Warner Music Group Corp.
Form 10-Q
August 07, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission File Number 001-32502

Warner Music Group Corp.

(Exact name of Registrant as specified in its charter)

Delaware	13-4271875
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1633 Broadway

New York, NY 10019

(Address of principal executive offices)

(212) 275-2000

(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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer		Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)	Smaller reporting company
Emerging growth company		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

There is no public market for the Registrant's common stock. As of August 7, 2018 the number of shares of the Registrant's common stock, par value $0.001 per share, outstanding was 1,052. All of the Registrant's common stock is owned by affiliates of Access Industries, Inc. The Registrant has filed all Exchange Act reports for the preceding 12 months.

WARNER MUSIC GROUP CORP.

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ITEM 1. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Warner Music Group Corp.

Consolidated Balance Sheets (Unaudited)

	June 30, 2018	September 30, 2017
	(in millions)	
Assets		
Current assets:		
Cash and equivalents	$905	$ 647
Accounts receivable, net of allowances of $41 million and $50 million	444	404
Inventories	40	39
Royalty advances expected to be recouped within one year	138	141
Prepaid and other current assets	58	44
Total current assets	1,585	1,275
Royalty advances expected to be recouped after one year	170	172
Property, plant and equipment, net	203	213
Goodwill	1,686	1,685
Intangible assets subject to amortization, net	1,884	2,090
Intangible assets not subject to amortization	146	117
Deferred tax assets, net	8	97
Other assets	82	69
Total assets	$5,764	$ 5,718
Liabilities and Equity		
Current liabilities:		
Accounts payable	$168	$ 208
Accrued royalties	1,492	1,263
Accrued liabilities	377	365
Accrued interest	19	41
Deferred revenue	212	197
Other current liabilities	19	26
Total current liabilities	2,287	2,100
Long-term debt	2,814	2,811
Deferred tax liabilities, net	197	190
Other noncurrent liabilities	275	309
Total liabilities	$5,573	$ 5,410
Equity:		
Common stock ($0.001 par value; 10,000 shares authorized; 1,052 shares issued and outstanding)	$—	$ —
Additional paid-in capital	1,128	1,128
Accumulated deficit	(758)	(654)
Accumulated other comprehensive loss, net	(195)	(181)

Total Warner Music Group Corp. equity	175	293
Noncontrolling interest	16	15
Total equity	191	308
Total liabilities and equity	$5,764	$ 5,718

See accompanying notes

Warner Music Group Corp.

Consolidated Statements of Operations (Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2018	2017	2018	2017
	(in millions)		(in millions)	
Revenue	$958	$917	$2,966	$2,659
Costs and expenses:				
Cost of revenue	(531)	(519)	(1,588)	(1,430)
Selling, general and administrative expenses (a)	(343)	(296)	(1,013)	(854)
Amortization expense	(56)	(51)	(164)	(152)
Total costs and expenses	(930)	(866)	(2,765)	(2,436)
Operating income	28	51	201	223
Loss on extinguishment of debt	(7)	(3)	(31)	(35)
Interest expense, net	(33)	(36)	(105)	(112)
Other income (expense), net	394	(21)	392	(21)
Income (loss) before income taxes	382	(9)	457	55
Income tax (expense) benefit	(61)	152	(132)	132
Net income	321	143	325	187
Less: Income attributable to noncontrolling interest	(1)	(2)	(4)	(5)
Net income attributable to Warner Music Group Corp.	$320	$141	$321	$182
(a) Includes depreciation expense of:	$(15)	$(13)	$(41)	$(38)

See accompanying notes

Warner Music Group Corp.

Consolidated Statements of Comprehensive Income (Unaudited)

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2018	2017	2018	2017
	(in millions)		(in millions)	
Net income	$321	$143	$325	$187
Other comprehensive (loss) income, net of tax:				
Foreign currency adjustment	(31)	26	(13)	13
Deferred (losses) gains on derivative financial instruments	(3)	1	(1)	—
Other comprehensive (loss) income, net of tax	(34)	27	(14)	13
Total comprehensive income	287	170	311	200
Less: Income attributable to noncontrolling interest	(1)	(2)	(4)	(5)
Comprehensive income attributable to Warner Music Group Corp.	$286	$168	$307	$195

See accompanying notes

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Warner Music Group Corp.

Consolidated Statements of Cash Flows (Unaudited)

	Nine Months Ended June 30, 2018 (in millions)		2017	
Cash flows from operating activities				
Net income	$	325	$	187
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization		205		190
Unrealized losses (gains) and remeasurement of foreign denominated loans		(6)		19
Deferred income taxes		105		(165)
Loss on extinguishment of debt		31		35
Net (gain) loss on divestitures and investments		(385)		17
Non-cash interest expense		5		6
Equity-based compensation expense		52		26
Changes in operating assets and liabilities:				
Accounts receivable		(43)		(55)
Inventories		(1)		2
Royalty advances		—		(15)
Accounts payable and accrued liabilities		(84)		(55)
Royalty payables		113		152
Accrued interest		(22)		(14)
Deferred revenue		—		(25)
Other balance sheet changes		(30)		4
Net cash provided by operating activities		265		309

Cash flows from investing activities		
Acquisition of music publishing rights, net	(11)	(11)
Capital expenditures	(40)	(29)
Investments and acquisitions of businesses, net	(14)	(9)
Proceeds from the sale of investments	516	43
Net cash provided by (used in) investing activities	451	(6)
Cash flows from financing activities		
Proceeds from issuance of Acquisition Corp. 4.125% Senior Secured Notes	—	380
Proceeds from issuance of Acquisition Corp. 4.875% Senior Secured Notes	—	250
Proceeds from issuance of Acquisition Corp. 5.50% Senior Notes	325	—
Proceeds from supplement of Acquisition Corp. Senior Term Loan Facility	320	22
Repayment of Acquisition Corp. 6.00% Senior Secured Notes	—	(450)
Repayment of Acquisition Corp. 6.25% Senior Secured Notes	—	(173)
Repayment of Acquisition Corp. 5.625% Senior Secured Notes	—	(28)
Repayment of Acquisition Corp. 6.75% Senior Notes	(635)	—
Call premiums paid on early redemption of debt	(23)	(27)
Deferred financing costs paid	(12)	(13)

Distribution to noncontrolling interest holder		(3)		(4)
Dividends paid		(425)		(54)
Net cash used in financing activities		(453)		(97)
Effect of exchange rate changes on cash and equivalents		(5)		2
Net (decrease) increase in cash and equivalents		258		208
Cash and equivalents at beginning of period		647		359
Cash and equivalents at end of period	$	905	$	567

See accompanying notes

Warner Music Group Corp.

Consolidated Statements of Equity (Unaudited)

	Common Stock Shares	Value	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Warner Music Group Corp. Equity	Noncontrolling Interest	Total Equity
	(in millions, except share amounts)							
Balance at September 30, 2017	1,055	$ —	$ 1,128	$ (654)	$ (181)	$ 293	$ 15	$ 308
Net income	—	—	—	321	—	321	4	325
Dividends	—	—	—	(425)	—	(425)	—	(425)
Other comprehensive loss, net of tax	—	—	—	—	(14)	(14)	—	(14)
Distribution to noncontrolling interest holders	—	—	—	—	—	—	(3)	(3)
Other	(3)	—	—	—	—	—	—	—
Balance at June 30, 2018	1,052	$ —	$ 1,128	$ (758)	$ (195)	$ 175	$ 16	$ 191

See accompanying notes

Warner Music Group Corp.

Notes to Consolidated Interim Financial Statements (Unaudited)

1. Description of Business

Warner Music Group Corp. (the "Company") was formed on November 21, 2003. The Company is the direct parent of WMG Holdings Corp. ("Holdings"), which is the direct parent of WMG Acquisition Corp. ("Acquisition Corp."). Acquisition Corp. is one of the world's major music-based content companies.

Acquisition of Warner Music Group by Access Industries

Pursuant to an Agreement and Plan of Merger, dated as of May 6, 2011 (the "Merger Agreement"), by and among the Company, AI Entertainment Holdings LLC (formerly Airplanes Music LLC), a Delaware limited liability company ("Parent") and an affiliate of Access Industries, Inc. ("Access"), and Airplanes Merger Sub, Inc., a Delaware corporation and a wholly owned subsidiary of Parent ("Merger Sub"), on July 20, 2011 (the "Merger Closing Date"), Merger Sub merged with and into the Company with the Company surviving as a wholly owned subsidiary of Parent (the "Merger"). In connection with the Merger, the Company delisted its common stock from the NYSE. The Company continues voluntarily to file with the SEC current and periodic reports that would be required to be filed with the SEC pursuant to Section 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") as provided for in certain covenants contained in the agreements governing its outstanding indebtedness.

Recorded Music Operations

The Company's Recorded Music business primarily consists of the discovery and development of artists and the related marketing, distribution and licensing of recorded music produced by such artists. The Company plays an integral role in virtually all aspects of the recorded music value chain from discovering and developing talent to producing music and promoting artists and their products.

In the United States, Recorded Music operations are conducted principally through the Company's major record labels—Warner Bros. Records and Atlantic Records. The Company's Recorded Music operations also include Rhino, a division that specializes in marketing the Company's music catalog through compilations and reissuances of previously released music and video titles. The Company also conducts its Recorded Music operations through a collection of additional record labels, including Asylum, Big Beat, Canvasback, East West, Elektra, Erato, FFRR, Fueled by Ramen, Nonesuch, Parlophone, Reprise, Roadrunner, Sire, Spinnin', Warner Classics and Warner Music Nashville.

Outside the United States, Recorded Music activities are conducted in more than 50 countries through various subsidiaries, affiliates and non-affiliated licensees. Internationally, the Company engages in the same activities as in the United States: discovering and signing artists and distributing, marketing and selling their recorded music. In most cases, the Company also markets and distributes the music of those artists for whom the Company's domestic record labels have international rights. In certain smaller markets, the Company licenses the right to distribute the Company's records to non-affiliated third-party record labels. The Company's international artist services operations include a network of concert promoters through which it provides resources to coordinate tours for the Company's artists and other artists as well as management companies that guide artists with respect to their careers.

The Company's Recorded Music distribution operations include Warner-Elektra-Atlantic Corporation ("WEA Corp."), which markets and sells music and video products to retailers and wholesale distributors; Alternative Distribution

Alliance (“ADA”), which distributes the products of independent labels to retail and wholesale distributors; and various distribution centers and ventures operated internationally.

In addition to the Company’s Recorded Music products being sold in physical retail outlets, Recorded Music products are also sold in physical form to online physical retailers such as Amazon.com and bestbuy.com and in digital form to an expanded universe of digital partners, including digital streaming services such as Amazon, Apple Music, Deezer, Napster, Soundcloud, Spotify and YouTube, digital radio services such as iHeart Radio, Pandora and Sirius XM and digital download services such as Apple’s iTunes and Google Play.

The Company has integrated the exploitation of digital content into all aspects of its business, including artist and repertoire (“A&R”), marketing, promotion and distribution. The Company’s business development executives work closely with A&R departments to ensure that while music is being produced, digital assets are also created with all distribution channels in mind, including streaming services, social networking sites, online portals and music-centered destinations. The Company also works side by side with its online and mobile partners to test new concepts. The Company believes existing and new digital businesses will be a significant source of growth and will provide new opportunities to successfully monetize its assets and create new revenue streams. The proportion of digital revenues attributed to each distribution channel varies by region and proportions may change as the roll out of new technologies continues. As an owner of music content, the Company believes it is well positioned to take advantage of growth in digital distribution and emerging technologies to maximize the value of its assets.

The Company has diversified its revenues beyond its traditional businesses by entering into expanded-rights deals with recording artists in order to partner with artists in other aspects of their careers. Under these agreements, the Company provides services to and participates in artists’ activities outside the traditional recorded music business such as touring, merchandising and sponsorships. The Company has built artist services capabilities and platforms for exploiting this broader set of music-related rights and participating more widely in the monetization of the artist brands it helps create.

The Company believes that entering into expanded-rights deals and enhancing its artist services capabilities in areas such as concert promotion and management have permitted it to diversify revenue streams and capitalize on other revenue opportunities. This provides for improved long-term relationships with artists and allows the Company to more effectively connect artists and fans.

Music Publishing Operations

While recorded music is focused on exploiting a particular recording of a composition, music publishing is an intellectual property business focused on the exploitation of the composition itself. In return for promoting, placing, marketing and administering the creative output of a songwriter, or engaging in those activities for other rightsholders, the Company’s Music Publishing business garners a share of the revenues generated from use of the composition.

The Company’s Music Publishing operations are conducted principally through Warner/Chappell, its global Music Publishing company, headquartered in Los Angeles with operations in over 50 countries through various subsidiaries, affiliates and non-affiliated licensees. The Company owns or controls rights to more than one million musical compositions, including numerous pop hits, American standards, folk songs and motion picture and theatrical compositions. Assembled over decades, its award-winning catalog includes over 70,000 songwriters and composers and a diverse range of genres including pop, rock, jazz, classical, country, R&B, hip-hop, rap, reggae, Latin, folk, blues, symphonic, soul, Broadway, techno, alternative and gospel. Warner/Chappell also administers the music and soundtracks of several third-party television and film producers and studios. The Company has an extensive production music library collectively branded as Warner/Chappell Production Music.

2. Summary of Significant Accounting Policies

Interim Financial Statements

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine month period ended June 30, 2018 are not necessarily indicative of the results that may be expected for the fiscal year ending September 30, 2018.

The consolidated balance sheet at September 30, 2017 has been derived from the audited consolidated financial statements at that date but does not include all of the information and notes required by U.S. GAAP for complete financial statements.

For further information, refer to the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2017 (File No. 001-32502).

Basis of Consolidation

The accompanying financial statements present the consolidated accounts of all entities in which the Company has a controlling voting interest and/or variable interest required to be consolidated in accordance with U.S. GAAP. All intercompany balances and transactions have been eliminated.

Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 810, Consolidation (“ASC 810”), requires the Company first evaluate its investments to determine if any investments qualify as a variable interest entity (“VIE”). A VIE is consolidated if the Company is deemed to be the primary beneficiary of the VIE, which is the party involved with the VIE that has both (i) the power to control the most significant activities of the VIE and (ii) either the obligation to absorb losses or the right to receive benefits that could potentially be significant to the VIE. If an entity is not deemed to be a VIE, the Company consolidates the entity if the Company has a controlling voting interest.

The Company maintains a 52-53 week fiscal year ending on the last Friday in each reporting period. As such, all references to June 30, 2018 and June 30, 2017 relate to the periods ended June 29, 2018 and June 30, 2017, respectively. For convenience purposes, the Company continues to date its financial statements as of June 30. The fiscal year ended September 30, 2017 ended on September 29, 2017.

The Company has performed a review of all subsequent events through the date the financial statements were issued, and has determined that no additional disclosures are necessary.

Income Taxes

At the end of each interim period, the Company makes its best estimate of the effective tax rate expected to be applicable for the full fiscal year and uses that rate to provide for income taxes on a current year-to-date basis before discrete items. If a reliable estimate of the annual effective tax rate cannot be made, which could be caused by the significant variability in rates when marginal earnings are expected for the year, a discrete tax rate is calculated for the period.

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the “Tax Act”). In accordance with ASC Topic 740, Income Taxes (“ASC 740”) the Company recorded the impacts in the period of enactment.

New Accounting Pronouncements

In October 2017, the Company adopted ASU 2016-09, Compensation - Stock Compensation ("ASU 2016-09"). This ASU provides amended guidance which simplifies the accounting for share-based payment transactions involving multiple aspects of the accounting for share-based transactions, including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The adoption of ASU 2016-09 did not have any effect on the Company’s consolidated financial statements and footnote disclosures as of June 30, 2018.

In May 2014, the FASB issued guidance codified in ASC 606, Revenue from Contracts with Customers (“ASC 606”), which replaces the guidance in former ASC 605, Revenue Recognition and ASC 928-605, Entertainment – Music. The amendment was the result of a joint effort by the FASB and the International Accounting Standards Board to improve financial reporting by creating common revenue recognition guidance for U.S. GAAP and international financial reporting standards ("IFRS"). The joint project clarifies the principles for recognizing revenue and develops a common revenue standard for U.S. GAAP and IFRS. ASC 606 is effective for annual periods beginning after December 15, 2017, and interim periods within those years. Early adoption is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. The update may be applied using one of two methods: retrospective application to each prior reporting period presented, or retrospective application with the cumulative effect of initially applying the update recognized at the date of initial application. The Company plans to adopt this ASU on October 1, 2018 under the modified retrospective method. While the Company has not completed its evaluation of the impact of adopting this new standard on the consolidated financial statements, the Company has made significant progress towards completing its assessment and believes the most significant impact will be a change in the timing of revenue recognition in our Music Publishing segments. The Company generally records revenue from the licensing of publishing rights when cash is received. Under the new revenue recognition rules, revenues will be recorded based on best estimates available in the period of sales or usage.

In January 2016, the FASB issued ASU 2016-01, Recognition and Measurement of Financial Assets and Financial Liabilities ("ASU 2016-01"). This ASU will require that equity investments are measured at fair value with changes in fair value recognized in net income. The Company may elect to measure equity investments that do not have a readily determinable fair value at cost minus impairment, if any, plus or minus changes resulting from observable price. ASU 2016-01 will be effective for annual periods beginning after December 15, 2017, and interim periods within those years. Earlier adoption is permitted. The adoption of this standard is not currently expected to have a significant impact on the Company's financial statements, other than disclosure, however the impact is dependent on the materiality of the Company's equity investments upon adoption.

In February 2016, the FASB issued ASU 2016-02, Leases (“ASU 2016-02”). This ASU establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the statement of operations. ASU 2016-02 will be effective for annual periods beginning after December 15, 2018, and interim periods within those years. Earlier adoption is permitted. The Company is evaluating the impact of the adoption of this standard on its financial statements and disclosures.

In August 2016, the FASB issued ASU 2016-15, Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments ("ASU 2016-15"). This ASU provides specific guidance of how certain cash receipts and cash payments should be presented and classified in the statement of cash flows. ASU 2016-15 is effective for annual periods beginning after December 15, 2017, and interim periods within those years. Early adoption is permitted. The adoption of this standard is not expected to have an impact on the Company’s financial statements.

In October 2016, the FASB issued ASU 2016-16, Income Taxes: Intra-Entity Transfers of Assets Other Than Inventory ("ASU 2016-16"). This ASU requires the recognition of current and deferred income taxes for intra-entity asset transfers when the transaction occurs. ASU 2016-16 is effective for annual periods beginning after December 15, 2017, and interim periods within those years. Early adoption is permitted using the modified retrospective approach with a cumulative-effect to opening retained earnings in the period of adoption. The Company does not plan to early adopt this standard and the impact upon the required adoption date is not expected to have a significant impact on the Company’s financial statements.

In August 2017, the FASB issued ASU 2017-12, Targeted Improvements to Accounting for Hedging Activities (“ASU 2017-12”). This ASU improves certain aspects of the hedge accounting model including making more risk management strategies eligible for hedge accounting and simplifying the assessment of hedge effectiveness. ASU 2017-12 is effective for all annual periods beginning after December 15, 2018 and interim periods within those fiscal years. Early adoption is permitted and requires a prospective adoption with a cumulative-effect adjustment to retained earnings as of the beginning of the fiscal year of adoption for existing hedging relationships. The Company is evaluating the impact of the adoption of this standard on its financial statements and disclosures.

In February 2018, FASB issued ASU 2018-02, Income Statement – Reporting Comprehensive Income (“ASU 2018-02”). This ASU allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Act. ASU 2018-02 is effective for all entities for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. Early adoption is permitted, including adoption in any interim period. The Company is evaluating the impact of the adoption of this standard on its financial statements and disclosures.

In March 2018, the FASB issued ASU 2018-05, Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118 (“ASU 2018-05”). This ASU allows companies, for one year following the enactment date, to consider the impact of the Tax Act as “provisional” when a company can make a reasonable estimate but does not have the necessary information available, prepared or analyzed in reasonable detail to finalize its accounting for the impact of the Tax Act. A company may need to reflect adjustments to its provisional amounts upon obtaining, preparing or analyzing additional information about facts and circumstances that existed at the period of enactment. The Company has adopted this standard on its financial statements and disclosures. Provisional amounts are identified in Note 7 of our Consolidated Financial Statements.

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3. Comprehensive Income (Loss)

Comprehensive income (loss), which is reported in the accompanying consolidated statements of equity, consists of net income (loss) and other gains and losses affecting equity that, under U.S. GAAP, are excluded from net income (loss). For the Company, the components of other comprehensive income (loss) primarily consist of foreign currency translation gains and losses and minimum pension liabilities. The following summary sets forth the changes in the components of accumulated other comprehensive loss, net of related taxes of less than $1 million:

	Foreign Currency Translation Loss (a)	Minimum Pension Liability Adjustment	Deferred Losses On Derivative Financial Instruments	Accumulated Other Comprehensive Loss, net
	(in millions)			
Balance at September 30, 2017	$ (171)	$ (10)	$ —	$ (181)
Other comprehensive income	(13)	—	(1)	(14)
Amounts reclassified from accumulated other comprehensive income	—	—	—	—
Balance at June 30, 2018	$ (184)	$ (10)	$ (1)	$ (195)

(a) Includes historical foreign currency translation related to certain intra-entity transactions.

4. Goodwill and Intangible Assets

Goodwill

The following analysis details the changes in goodwill for each reportable segment:

	Recorded Music	Music Publishing	Total
	(in millions)		
Balance at September 30, 2017	$ 1,221	$ 464	$ 1,685
Acquisitions	10	—	10
Divestitures	—	—	—
Other adjustments (a)	(9)	—	(9)
Balance at June 30, 2018	$ 1,222	$ 464	$ 1,686

(a) Other adjustments during the nine months ended June 30, 2018 represent foreign currency movements.

The Company performs its annual goodwill impairment test in accordance with ASC 350, Intangibles—Goodwill and other (“ASC 350”) during the fourth quarter of each fiscal year as of July 1. The Company may conduct an earlier review if events or circumstances occur that would suggest the carrying value of the Company’s goodwill may not be recoverable. No indicators of impairment were identified during the current period that required the Company to perform an interim assessment or recoverability test.

At June 30, 2018 and September 30, 2017, the goodwill and intangible assets balances presented include the preliminary purchase accounting allocation resulting from the acquisition of Spinnin’ Records on September 7, 2017. The acquisition of Spinnin’ Records was accounted for as a business combination under ASC 805, which requires the acquisition method of accounting. At September 30, 2017, the Company performed a preliminary purchase allocation under the acquisition method of accounting, which is subject to revision based on final determinations of fair value and allocations of purchase price to the identifiable assets and liabilities acquired. At June 30, 2018, the Company updated the preliminary allocation recorded at September 30, 2017 based on a revised fair market valuation of certain intangible assets. The updated preliminary allocation resulted in an increase in goodwill of $10 million, a decrease in intangible assets of $13 million, and a decrease in deferred tax liabilities of $3 million during the quarter. The purchase price is subject to revision based on final determinations of fair value and allocations of purchase price to the identifiable assets and liabilities acquired.

Intangible Assets

Intangible assets consist of the following:

	Weighted Average Useful Life	June 30, 2018	September 30, 2017
		(in millions)	
Intangible assets subject to amortization:			
Recorded music catalog	10 years	$869	$ 898
Music publishing copyrights	27 years	1,537	1,534
Artist and songwriter contracts	13 years	863	904
Trademarks	6 years	14	14
Other intangible assets	7 years	18	10
Total gross intangible asset subject to amortization		3,301	3,360
Accumulated amortization		(1,417)	(1,270)
Total net intangible assets subject to amortization		1,884	2,090
Intangible assets not subject to amortization:			
Trademarks and tradenames	Indefinite	146	117
Total net intangible assets		$2,030	$ 2,207

5. Debt

Debt Capitalization

Long-term debt consists of the following:

	June 30, 2018	September 30, 2017
	(in millions)	
Revolving Credit Facility—Acquisition Corp. (a)	$—	$ —
Senior Term Loan Facility due 2023—Acquisition Corp. (b)	1,309	990
5.625% Senior Secured Notes due 2022—Acquisition Corp. (c)	246	246
5.00% Senior Secured Notes due 2023—Acquisition Corp. (d)	297	297
4.125% Senior Secured Notes due 2024— Acquisition Corp. (e)	395	402
4.875% Senior Secured Notes due 2024— Acquisition Corp. (f)	247	246
6.75% Senior Notes due 2022—Acquisition Corp. (g)	—	630
5.50% Senior Notes due 2026—Acquisition Corp. (h)	320	—
Total debt (i)	$2,814	$ 2,811

(a) Reflects $180 million and $150 million of commitments under the Revolving Credit Facility at June 30, 2018 and September 30, 2017, respectively, less letters of credit outstanding of approximately $12 million at both June 30, 2018 and September 30, 2017. There were no loans outstanding under the Revolving Credit Facility at June 30, 2018 or September 30, 2017.
(b) Principal amount of $1.326 billion and $1.006 billion less unamortized discount of $4 million and $6 million and unamortized deferred financing costs of $13 million and $10 million at June 30, 2018 and September 30, 2017, respectively.
(c) Principal amount of $248 million less unamortized deferred financing costs of $2 million at both June 30, 2018 and September 30, 2017.
(d) Principal amount of $300 million less unamortized deferred financing costs of $3 million at both June 30, 2018 and September 30, 2017.
(e) Face amount of €345 million. Above amounts represent the dollar equivalent of such notes at June 30, 2018 and September 30, 2017. Principal amount of $399 million and $407 million at June 30, 2018 and September 30, 2017, respectively, less unamortized deferred financing costs of $4 million and $5 million at June 30, 2018 and September 30, 2017, respectively.
(f) Principal amount of $250 million at both June 30, 2018 and September 30, 2017 less unamortized deferred financing costs of $3 million and $4 million at June 30, 2018 and September 30, 2017, respectively.
(g) Principal amount of $635 million less unamortized deferred financing costs of $5 million at September 30, 2017.
(h) Principal amount of $325 million less unamortized deferred financing costs of $5 million at June 30, 2018.
(i) Principal amount of debt of $2.848 billion and $2.846 billion less unamortized discount of $4 million and $6 million and unamortized deferred financing costs of $30 million and $29 million at June 30, 2018 and September 30, 2017, respectively.

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December 2017 Senior Term Loan Credit Agreement Amendment

On December 6, 2017, Acquisition Corp. entered into an amendment (the "December 2017 Senior Term Loan Credit Agreement Amendment") to the Senior Term Loan Credit Agreement, dated November 1, 2012, among Acquisition Corp., the guarantors party thereto, the lenders party thereto and Credit Suisse AG, as administrative agent, governing Acquisition Corp.'s senior secured term loan facility with Credit Suisse AG, as administrative agent, and the other financial institutions and lenders from time to time party thereto, to, among other things, reduce the pricing terms of its outstanding term loans, change certain incurrence thresholds governing the ability to incur debt and liens, change certain EBITDA add-backs and increase the thresholds above which the excess cash flow sweep is triggered. The Company recorded a loss on extinguishment of debt of approximately $1 million, which represented the discount and unamortized deferred financing costs related to the prior tranche of debt of the lenders that was replaced.

New Revolving Credit Agreement

On January 31, 2018, the Company entered into a new revolving credit agreement (the "Revolving Credit Agreement") for its Revolving Credit Facility, and terminated its existing revolving credit agreement (the "Old Revolving Credit Agreement"). The Revolving Credit Agreement differs from the Old Revolving Credit Agreement in that it, among other things, reduces the interest rate margin applicable to the loans, extends the maturity date thereunder, provides for the option to increase the commitments under the Company's then existing revolving credit agreement, provides for greater flexibility to amend and extend the Company's then existing revolving credit agreement and create additional tranches thereunder, provides for greater flexibility over future amendments, increases the springing financial maintenance covenant to 4.75:1.00 and provides that the covenant shall not be tested unless at the end of a fiscal quarter the outstanding amount of loans and drawings under letters of credit which have not been reimbursed exceeds $54 million and aligns the other negative covenants with those of the Senior Term Loan Credit Agreement. References to "Revolving Credit Facility" below in this Note 5 are to our new revolving credit facility.

March 2018 Senior Term Loan Credit Agreement Amendment

On March 14, 2018, Acquisition Corp. incurred $320 million of supplemental term loans (the "Supplemental Term Loans") pursuant to an increase supplement (the "March 2018 Senior Term Loan Credit Agreement Supplement") to the Senior Term Loan Credit Agreement, dated November 1, 2012, among Acquisition Corp., the guarantors party thereto, the lenders party thereto and Credit Suisse AG, as administrative agent, governing Acquisition Corp.'s senior secured term loan facility with Credit Suisse AG, as administrative agent, and the other financial institutions and lenders from time to time party thereto (as amended, the "Senior Term Loan Credit Agreement"). The principal amount outstanding under the Senior Term Loan Credit Agreement including the Supplemental Term Loans is $1.326 billion.

Notes Offering

On March 14, 2018, Acquisition Corp. issued $325 million in aggregate principal amount of its 5.50% Senior Notes due 2026. Acquisition Corp. used the net proceeds to pay the consideration in the tender offer for its 6.75% Senior Notes due 2022 (the "6.75% Senior Notes") and to redeem the remaining 6.75% Senior Notes as described below.

Tender Offer and Notes Redemption

On March 14, 2018, Acquisition Corp. accepted for purchase in connection with the tender offer for the 6.75% Senior Notes that had been validly tendered and not validly withdrawn at or prior to 5:00 p.m., New York City time on March 13, 2018 (the "Expiration Time") thereby reducing the aggregate principal amount of the 6.75% Senior Notes by $523 million. Acquisition Corp. then issued a notice of redemption on March 14, 2018 with respect to the remaining $112 million of 6.75% Senior Notes outstanding that were not accepted for payment pursuant to the tender offer.

Following payment of the 6.75% Senior Notes tendered at or prior to the Expiration Time, Acquisition Corp. deposited with the Trustee funds of $119 million to satisfy all obligations under the applicable indenture governing the 6.75% Senior Notes, including call premiums and interest through the date of redemption on April 15, 2018, for the remaining 6.75% Senior Notes not accepted for purchase in the tender offer. On April 15, 2018, Acquisition Corp. redeemed the remaining outstanding 6.75% Senior Notes. The Company recorded a loss on extinguishment of debt in connection with the tender offer of approximately $23 million as a result of the partial debt redemption, which represents the premium paid on early redemption and unamortized deferred financing costs in March 2018. The Company incurred an additional loss on extinguishment of approximately $5 million in April 2018 related to the redemption on the remaining 6.75% Senior Notes, which represents the premium paid on early redemption and unamortized deferred financing costs.

June 2018 Senior Term Loan Credit Agreement Amendment

On June 7, 2018, Acquisition Corp. entered into an amendment (the “June 2018 Senior Term Loan Credit Agreement Amendment”) to the Senior Term Loan Credit Agreement, dated November 1, 2012, among Acquisition Corp., the guarantors party thereto, the lenders party thereto and Credit Suisse AG, as administrative agent, governing Acquisition Corp.’s senior secured term loan facility with Credit Suisse AG, as administrative agent, and the other financial institutions and lenders from time to time party thereto, to, among other things, reduce the pricing terms of its outstanding term loans, change certain incurrence thresholds governing the ability to incur debt and liens and exclude from the definition of “Senior Secured Indebtedness” certain liens that have junior lien priority on the collateral in relation to the outstanding term loans and the relevant guarantees, as applicable. The Company recorded a loss on extinguishment of debt of approximately $2 million, which represented the discount and unamortized deferred financing costs related to the prior tranche of debt of the lenders that was replaced.

Interest Rates

The loans under the Revolving Credit Facility bear interest at Acquisition Corp.’s election at a rate equal to (i) the rate for deposits in the borrowing currency in the London interbank market (adjusted for maximum reserves) for the applicable interest period (“Revolving LIBOR”) subject to a zero floor, plus 1.75% per annum, or (ii) the base rate, which is the highest of (x) the corporate base rate established by the administrative agent from time to time, (y) 0.50% in excess of the overnight federal funds rate and (z) the one-month Revolving LIBOR plus 1.0% per annum, plus, in each case, 0.75% per annum. If there is a payment default at any time, then the interest rate applicable to overdue principal will be the rate otherwise applicable to such loan plus 2.0% per annum. Default interest will also be payable on other overdue amounts at a rate of 2.0% per annum above the amount that would apply to an alternative base rate loan.

The loans under the Senior Term Loan Facility bear interest at Acquisition Corp.’s election at a rate equal to (i) the rate for deposits in U.S. dollars in the London interbank market (adjusted for maximum reserves) for the applicable interest period (“Term Loan LIBOR”) subject to a zero floor, plus 2.125% per annum, or (ii) the base rate, which is the highest of (x) the corporate base rate established by the administrative agent as its prime rate in effect at its principal office in New York City from time to time, (y) 0.50% in excess of the overnight federal funds rate and (z) one-month Term Loan LIBOR, plus 1.00% per annum, plus, in each case, 1.125% per annum. If there is a payment default at any time, then the interest rate applicable to overdue principal and interest will be the rate otherwise applicable to such loan plus 2.0% per annum. Default interest will also be payable on other overdue amounts at a rate of 2.0% per annum above the amount that would apply to an alternative base rate loan.

The Company has entered into, and in the future may enter into, interest rate swaps to manage interest rate risk.

Maturity of Senior Term Loan Facility

The loans outstanding under the Senior Term Loan Facility mature on November 1, 2023.

Maturity of Revolving Credit Facility

The maturity date of the Revolving Credit Facility is January 31, 2023.

Maturities of Senior Notes and Senior Secured Notes

As of June 30, 2018, there are no scheduled maturities of notes until 2022, when $248 million is scheduled to mature. Thereafter, $1.274 billion is scheduled to mature.

Interest Expense, net

Total interest expense, net, was $33 million and $36 million for the three months ended June 30, 2018 and June 30, 2017, respectively. Total interest expense, net, was $105 million and $112 million for the nine months ended June 30, 2018 and June 30, 2017, respectively. The weighted-average interest rate of the Company’s total debt was 4.7% at June 30, 2018 and 4.9% at September 30, 2017 and June 30, 2017.

6. Commitments and Contingencies

Pricing of Digital Music Downloads

On December 20, 2005 and February 3, 2006, the Attorney General of the State of New York served the Company with requests for information in connection with an industry-wide investigation as to the pricing of digital music downloads. On February 28, 2006, the Antitrust Division of the U.S. Department of Justice served us with a Civil Investigative Demand, also seeking information relating to the pricing of digitally downloaded music. Both investigations were ultimately closed, but subsequent to the announcements of the investigations, more than thirty putative class action lawsuits were filed concerning the pricing of digital music downloads. The lawsuits were consolidated in the Southern District of New York. The consolidated amended complaint, filed on April 13, 2007, alleges conspiracy among record companies to delay the release of their content for digital distribution, inflate their pricing of CDs and fix prices for digital downloads. The complaint seeks unspecified compensatory, statutory and treble damages. On October 9, 2008, the District Court issued an order dismissing the case as to all defendants, including us. However, on January 13, 2010, the Second Circuit vacated the judgment of the District Court and remanded the case for further proceedings and on January 10, 2011, the U.S. Supreme Court denied the defendants' petition for Certiorari.

Upon remand to the District Court, all defendants, including the Company, filed a renewed motion to dismiss challenging, among other things, plaintiffs' state law claims and standing to bring certain claims. The renewed motion was based mainly on arguments made in defendants' original motion to dismiss, but not addressed by the District Court. On July 18, 2011, the District Court granted defendants' motion in part, and denied it in part. Notably, all claims on behalf of the CD-purchaser class were dismissed with prejudice. However, a wide variety of state and federal claims remain for the class of Internet download purchasers. On March 19, 2014, plaintiffs filed a motion for class certification. Plaintiffs filed an operative consolidated amended complaint on September 25, 2015. The Company filed its answer to the fourth amended complaint on October 9, 2015, and filed an amended answer on November 3, 2015. A mediation took place on February 22, 2016, but the parties were unable to reach a resolution. On July 18, 2017, the District Court denied plaintiffs' motion for class certification. On August 1, 2017, plaintiffs filed a petition with the Second Circuit seeking permission to appeal the district court's order denying class certification. On August 11, 2017, defendants filed their opposition to plaintiffs' petition. On December 8, 2017, the Second Circuit denied plaintiffs' request for leave to appeal the District Court's order denying their motion for class certification. On May 8, 2018, the parties filed a joint stipulation to voluntarily dismiss the case with prejudice, and on May 15, 2018, the District Court dismissed the case.

Sirius XM

On September 11, 2013, the Company joined with Capitol Records, LLC, Sony Music Entertainment, UMG Recordings, Inc. and ABKCO Music & Records, Inc. in a lawsuit brought in California Superior Court against Sirius XM Radio Inc., alleging copyright infringement for Sirius XM's use of pre-1972 sound recordings under California law. A nation-wide settlement was reached on June 17, 2015 pursuant to which Sirius XM paid the plaintiffs, in the aggregate, $210 million on July 29, 2015 and the plaintiffs dismissed their lawsuit with prejudice. The settlement resolves all past claims as to Sirius XM's use of pre-1972 recordings owned or controlled by the plaintiffs and enables Sirius XM, without any additional payment, to reproduce, perform and broadcast such recordings in the United States through December 31, 2017. The allocation of the settlement proceeds among the plaintiffs was determined and the settlement proceeds were distributed accordingly. This resulted in a cash distribution to the Company of $33 million of which $28 million was recognized in revenue during the 2016 fiscal year and $4 million was recognized in revenue during the 2017 fiscal year. The balance of $1 million was recognized in the first quarter of the 2018 fiscal year. The Company is sharing its allocation of the settlement proceeds with its artists on the same basis as statutory revenue from Sirius XM is shared, i.e., the artist share of our allocation will be paid to artists by SoundExchange.

As part of the settlement, plaintiffs agreed to negotiate in good faith to grant Sirius XM a license to publicly perform the plaintiffs' pre-1972 sound recordings for the five-year period running from January 1, 2018 to December 31, 2022. Pursuant to the settlement, if the parties are unable to reach an agreement on license terms, the royalty rate for each license will be determined by binding arbitration on a willing buyer/willing seller standard. On December 21, 2017, Sirius XM commenced a single arbitration against all of the plaintiffs in California through JAMS to determine the rate for the five-year period. On May 1, 2018, the Company filed a lawsuit against Sirius XM in New York state court to stay the California arbitration and to compel a separate arbitration in New York solely between Sirius XM and the Company.

Other Matters

In addition to the matters discussed above, the Company is involved in various litigation and regulatory proceedings arising in the normal course of business. Where it is determined, in consultation with counsel based on litigation and settlement risks, that a loss is probable and estimable in a given matter, the Company establishes an accrual. In the currently pending proceedings, the amount of accrual is not material. An estimate of the reasonably possible loss or range of loss in excess of the amounts already accrued cannot be made at this time due to various factors typical in contested proceedings, including (1) the results of ongoing discovery; (2) uncertain damage theories and demands; (3) a less than complete factual record; (4) uncertainty concerning legal theories and their resolution by courts or regulators; and (5) the unpredictable nature of the opposing party and its demands. However, the Company cannot predict with certainty the outcome of any litigation or the potential for future litigation. As such, the Company continuously monitors these proceedings as they develop and adjusts any accrual or disclosure as needed. Regardless of the outcome, litigation could have an adverse impact on the Company, including the Company's brand value, because of defense costs, diversion of management resources and other factors and it could have a material effect on the Company's results of operations for a given reporting period.

7. Income Taxes

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act ("Tax Act"). The Tax Act contains significant revisions to U.S. corporate income tax provisions, including, but not limited to, a reduction of the U.S. corporate statutory tax rate from 35% to 21%, a one-time transition tax on accumulated foreign earnings, an income inclusion of global intangible low-taxed income ("GILTI"), and a new minimum tax, base erosion anti-abuse tax ("BEAT"). In accordance with ASC 740, the Company recorded the effects of the Tax Act during the three months ended December 31, 2017, the period of enactment.

The reduction in U.S. corporate statutory tax rate from 35% to 21% is effective January 1, 2018. The Tax Act requires companies with a fiscal year that begins before and ends after the effective date of the rate change to calculate a blended tax rate based on the pro rata number of days in the fiscal year before and after the effective date. As a result, for the fiscal year ending September 30, 2018, the Company's statutory income tax rate will be 24.5%. For the fiscal year ending September 30, 2019, the Company will be subject to the U.S. corporate statutory tax rate of 21%.

The reduction in the U.S. corporate statutory tax rate requires the Company to adjust its U.S. deferred tax assets and liabilities using the newly enacted tax rate of 21%. As a result, the Company initially recorded a provisional U.S. income tax expense of $27 million for the reduction of its net U.S. deferred tax assets as a discrete item for the three months ended December 31, 2017. Since the Company has a fiscal year ending September 30, 2018, and has applied an annual effective tax rate in calculating its income tax provision for the three and nine months ended June 30, 2018, the Company's provisional U.S. income tax expense from the reduction in the U.S. corporate statutory tax rate was revised to $17 million as of June 30, 2018. The impact of the U.S. corporate statutory tax rate change will not be finalized until September 30, 2018. Furthermore, the Company has a provisional deferred tax liability of approximately $4 million, after the impact of the newly enacted tax rate, associated with unremitted earnings due to the uncertainty of the treatment of future distributions under the Tax Act.

The one-time transition tax on accumulated foreign earnings ("Transition Tax") would be imposed at a rate of 15.5% for cash and equivalents and 8% for illiquid assets. The Company reasonably estimates that there is no income tax impact related to the Transition Tax and recorded no income tax liability for the three and nine months ended June 30, 2018 due to an estimated overall deficit in accumulated foreign earnings. This estimate is provisional since the Company has not obtained and analyzed information necessary to finalize its accounting for the impact of the Transition Tax. The final impacts of the Transition Tax may differ from the estimate due to changes in interpretations of the Tax Act and updates or changes to the information that the Company has used to estimate the transition impact, including, but not limited to, the impacts from changes to foreign earnings estimates, foreign exchange rates, and cash positions of foreign subsidiaries.

GILTI and BEAT are effective for the Company for the fiscal year ended September 30, 2019. For the period of enactment, the Company has elected not to adjust its deferred taxes for the impact of GILTI and will consider the impact of GILTI in the specific period in which it occurs.

For the three and nine months ended June 30, 2018, the Company recorded an income tax expense of $61 million and $132 million, respectively. The income tax expense for the three months ended June 30, 2018 is lower than the expected tax at the blended statutory tax rate of 24.5% primarily due to recognition of a deferred tax asset related to a prior year intergroup transfer, $9 million change in provisional amount for the U.S. income tax reform and a release of uncertain tax positions partially offset by state tax expense. The income tax expense for the nine months ended June 30, 2018 is greater than the expected income tax expense at the blended statutory tax rate of 24.5% primarily due to a U.S. income tax expense of $17 million arising from a reduction in net U.S. deferred tax assets due to the change in the U.S. statutory tax rate, state tax expense, foreign income taxed at rates higher than the U.S. statutory tax rate, income withholding taxes, foreign losses with no tax benefit reduced by recognition of the deferred tax asset related to a prior year intergroup transfer and a release in uncertain tax positions.

For the three and nine months ended June 30, 2017, the Company recorded an income tax benefit of $152 million and $132 million, respectively. The tax benefit for the three months ended June 30, 2017 is lower than the expected tax at the statutory tax rate of 35% primarily due to a U.S. tax benefit of $128 million for the reversal of a significant portion of our U.S. deferred tax valuation allowance and a U.S. tax benefit of $51 million related to foreign currency losses on intra-entity loans, partially offset by income withholding taxes, foreign losses with no tax benefit and an increase in uncertain tax positions. The tax benefit for the nine months ended June 30, 2017 is lower than the expected tax at the statutory tax rate of 35% primarily due to a U.S. tax benefit of $128 million for the reversal of a significant portion of our U.S. deferred tax valuation allowance and a U.S. tax benefit of $60 million related to foreign currency losses on intra-entity loans, partially offset by income withholding taxes, foreign losses with no tax benefit and an increase in uncertain tax positions.

The Company has determined that it is reasonably possible that the gross unrecognized tax benefits as of June 30, 2018 could decrease by up to approximately $1 million related to various ongoing audits and settlement discussions in various foreign jurisdictions during the next twelve months.

8. Derivative Financial Instruments

The Company uses derivative financial instruments, primarily foreign currency forward exchange contracts and interest rate swaps, for the purposes of managing foreign currency exchange rate risk and interest rate risk on expected future cash flows. However, the Company may choose not to hedge certain exposures for a variety of reasons including, but not limited to, accounting considerations and the prohibitive economic cost of hedging particular exposures. There can be no assurance the hedges will offset more than a portion of the financial impact resulting from movements in foreign currency exchange or interest rates.

The Company enters into foreign currency forward exchange contracts primarily to hedge the risk that unremitted or future royalties and license fees owed to its domestic companies for the sale, or anticipated sale, of U.S.-copyrighted products abroad may be adversely affected by changes in foreign currency exchange rates. The Company focuses on managing the level of exposure to the risk of foreign currency exchange rate fluctuations on its major currencies, which include the Euro, British pound sterling, Japanese yen, Canadian dollar, Swedish krona and Australian dollar. The foreign currency forward exchange contracts related to royalties are designated and qualify as cash flow hedges under the criteria prescribed in ASC 815, Derivatives and Hedging. The Company records these contracts at fair value on its balance sheet and gains or losses on these contracts are deferred in equity (as a component of comprehensive loss). These deferred gains and losses are recognized in income in the period in which the related royalties and license fees being hedged are received and recognized in income. However, to the extent that any of these contracts are not considered to be perfectly effective in offsetting the change in the value of the royalties and license fees being hedged, any changes in fair value relating to the ineffective portion of these contracts are immediately recognized in the statement of operations.

The Company may at times choose to hedge foreign currency risk associated with financing transactions such as third-party debt and other balance sheet items. The foreign currency forward exchange contracts related to balance sheet items denominated in foreign currency are reviewed on a contract-by-contract basis and are designated accordingly. If these foreign currency forward exchange contracts do not qualify for hedge accounting, then the Company records these contracts at fair value on its balance sheet and the related gains and losses are immediately recognized in the statement of operations where there is an equal and offsetting entry related to the underlying exposure.

The Company has entered into, and in the future may enter into, interest rate swaps to manage interest rate risk. These instruments may offset a portion of changes in income or expense, or changes in fair value of the Company's term debt. The interest rate swap instruments are designated and qualify as cash flow hedges under the criteria prescribed in ASC 815, Derivatives and Hedging. The Company records these contracts at fair value on its balance sheet and gains or losses on these contracts are deferred in equity (as a component of comprehensive loss).

The fair value of foreign currency forward exchange contracts is determined by using observable market transactions of spot and forward rates (i.e., Level 2 inputs) which is discussed further in Note 11. Additionally, netting provisions are provided for in existing International Swap and Derivative Association Inc. agreements in situations where the Company executes multiple contracts with the same counterparty. As a result, net assets or liabilities resulting from foreign exchange derivatives subject to these netting agreements are classified within other current assets or other current liabilities in the Company's consolidated balance sheets.

The Company's hedged interest rate transactions as of June 30, 2018 are expected to be recognized within 5 years. The fair value of interest rate swaps is based on dealer quotes of market rates (i.e., Level 2 inputs) which is discussed further in Note 11. Interest income or expense related to interest rate swaps is recognized in interest income, net in the same period as the related expense is recognized. The ineffective portions of interest rate swaps is recognized in other income/(expense), net in the period measured.

The Company monitors its positions with, and the credit quality of, the financial institutions that are party to any of its financial transactions.

As of June 30, 2018, the Company had outstanding hedge contracts for the sale of $109 million and the purchase of $64 million of foreign currencies at fixed rates that will be settled by September 2018. As of June 30, 2018, the Company had $1 million of unrealized deferred losses in comprehensive income related to foreign exchange hedging. As of September 30, 2017, the Company had no outstanding hedge contracts and no deferred gains or losses in comprehensive loss related to foreign exchange hedging.

As of June 30, 2018, the Company had outstanding $320 million in pay-fixed receive-variable interest rate swaps with $2 million of unrealized deferred gains in comprehensive income related to the interest rate swap. As of September 30, 2017, the Company had no outstanding interest rate swaps and no deferred gains or losses in comprehensive income or losses related to interest rate swaps.

The pre-tax losses of the Company's foreign exchange forward exchange contracts designated as cash flow hedges recorded in other comprehensive income and the Consolidated Statement of Comprehensive Income during the three months ended June 30, 2018 and September 30, 2017 were $3 million and $0 million, respectively.

The pre-tax gains of the Company's derivative interest rate swaps designated as cash flow hedges recorded in other comprehensive income and the Consolidated Statement of Comprehensive Income during the three months ended June 30, 2018 and September 30, 2017 were $3 million and $0 million, respectively.

The following is a summary of amounts recorded in the Consolidated Balance Sheet pertaining to the Company's designated cash flows hedges at June 30, 2018 and September 30, 2017:

	June 30, 2018 (a)	September 30, 2017
	(in millions)	
Other current assets	$ 3	$ —
Other current liabilities	1	—
Other noncurrent assets	2	—
Other noncurrent liabilities	—	—

(a) $5 million and $3 million of foreign exchange derivative contracts in asset and liability positions, respectively, and $2 million of interest rate swap in an asset position including non-designated cash flow hedges.

9. Segment Information

As discussed more fully in Note 1, based on the nature of its products and services, the Company classifies its business interests into two fundamental operations: Recorded Music and Music Publishing, which also represent reportable segments of the Company. Information as to each of these operations is set forth below. The Company evaluates performance based on several factors, of which the primary financial measure is operating income (loss) before non-cash depreciation of tangible assets and non-cash amortization of intangible assets (“OIBDA”). The Company has supplemented its analysis of OIBDA results by segment with an analysis of operating income (loss) by segment.

The accounting policies of the Company's business segments are the same as those described in the summary of significant accounting policies included elsewhere herein. The Company accounts for intersegment sales at fair value as if the sales were to third parties. While intercompany transactions are treated like third-party transactions to determine segment performance, the revenues (and corresponding expenses recognized by the segment that is counterparty to the transaction) are eliminated in consolidation, and therefore, do not themselves impact consolidated results.

Three Months Ended	Recorded Music (in millions)	Music Publishing	Corporate expenses and eliminations	Total
June 30, 2018				
Revenues	$802	$ 159	$ (3)	$958
Operating income (loss)	67	5	(44)	28
Amortization of intangible assets	39	17	—	56
Depreciation of property, plant and equipment	9	2	4	15
OIBDA	115	24	(40)	99
June 30, 2017				
Revenues	$770	$ 150	$ (3)	$917
Operating income (loss)	77	6	(32)	51
Amortization of intangible assets	35	16	—	51
Depreciation of property, plant and equipment	8	1	4	13
OIBDA	120	23	(28)	115

Nine Months Ended	Recorded Music (in millions)	Music Publishing	Corporate expenses and eliminations	Total
June 30, 2018				
Revenues	$2,497	$ 476	$ (7)	$2,966
Operating income (loss)	276	45	(120)	201
Amortization of intangible assets	113	51	—	164
Depreciation of property, plant and equipment	26	5	10	41
OIBDA	415	101	(110)	406
June 30, 2017				
Revenues	$2,253	$ 419	$ (13)	$2,659
Operating income (loss)	269	45	(91)	223
Amortization of intangible assets	104	48	—	152
Depreciation of property, plant and equipment	24	4	10	38
OIBDA	397	97	(81)	413

10. Additional Financial Information

Cash Interest and Taxes

The Company made interest payments of approximately $41 million and $56 million during the three months ended June 30, 2018 and June 30, 2017, respectively. The Company made interest payments of approximately $126 million and $120 million during the nine months ended June 30, 2018 and June 30, 2017, respectively. The Company paid approximately $16 million of income and withholding taxes, partially offset by $1 million of refunds, during the three months ended June 30, 2018 and paid approximately $8 million of income and withholding taxes with no offsetting refunds during the three months ended June 30, 2017. The Company paid approximately $35 million of income and withholding taxes, partially offset by $2 million of refunds, during the nine months ended June 30, 2018 and paid approximately $30 million of income and withholding taxes, partially offset by $3 million of refunds during the nine months ended June 30, 2017.

Special Cash Dividend

On December 2, 2016, the Company’s Board of Directors approved a special cash dividend of $54 million, which was paid on January 3, 2017 to stockholders of record as of December 30, 2016.

On June 5, 2017, the Company's Board of Directors approved a special cash dividend of $30 million, which was paid on July 31, 2017 to stockholders of record as of June 30, 2017.

On January 8, 2018, the Company's Board of Directors approved a special cash dividend of $125 million, which was paid on January 12, 2018 to stockholders of record as of January 11, 2018.

On May 7, 2018, the Company's Board of Directors approved a special cash dividend of $300 million, which was paid on May 11, 2018 to stockholders of record as of May 7, 2018.

Spotify Share Sale

During the three months ended June 30, 2018, the Company sold all of its shares of common stock in Spotify Technology S.A. ("Spotify") for cash proceeds of $504 million. In February 2016, the Company publicly announced that it would pay royalties in connection with these proceeds. The sale of shares resulted in an estimated pre-tax gain, net of the estimated royalty expense and other related costs, of $378 million, which has been recorded as other income (expense) in the quarter. As of June 30, 2018, the estimated royalty expense and other related costs have been accrued, but not yet paid. The processing of the royalty expense will result in advance recoveries of previously expensed royalty advances. The Company has estimated the advance recoveries to be approximately $16 million, and has recorded these advance recoveries as a credit within operating expense in the three and nine months ended June 30, 2018. The Company also recorded estimated tax expense of $77 million associated with the net income on the sale of shares in the quarter.

Additionally, the cash proceeds received in connection with the sale of shares have been reflected as an investing activity on the statement of cash flows in the quarter within proceeds from the sale of investments.

11. Fair Value Measurements

ASC 820, Fair Value Measurement, defines fair value as the price that would be received upon sale of an asset or paid upon transfer of a liability in an orderly transaction between market participants at the measurement date and in the principal or most advantageous market for that asset or liability. The fair value should be calculated based on assumptions that market participants would use in pricing the asset or liability, not on assumptions specific to the entity.

In addition to defining fair value, ASC 820 expands the disclosure requirements around fair value and establishes a fair value hierarchy for valuation inputs. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels which is determined by the lowest level input that is significant to the fair value measurement in its entirety. These levels are:

- Level 1—inputs are based upon unadjusted quoted prices for identical instruments traded in active markets.
- Level 2—inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
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Level 3—inputs are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques that include option pricing models, discounted cash flow models and similar techniques.

In accordance with the fair value hierarchy, described above, the following table shows the fair value of the Company's financial instruments that are required to be measured at fair value as of June 30, 2018 and September 30, 2017.

	Fair Value Measurements as of June 30, 2018			
	(Level 1)	(Level 2)	(Level 3)	Total
	(in millions)			
Other Current Assets:				
Foreign Currency Forward Exchange Contracts (a)	$ —	$ 3	$ —	$ 3
Other Current Liabilities:				
Foreign Currency Forward Exchange Contracts (a)	—	(1)	—	(1)
Contractual Obligations (b)	—	—	—	—
Other Non-Current Assets:				
Interest Rate Swap (c)	—	2	—	2
Other Non-Current Liabilities:				
Contractual Obligations (b)	—	—	(6)	(6)
Interest Rate Swap (c)	—	—	—	—
Total	$ —	$ 4	$ (6)	$ (2)

	Fair Value Measurements as of September 30, 2017			
	(Level 1)	(Level 2)	(Level 3)	Total
	(in millions)			
Other Current Liabilities:				
Contractual Obligations (b)	—	—	—	—
Other Non-Current Liabilities:				
Contractual Obligations (b)	—	—	(5)	(5)
Total	$ —	$ —	$ (5)	$ (5)

(a) The fair value of foreign currency forward exchange contracts is based on dealer quotes of market forward rates and reflects the amount that the Company would receive or pay at their maturity dates for contracts involving the same currencies and maturity dates.

(b) This represents purchase obligations and contingent consideration related to the Company's various acquisitions. This is based on a discounted cash flow approach and it is adjusted to fair value on a recurring basis and any adjustments are included as a component of operating income in the statement of operations. These amounts were mainly calculated using unobservable inputs such as future earnings performance of the Company's various acquisitions and the expected timing of the payment.

(c) The fair value of the interest rate swap is based on dealer quotes of market forward rates and reflects the amount that the Company would receive or pay as of June 30, 2018 for contracts involving the same attributes and maturity dates.

The following table reconciles the beginning and ending balances of net assets and liabilities classified as Level 3:

	Total (in millions)
Balance at September 30, 2017	(5)
Additions	(1)
Reductions	—
Payments	—
Balance at June 30, 2018	$ (6)

The majority of the Company's non-financial instruments, which include goodwill, intangible assets, inventories, and property, plant, and equipment, are not required to be re-measured to fair value on a recurring basis. These assets are evaluated for impairment if certain triggering events occur. If such evaluation indicates that impairment exists, the asset is written down to its fair value. In addition, an impairment analysis is performed at least annually for goodwill and indefinite-lived intangible assets.

Fair Value of Debt

Based on the level of interest rates prevailing at June 30, 2018, the fair value of the Company’s debt was $2.872 billion. Based on the level of interest rates prevailing at September 30, 2017, the fair value of the Company’s debt was $2.936 billion. The fair value of the Company’s debt instruments are determined using quoted market prices from less active markets or by using quoted market prices for instruments with identical terms and maturities; both approaches are considered a Level 2 measurement.

12. Subsequent Events

Special Cash Dividend

On August 7, 2018, our Board of Directors declared a special cash dividend of $500 million to be paid on August 10, 2018 to stockholders of record as of August 7, 2018.

WARNER MUSIC GROUP CORP.

Supplementary Information

Consolidating Financial Statements

The Company is the direct parent of Holdings, which is the direct parent of Acquisition Corp. Acquisition Corp. has issued and outstanding the 5.625% Senior Secured Notes due 2022, the 5.00% Senior Secured Notes due 2023, the 4.125% Senior Secured Notes due 2024, the 4.875% Senior Secured Notes due 2024, and the 5.50% Senior Notes due 2026 (together, the “Acquisition Corp. Notes”).

The Acquisition Corp. Notes are guaranteed by the Company and, in addition, are guaranteed by all of Acquisition Corp.’s domestic wholly-owned subsidiaries. The secured notes are guaranteed on a senior secured basis and the unsecured notes are guaranteed on an unsecured senior basis. The Company’s guarantee of the Acquisition Corp. Notes is full and unconditional. The guarantee of the Acquisition Corp. Notes by Acquisition Corp.’s domestic, wholly-owned subsidiaries are full, unconditional and joint and several. The following condensed consolidating financial statements are also presented for the information of the holders of the Acquisition Corp. Notes and present the results of operations, financial position and cash flows of (i) Acquisition Corp., which is the issuer of the Acquisition Corp. Notes, (ii) the guarantor subsidiaries of Acquisition Corp., (iii) the non-guarantor subsidiaries of Acquisition Corp. and (iv) the eliminations necessary to arrive at the information for Acquisition Corp. on a consolidated basis. Investments in consolidated subsidiaries are presented under the equity method of accounting. There are no restrictions on Acquisition Corp.’s ability to obtain funds from any of its wholly-owned subsidiaries through dividends, loans or advances.

The Company and Holdings are holding companies that conduct substantially all of their business operations through Acquisition Corp. Accordingly, the ability of the Company and Holdings to obtain funds from their subsidiaries is restricted by the indentures for the Acquisition Corp. Notes and the credit agreements for the Acquisition Corp. Senior Credit Facilities, including the Revolving Credit Facility and Senior Term Loan Facility.

Consolidating Balance Sheet (Unaudited)

June 30, 2018

	WMG Acquisition Corp. (issuer)	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	WMG Acquisition Corp. Consolidated	WMG Holdings Corp.	Warner Music Group Corp.	Eliminations	Warner Music Group Corp. Consolidated
	(in millions)								
Assets:									
Current assets:									
Cash and equivalents	$—	$ 554	$ 351	$ —	$ 905	$ —	$ —	$ —	$ 905
Accounts receivable, net	—	251	193	—	444	—	—	—	444
Inventories	—	17	23	—	40	—	—	—	40
Royalty advances expected to be recouped within one year	—	87	51	—	138	—	—	—	138
Prepaid and other current assets	—	15	43	—	58	—	—	—	58
Total current assets	—	924	661	—	1,585	—	—	—	1,585
Due (to) from parent companies	401	(109)	(292)	—	—	—	—	—	—
Investments in and advances to consolidated subsidiaries	2,599	1,590	—	(4,189)	—	684	684	(1,368)	—
Royalty advances expected to be recouped after one year	—	110	60	—	170	—	—	—	170
Property, plant and equipment, net	—	132	71	—	203	—	—	—	203
Goodwill	—	1,367	319	—	1,686	—	—	—	1,686
Intangible assets subject to amortization, net	—	976	908	—	1,884	—	—	—	1,884
Intangible assets not subject to amortization	—	71	75	—	146	—	—	—	146
Deferred tax assets, net	—	—	8	—	8	—	—	—	8
Other assets	9	61	12	—	82	—	—	—	82
Total assets	$3,009	$ 5,122	$ 1,822	$ (4,189)	$ 5,764	$ 684	$ 684	$ (1,368)	$ 5,764
Liabilities and Deficit:									
Current liabilities:									
Accounts payable	$—	$ 95	$ 73	$ —	$ 168	$ —	$ —	$ —	$ 168
Accrued royalties	—	862	630	—	1,492	—	—	—	1,492
Accrued liabilities	—	180	197	—	377	—	—	—	377

Accrued interest	19	—	—	—	19	—	—	—	19
Deferred revenue	—	171	41	—	212	—	—	—	212
Current portion of long-term debt	—	—	—	—	—	—	—	—	—
Other current liabilities	—	2	17	—	19	—	—	—	19
Total current liabilities	19	1,310	958	—	2,287	—	—	—	2,287
Long-term debt	2,814	—	—	—	2,814	—	—	—	2,814
Deferred tax liabilities, net	—	—	197	—	197	—	—	—	197
Other noncurrent liabilities	1	169	105	—	275	—	—	—	275
Total liabilities	2,834	1,479	1,260	—	5,573	—	—	—	5,573
Total Warner Music Group Corp. equity	175	3,639	550	(4,189)	175	684	684	(1,368)	175
Noncontrolling interest	—	4	12	—	16	—	—	—	16
Total equity	175	3,643	562	(4,189)	191	684	684	(1,368)	191
Total liabilities and equity	$3,009	$ 5,122	$ 1,822	$ (4,189)	$ 5,764	$ 684	$ 684	$ (1,368)	$ 5,764

Consolidating Balance Sheet

September 30, 2017

	WMG Acquisition Corp. (issuer) (in millions)	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	WMG Acquisition Corp. Consolidated	WMG Holdings Corp.	Warner Music Group Corp.	Eliminations	Warner Music Group Corp. Consolidated
Assets:									
Current assets:									
Cash and equivalents	$—	$ 347	$ 300	$ —	$ 647	$ —	$—	$ —	$ 647
Accounts receivable, net	—	214	190	—	404	—	—	—	404
Inventories	—	12	27	—	39	—	—	—	39
Royalty advances expected to be recouped within one year	—	89	52	—	141	—	—	—	141
Prepaid and other current assets	—	15	29	—	44	—	—	—	44
Total current assets	—	677	598	—	1,275	—	—	—	1,275
Due from (to) parent companies	418	96	(514)	—	—	—	—	—	—
Investments in and advances to consolidated subsidiaries	2,721	1,312	—	(4,033)	—	377	377	(754)	—
Royalty advances expected to be recouped after one year	—	109	63	—	172	—	—	—	172
Property, plant and equipment, net	—	139	74	—	213	—	—	—	213
Goodwill	—	1,368	317	—	1,685	—	—	—	1,685
Intangible assets subject to amortization, net	—	1,029	1,061	—	2,090	—	—	—	2,090
Intangible assets not subject to amortization	—	71	46	—	117	—	—	—	117
Deferred tax assets, net	—	89	8	—	97	—	—	—	97
Other assets	7	45	17	—	69	—	—	—	69
Total assets	$3,146	$ 4,935	$ 1,670	$ (4,033)	$ 5,718	$ 377	$ 377	$ (754)	$ 5,718
Liabilities and Deficit:									
Current liabilities:									
Accounts payable	$—	$ 135	$ 73	$ —	$ 208	$ —	$—	$ —	$ 208
Accrued royalties	—	732	531	—	1,263	—	—	—	1,263
Accrued liabilities	—	144	221	—	365	—	—	—	365
Accrued interest	41	—	—	—	41	—	—	—	41
Deferred revenue	—	125	72	—	197	—	—	—	197
Other current liabilities	—	3	23	—	26	—	—	—	26

Total current liabilities	41	1,139	920	—	2,100	—	—	—	2,100
Long-term debt	2,811	—	—	—	2,811	—	—	—	2,811
Deferred tax liabilities, net	—	—	190	—	190	—	—	—	190
Other noncurrent liabilities	1	196	112	—	309	—	—	—	309
Total liabilities	2,853	1,335	1,222	—	5,410	—	—	—	5,410
Total Warner Music Group Corp. equity	293	3,596	437	(4,033)	293	377	377	(754)	293
Noncontrolling interest	—	4	11	—	15	—	—	—	15
Total equity	293	3,600	448	(4,033)	308	377	377	(754)	308
Total liabilities and equity	$3,146	$ 4,935	$ 1,670	$ (4,033)	$ 5,718	$ 377	$ 377	$ (754)	$ 5,718

Consolidating Statement of Operations (Unaudited)

For The Three Months Ended June 30, 2018

	WMG Acquisition Corp. (issuer)	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	WMG Acquisition Corp. Consolidated	WMG Holdings Corp.	Warner Music Group Corp.	Eliminations	Warner Music Group Corp. Consolidated
(in millions)									
Revenues	$—	$ 544	$ 533	$ (119)	$ 958	$ —	$ —	$ —	$ 958
Costs and expenses:									
Cost of revenue	—	(261)	(346)	76	(531)	—	—	—	(531)
Selling, general and administrative expenses	—	(252)	(133)	42	(343)	—	—	—	(343)
Amortization of intangible assets	—	(23)	(33)	—	(56)	—	—	—	(56)
Total costs and expenses	—	(536)	(512)	118	(930)	—	—	—	(930)
Operating income	—	8	21	(1)	28	—	—	—	28
Loss on extinguishment of debt	(7)	—	—	—	(7)	—	—	—	(7)
Interest expense, net	(27)	2	(8)	—	(33)	—	—	—	(33)
Equity gains from equity method investments	39	23	—	(62)	—	320	320	(640)	—
Other expense, net	376	(1)	19	—	394	—	—	—	394
Income before income taxes	381	32	32	(63)	382	320	320	(640)	382
Income tax (expense) benefit	(61)	(62)	7	55	(61)	—	—	—	(61)
Net income (loss)	320	(30)	39	(8)	321	320	320	(640)	321
Less: income attributable to noncontrolling interest	—	—	(1)	—	(1)	—	—	—	(1)
Net income (loss) attributable to Warner Music Group Corp.	$320	$ (30)	$ 38	$ (8)	$ 320	$ 320	$ 320	$ (640)	$ 320

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Consolidating Statement of Operations (Unaudited)

For The Three Months Ended June 30, 2017

	WMG Acquisition Corp. (issuer)	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	WMG Acquisition Corp. Consolidated	WMG Holdings Corp.	Warner Music Group Corp.	Eliminations	Warner Music Group Corp. Consolidated
	(in millions)								
Revenues	$—	$ 509	$ 510	$ (102)	$ 917	$ —	$ —	$ —	$ 917
Costs and expenses:									
Cost of revenue	—	(249)	(342						