighted-average common share, as reported	$ 0.67	$ 0.78	$ 1.80	$ 1.64
Pro forma basic net income per weighted-average common share	$ 0.63	$ 0.76	$ 1.67	$ 1.58
Diluted net income per weighted-average common share, as reported	$ 0.66	$ 0.77	$ 1.77	$ 1.62
Pro forma diluted net income per weighted- average common share	$ 0.63	$ 0.74	$ 1.66	$ 1.54
Options granted to employees and directors	21,502	366,062	576,434	472,999
Weighted-average exercise price	$ 40.92	$ 38.24	$ 40.90	$ 38.00
Weighted-average fair value	$ 13.53	$ 13.85	$ 13.71	$ 13.04
Weighted-average assumptions:				
Expected lives in years	6.5	6.5	6.5	6.0
Expected volatility	28.1%	27.3%	28.5%	27.3%
Expected dividend rate	1.0%		1.0%	
Risk-free interest rate	4.11%	3.75%	3.87%	3.68%

During the quarter ended September 30, 2005, Arbitron granted 15,000 shares of stock awards with a fair value of $0.6 million vesting monthly over a sixty month period.

3. Acquisition

On September 20, 2005, Arbitron acquired the net assets of Integrated Radio Systems, L.L.C. (IRS[SM]) for $4.6 million, including $0.1 million in transaction costs. IRS is a provider of software systems that help radio stations manage their advertising sales process and automate the daily tasks in a sales department. The IRS applications combine a customer relationship management system with scheduling and research applications and with inventory/pricing management tools. The $4.6 million purchase price was allocated to $1.8 million in identifiable intangible assets and tangible net assets and $2.8 million in goodwill. The purchase price includes a deferred cash payment of $0.5 million, which is due in September 2008.

4. Long-Term Debt

Long-term debt consisted of senior secured fixed-rate notes in the amount of $50.0 million as of September 30, 2005, and December 31, 2004. The notes bear interest at a fixed rate of 9.96% and mature on January 31, 2008. The fair values of the senior secured notes as of September 30, 2005, and December 31, 2004, were $52.2 million and $53.8 million, respectively, and were estimated using a cash flow valuation model and available market data for securities with similar maturity dates. The senior-secured-notes agreement contains certain financial covenants and also contains a make-whole provision that applies in the event of early prepayment of principal. The senior secured notes limit, among other things, the Company s ability to incur additional indebtedness, grant or incur liens on its assets, pay cash dividends over a certain amount, make investments or acquisitions, repurchase or redeem capital stock and engage in certain mergers or consolidations. On June 10, 2005, the senior-secured-notes agreement was amended. The amendment deleted certain requirements to make mandatory prepayment offers, amended certain notice requirements, deleted interest rate hedging obligations, and eliminated or loosened the restrictions applicable under various negative covenants, including those relating to, among other things, acquisitions, the creation of joint ventures, the payment of dividends and distributions, and capital expenditures. The Company was in compliance with its covenants as of September 30, 2005.

If a default occurs under the terms of Arbitron s senior secured notes, the lenders could proceed against the lenders collateral, which includes a first-priority lien on substantially all of the assets of Arbitron and its domestic subsidiaries and a pledge of the capital stock of all of its domestic subsidiaries and of 65% of the capital stock of its foreign subsidiaries. In addition, a default may result in higher rates of interest and the inability to obtain additional financing.

5. Stockholders Equity

Changes in stockholders equity for the nine months ended September 30, 2005, were as follows (in thousands):

	Shares Outstanding	Common Stock	Treasury Stock	Additional Paid-In Capital	Net Distributions to Ceridian in Excess of Accumulated Earnings	Retained Earnings Subsequent to Spin-off	Accumulated Other Compre-hensive Loss	Total Stock-Holders Equity
Balance as of December 31, 2004	30,960	$16,168	$(688)	$101,914	$(242,870)	$173,360	$(2,504)	$45,380
Net income						56,132		56,132
Common stock issued	847		423	21,516				21,939
Stock repurchased	(949)		(474)	(39,502)				(39,976)
Tax benefit from stock option exercises				5,053				5,053
Noncash compensation				296				296
Dividends declared						(9,358)		(9,358)
Other comprehensive loss							(172)	(172)
Balance as of September 30, 2005	30,858	$ 16,168	$ (739)	$ 89,277	$ (242,870)	$ 220,134	$ (2,676)	$ 79,294

A quarterly cash dividend of $0.10 per common share was paid to stockholders on April 1, July 1, and October 3, 2005.

6. Net Income Per Weighted-Average Common Share

The computations of basic and diluted net income per weighted-average common share for the three and nine months ended September 30, 2005, and 2004 are based on Arbitron s weighted-average shares of common stock and potentially dilutive securities outstanding.

Potentially dilutive securities are calculated in accordance with the treasury stock method, which assumes that the proceeds from the exercise of all stock options are used to repurchase the Company s common stock at the average market price for the period. On June 15, 2005, the Company announced that its Board of Directors authorized a program to repurchase up to $40.0 million of its outstanding common stock through either periodic open-market or private transactions through November 2005. As of August 22, 2005, the repurchase program was completed with 948,594 shares repurchased for an aggregate purchase price of approximately $40.0 million.

7. Comprehensive Income

The Company s comprehensive income comprises net income, foreign currency translation adjustments and changes in additional minimum pension liability. The components of comprehensive income were as follows (in thousands) :

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
	2005	**2004**	**2005**	**2004**
Net income	$ 20,901	$ 24,228	$ 56,132	$ 50,947
Items of other comprehensive income				
Change in foreign currency translation adjustment	(37)	(5)	(258)	53
Change in fair value of interest rate swap		292		1,171
Income tax benefit (expense), net	14	(134)	86	(564)
Comprehensive income	$ 20,878	$ 24,381	$ 55,960	$ 51,607