Before the
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Washington, D.C.

In the Matter of Mechanical and Digital Phonorecord Delivery Rate Adjustment Proceeding	Docket No. 2006-3 CRB DPRA

THE WRITTEN DIRECT STATEMENT, WITNESS STATEMENTS & EXHIBITS OF NATIONAL MUSIC PUBLISHERS' ASSOCIATION, INC., THE SONGWRITERS GUILD OF AMERICA, AND THE NASHVILLE SONGWRITERS ASSOCIATION INTERNATIONAL

VOLUME XIX

Filed on April 10, 2007

EXHIBIT CO 0944

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... POWER ...

Form 10-K

Warner Music Group Corp. - WMG

Filed: December 01, 2005 (period: September 30, 2005)

Annual report which provides a comprehensive overview of the company for the past year

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended September 30, 2005

OR

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

For the transition period from to

Commission File Number 001-32502

Warner Music Group Corp.
(Exact name of Registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	13-4271875 (I.R.S. Employer Identification No.)
75 Rockefeller Plaza New York, NY 10019 (Address of principal executive offices)	10019 (Zip Code)

Registrant's telephone number, including area code: (212) 275-2000

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

Title of each class	Name of each exchange on which registered
Common Stock, $.001 par value	New York Stock Exchange

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

None

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 if the disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendments to this Form 10-K. ☐

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

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

As of March 31, 2005, there was no established market for the registrant's common stock. The aggregate market value of common stock held by non-affiliates as of September 30, 2005 was approximately $603,426,000, using the closing price per share of $18.51, as reported on the New York Stock Exchange as of such date.

As of November 24, 2005, the number of shares of the registrant's common stock, par value $0.001 per share, outstanding was 148,460,662.724.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Part III of this report is incorporated by reference from the registrant's proxy statement to be filed pursuant to Regulation 14A with respect to the registrant's fiscal 2005 annual meeting of stockholders.

WARNER MUSIC GROUP CORP.

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ITEM 1. BUSINESS

FORWARD-LOOKING STATEMENTS

This Form 10-K includes "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements are based on current expectations, estimates, forecasts and projections about the industry in which we operate, management's beliefs and assumptions made by management. Words such as "may," "will," "expect," "intend," "estimate," "anticipate," "believe," or "continue" or the negative thereof or variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements. We disclaim any duty to update or revise any forward-looking statements whether as a result of new information, future events or otherwise. See "Safe Harbor Statement Under Private Securities Litigation Reform Act of 1995."

Our Company

We are one of the world's major music content companies. Our company is composed of two businesses: Recorded Music and Music Publishing. We believe we are the world's fourth-largest recorded music company (third-largest in the U.S.) and the world's second-largest music publishing company. We are a global company, generating over half of our revenues in more than 50 countries outside of the U.S. We generated revenues of $3.502 billion during our fiscal year ended September 30, 2005.

Our Recorded Music business produces revenue through the marketing, sale and licensing of recorded music in various physical (such as CDs, cassettes, LPs and DVDs) and digital (such as downloads and ringtones) formats. We have one of the world's largest and most diverse recorded music catalogs, including 28 of the top 100 U.S. best-selling albums of all time—more than any other recorded music company, including *The Eagles: Their Greatest Hits 1971-1975* (the best-selling album of all time), *Led Zeppelin IV* and *Rumours* by Fleetwood Mac. We also lead all recorded music companies in albums certified as "Diamond" by RIAA, which are those albums that have more than 10 million net shipped units in the U.S., with approximately 30% of the total. Our roster of artists spans all musical genres and includes Led Zeppelin, The Eagles, Madonna, Green Day, Metallica and Fleetwood Mac. Our more recent album successes include artists such as Rob Thomas, Mike Jones, James Blunt, My Chemical Romance, Eric Clapton, T.I., Faith Hill, Death Cab for Cutie, Green Day, Disturbed, Paul Wall, and Big & Rich. Our Recorded Music business generated revenues of $2.924 billion during our fiscal year ended September 30, 2005. The sale of digital content has provided additional revenue streams for our Recorded Music business. Digital recorded music revenue has grown from essentially nothing at the time of our acquisition in 2004 to $137 million during our fiscal year ended September 30, 2005, and represented approximately 6% of recorded music revenues for the fourth quarter of fiscal 2005.

Our Music Publishing business owns and acquires rights to musical compositions, exploits and markets these compositions and receives royalties or fees for their use. We publish music across a broad range of musical styles. We hold rights in over one million copyrights from over 65,000 songwriters and composers. Our library includes titles such as "Summertime" by George and Ira Gershwin and DuBose Heyward, "Happy Birthday to You" by Mildred and Patty Hill, "Night and Day" by Cole Porter, "Layla" by Eric Clapton and Jim Gordon, "When a Man Loves a Woman" by Calvin Lewis and Andrew Wright, "Winter Wonderland" by Felix Bernard and Dick Smith, "Star Wars Theme" by John Williams, "The Wind Beneath My Wings" by Jeff Silbar and Larry Henley and "Frosty the Snowman" by Steve Nelson and Jack Rollins as well as more recent popular titles such as "Cry Me A River" performed by Justin Timberlake, "Smooth" by Itaal Shur and Rob Thomas, "Crazy in Love" performed by Beyoncé Knowles and Jay-Z, "Photograph" performed by Nickelback, "Burn" performed by Usher, "It's Been Awhile" performed by Staind, "Pieces of Me" performed by Ashlee Simpson, "Thank You" performed by Dido Armstrong, "American Idiot" performed by Green Day, "The Reason" performed by

Hoobastank, "Pon DeReplay" performed by Rihanna, "Gold Digger" performed by Kanye West, "We Belong Together" performed by Mariah Carey and "Outta Control" performed by 50 Cent. Our Music Publishing business generated revenues of $607 million during our fiscal year ended September 30, 2005. The sale of digital content has also provided new revenue streams for our Music Publishing business. Digital music publishing revenue has grown from essentially nothing at the time of our acquisition in 2004 to $20 million during our fiscal year ended September 30, 2005, and represented 4% of music publishing revenue for the fourth quarter of fiscal 2005.

Our Business Strengths

While we have recorded net losses on a historical and pro forma basis, primarily due to the decline since 1999 of recorded music sales, increased operating costs, increased competition, and such items as impairment charges and charges related to our initial common stock offering, we believe the following competitive strengths will enable us to continue to generate stable cash flow through our diverse base of recorded music and music publishing assets:

Industry Leading Recording Artists and Songwriters. We have been able to consistently attract, develop and retain successful recording artists and songwriters. Our talented local artist and repertoire teams are focused on finding and nurturing future successful recording artists and songwriters, as evidenced by our recent recorded music album and music publishing successes. This has enabled us to develop a large and varied portfolio of recorded music and music publishing assets that generate stable and recurring cash flows. We believe these assets demonstrate our historical success in developing talent and will help to attract future talent in order to enable our continued success.

Stable, Highly Diversified Revenue Base. Our revenue base is derived primarily from relatively stable and recurring sources such as our music publishing library, our catalog of recorded music and new releases from our existing base of established artists. In any given year, we believe that less than 10% of our total revenues depend on artists without an established track record, with each of these artists typically representing less than 1% of our revenues. We have built a large and diverse catalog of recordings and compositions that covers a wide breadth of musical styles including pop, rock, jazz, country, R&B, hip-hop, rap, reggae, Latin, alternative, folk, blues, gospel and other Christian music. We are a significant player in each of our major geographic regions.

High Cash Flow Business Model. We have a highly variable cost structure, with substantial discretionary spending and minimal capital requirements. In October 2003, Time Warner's CD and DVD manufacturing, packaging and physical distribution operations were sold to Cinram, resulting in a significant reduction of our fixed cost base. As part of the sale, we entered into an outsourcing arrangement with Cinram that significantly reduced our exposure to fixed costs and will reduce our future capital expenditure requirements. We spent $30 million in capital expenditures for our fiscal year ended September 30, 2005, $18 million for our ten-month fiscal year ended September 30, 2004 and $51 million for our twelve-month fiscal year ended November 30, 2003. We continuously seek sensible opportunities to convert fixed costs to variable costs. Finally, in addition to our variable cost base and relatively low capital requirements, we have contractual flexibility with regard to the timing and amounts of advances paid to existing recording artists and songwriters as well as discretion regarding future investment in new artists and songwriters, which further allows us to respond to changing industry conditions.

Well Positioned For Growth In Digital Distribution and Emerging Technologies. Through the first three quarters of calendar 2005, our shares of digital recorded music track and album sales in the U.S. as measured by SoundScan were higher than our overall recorded music album share in the U.S., which we believe reflects the relative strength of our content and in particular our catalog content, as well as the success of our recent digital innovation efforts (such as, digital album bundles). In addition, we are highly focused on several new media initiatives: supporting existing and new online services in the U.S. and abroad, working with legitimate peer-to-peer, or P2P, providers and influencing the evolution of new mobile phone services and formats (we have, for example, an agreement between our recorded music and music publishing division for rates on mastertones, ringback tones and other new wireless formats). We have been a leader in mobile music and the use of wireless

technology. We work closely with cellular carriers and device manufacturers to develop mobile music content, including ringtones, ringback tones, artist-branded games, music videos and celebrity non-music personalization products for mobile channels. In the U.S., we have led the music industry with a series of accomplishments in the wireless industry, including being the first major music company to offer a mobile music streaming service and the first major music company to offer full music video downloads through a wireless carrier.

Proven and Committed Management Team. We are led by an experienced senior management team with an average of approximately 20 years of entertainment industry experience. Edgar Bronfman, Jr., our Chairman of the Board and Chief Executive Officer, has extensive and directly relevant experience in the music industry. In 1998, Mr. Bronfman, while President and CEO of Seagram, oversaw the merger of Universal and PolyGram and successfully managed the combined business, the world's largest recorded music company. In addition, Lyor Cohen, who is our Chairman and CEO of U.S. Recorded Music operations, has nearly two decades of experience in the music industry and has previously worked with Mr. Bronfman in his former role as the Chairman and CEO of Universal's Island Def Jam Music Group. Paul-René Albertini, the Chairman and CEO of Warner Music International, is also a music industry veteran with over 20 years of experience. In May of 2005, we hired Richard Blackstone as the Chairman and CEO of our Music Publishing business, Warner/Chappell Music. Mr. Blackstone, who was previously the President and Chief Executive Officer of Zomba Music Publishing, has 15 years of experience in the music publishing business. Our senior management team is very committed to our success. For example, Music Capital Partners, L.P., an investment vehicle controlled by Edgar Bronfman, Jr., owned approximately 9.6% of our equity as of September 30, 2005. The rest of our senior management team owns a meaningful share of our equity through service and performance-based equity plans.

Strong Equity Sponsorship. Thomas H. Lee Partners L.P. and its affiliates (THL), Bain Capital, LLC and its affiliates (Bain Capital), and Providence Equity Partners, Inc. and its affiliates (Providence Equity) are each leading private equity firms with extensive experience in managing investments in entertainment and media assets and a long history of working successfully together. These equity sponsors currently manage entertainment and media companies including Houghton Mifflin Company, ProSiebenSAT.1 Media, American Media and Mountain States Cable. The addition of Edgar Bronfman, Jr., through Music Capital Partners L.P. (Music Capital, and together with THL, Bain Capital and Providence Equity, the Investor Group), brings substantial and directly relevant management experience in the music industry.

Our Strategy

We intend to increase revenues and cash flow through the following business strategies:

Attract, Develop and Retain Established and Emerging Recording Artists and Songwriters. A critical element of our strategy is to find, develop and retain recording artists and songwriters who achieve long-term success. Our local artist and repertoire ("A&R") teams seek to sign talented recording artists with strong potential, whose new releases will generate a meaningful level of sales and increase the enduring value of our catalog by continuing to generate sales on an ongoing basis, with little additional marketing expenditure. We also work to identify promising songwriters who will write musical compositions that will augment the lasting value and stability of our music publishing library. We believe our relative size, the strength of our management team, our ability to respond to industry and consumer trends and challenges, our diverse array of genres, our large catalog of hit releases and our valuable music publishing library will help us continue to successfully build our roster of artists and songwriters. We are constantly looking for new, innovative ways to develop and execute our A&R strategy. For example, in the U.S., we have designed an incubator system, which leverages our strong independent distribution network to identify major acts of the future at a lower cost. At its essence, the incubator system is innovative A&R spending. In addition, we have recently launched Cordless Recordings, an "e-label" that gives its artists the ability to come to market with one or several songs in the digital world without the need to create an entire album. This is another example of ways we are expanding our A&R strategy to adapt to and take advantage of the changing marketplace to find and develop new recording artists and songwriters.

Maximize the Value of our Music Assets. Our relationships with our recording artists and songwriters, our recorded music catalog and our music publishing library are our most valuable assets. We intend to continue to

exploit the value of these assets through a variety of distribution channels to generate significant cash flow from our music content. We believe that the ability to monetize our music content should increase over time as new distribution channels and new formats increase.

- Our Recorded Music business focuses on marketing our artists and catalog in new ways to retain existing fans of established artists and to generate new demand for our proven hits. For example, in 2005, we released a number of successful repurposed catalog compilations, including Ray Charles— *The Ray Soundtrack, Vol 2*, Crosby, Stills & Nash —*Greatest Hits*, and Michael McDonald —*Ultimate Collection*. We also released successful video content such as *George Harrison—The Concert for Bangladesh*. The growing number of legitimate digital distribution outlets allows us to generate incremental catalog sales. From the launch of Apple's iTunes Music Store in the United States in April 2003 through October 2, 2005, catalog sales have represented 54% of our top 200 digital track sales sold on iTunes versus 41% of our physical album sales over the same period.

- Our Music Publishing business seeks to capitalize on the growing demand for the use of musical compositions in media products such as videogames, commercials, other musical works (such as authorized sampling), films, DVDs, mobile phone ringtones and Internet and wireless streaming and downloads by marketing and promoting our libraries to producers of these media in new and innovative ways.

We will seek to exploit the potential of previously unmonetized content in new products and channels from ringtones to full track video and song downloads on mobile phones. For example, we have over 20 years of music videos that we have yet to fully monetize as well as unexploited album art, lyrics, and B-side tracks that that have never been physically released. We are seeking opportunities to create premium-priced album bundles by combining our existing assets with new assets that we are creating such as bonus tracks, music videos and "behind the scenes" footage.

We intend to enhance the value of our assets by continuing to attract and develop new artists and songwriters with staying power and market potential. Additionally, we intend to continually evaluate our artist and songwriter roster to ensure we remain focused on developing the most promising and profitable talent. We will also continue to work with our partners to explore creative approaches and constantly experiment with new deal structures and products to take advantage of new distribution channels.

Focus on Continued Management of Our Cost Structure. We will continue to maintain a disciplined approach to cost management in our business and to pursue additional cost savings. We will also continue to monitor industry conditions to ensure that our business remains aligned with industry trends. For example, subsequent to the acquisition of our company by the Investor Group in 2004, we implemented a broad restructuring plan in order to realign our cost structure with the changing economics of the music industry. The restructuring plan included the consolidation of select business divisions of our Elektra and Atlantic labels, including the legal and business affairs, finance and label sales units, rationalization of our global network, pruning of approximately 30% of our artist roster and an approximately 20% reduction in our global workforce. We completed substantially all of these restructuring efforts in fiscal 2005. In connection with the restructuring plan, we implemented approximately $250 million of annualized cost savings.

Invest in Accordance with an Improved Asset Allocation Strategy and More Efficiently Allocate Capital. We seek to invest in lines of business, geographic locations and individual projects where we believe we can optimize our return on capital. We will also consider the strategic importance of alternative investments in addition to their financial metrics. We believe that as a result of our management processes, analytic techniques and investment discipline, we are well positioned to efficiently deploy our capital. For example, we will continue to seek better returns through a more efficient allocation of our resources by, among other initiatives (1) allocating capital to a smaller number of acts to increase A&R spend per act, (2) reducing our operations in unprofitable geographies and (3) developing initiatives such as our incubator strategy and our new e-label, Cordless Recordings, to identify artists earlier in their careers, allowing us to broaden the scope of our investments in new artists without significant upfront capital.

Develop and Optimize Our Physical Distribution Channel Strategies. We will continue to develop innovative programs with our physical distribution partners to achieve greater sales volume. The physical distribution channels for records are evolving as new outlets develop, the mix of channels and retailers change, new formats for our content are created and pricing models multiply to meet a wide range of needs. Our Recorded Music business will continue to cooperate with its physical distribution channel partners in order to implement forward-looking strategies for our mutual benefit. We will also invest to meet the needs of our channel partners to create more efficient collaboration, such as direct-to-retail distribution strategies and vendor managed inventory.

Capitalize on Digital Distribution and Emerging Technologies. Digital formats should continue to represent new avenues for the distribution and exploitation of our recorded music and music publishing assets. We believe that the development of legitimate Internet and wireless channels for the purchase of music holds significant promise and opportunity for the industry. In particular, new and emerging third-party digital distribution outlets are not only reasonably priced, but also offer a superior customer experience relative to illegal alternatives, as they are easy to use, offer uncorrupted song files and integrate seamlessly with increasingly popular portable music players such as the Apple iPod and its recently released iPod Nano and video versions, the Dell DJ Digital Jukebox and the Creative Nomad. In addition, we believe digital distribution will stimulate incremental catalog sales given the ability to offer enhanced presentation and searchability of our catalog. As networks and phone handsets become more sophisticated, our music is increasingly becoming available on mobile phone platforms through wireless service providers via ringtones, ringback tones, full track downloads and music video downloads. We believe the wireless business offers a more secure environment than does the Internet and thereby reduces our exposure to piracy.

Contain Digital Piracy. Containing piracy is a major focus of the music industry and we, along with the rest of the industry, are taking multiple measures through technological innovation, litigation, education and the promotion of legislation to combat piracy. We will continue to take a leadership role in the music industry's war against piracy, as we did by championing the industry-wide development of the new DualDisc (CD/DVD) physical format, partnering with Apple on its security model for its Macintosh and PC launches of iTunes, and encouraging Microsoft to retool its digital rights management digital media copyright protection technology and include playlist burn limits. In addition, we continue to support the aggressive measures taken by RIAA, IFPI and NMPA, including civil lawsuits, education programs, political lobbying for tougher restrictions on use and international efforts to preserve music copyrights. We believe new technologies geared towards degrading the illegal file-sharing process and tracking the source of pirated music and offer a means to reduce piracy. Furthermore, recent legal actions by our industry, both in and outside the U.S., have been designed to educate consumers that stealing music is against the law and deter illegal downloads. A number of recent decisions, including the U.S. Supreme Court decision in Grokster and the Federal Court of Australia's ruling in a case involving KaZaA have held that P2P networks can be held liable if they induce users to violate copyright laws. The industry has also been working with educational institutions to implement controls to prohibit students from illegally downloading copyrighted material. We believe that consumer awareness of the illegality of piracy has increased as a result of these initiatives. We believe these actions, in addition to the expansive growth of legitimate online music offerings, will help to limit the revenues lost to digital piracy. See "*Industry Overview—Recorded Music—Piracy*".

Company History

Our history dates back to 1929, when Jack Warner, president of Warner Bros. Pictures, Inc., founded Music Publishers Holding Company ("MPHC") to acquire music copyrights as a means of providing inexpensive music for films. MPHC was constructed through the acquisition of M. Witmark & Sons, Remick Music Corp., Harms, Inc. and Advanced Music Corporation. Along with these companies came the beginning of our valuable library of publishing assets, including the works of Cole Porter, Richard Rodgers and Lorenz Hart. Collectively, these assets, as well as numerous others were acquired over the last 75 years, including Chappell & Intersong Music Group acquired in 1987.

Encouraged by the success of MPHC, Warner Bros. extended its presence in the music industry with the founding of Warner Bros. Records in 1958 as a means of distributing movie soundtracks and further exploiting actors' contracts. For over 45 years, Warner Bros. Records has pushed the bounds of the industry both creatively and financially with the discovery of artists such as Neil Young, Grateful Dead and the acquisition of Frank Sinatra's Reprise Records in 1963. Today, Warner Bros. Records is home to such artists as Faith Hill, Red Hot Chili Peppers, Linkin Park, Josh Groban and Madonna.

Atlantic Records was launched in 1947 by Ahmet Ertegun and Herb Abramson as a small New York-based label focused on jazz and R&B. Led by Ertegun, Atlantic had early hits by such artists as Ray Charles, John Coltrane and Aretha Franklin, but quickly broadened its reach and found increasing success with artists such as Bobby Darin, Crosby, Stills & Nash, Buffalo Springfield, Sonny and Cher and Led Zeppelin. Elektra Records was founded in 1950 by Jac Holzman as a folk music label. With an eye to emerging music, Elektra Records signed such artists as Joni Mitchell, The Eagles, The Doors and Jackson Browne. The Atlantic Records Group is home to Elektra Records, Atlantic Records and Lava Records and boasts a roster of acclaimed artists such as matchbox twenty, Led Zeppelin, Phil Collins, Jewel, Kid Rock, T.I., Tracy Chapman, Metallica, Simple Plan, James Blunt and Lil' Kim.

Since 1970, we have operated internationally through Warner Music International ("WMI"). WMI is responsible for the sale and marketing of our U.S. artists abroad as well as the acquisition and development of international artists such as The Darkness, Alejandro Sanz, Maná, MC Solaar and Laura Pausini.

In 2002, we acquired Word Entertainment to expand our presence in the Christian music genre. Word Entertainment boasts a deep roster of Christian artists, including Jaci Velasquez and Randy Travis.

Warner Music Group was acquired by the Investor Group from Time Warner Inc. ("Time Warner") in March 2004.

Warner Music Group became the only stand-alone music company with publicly traded common stock in the United States in May 2005.

Recorded Music (83%, 81% and 84% of consolidated revenues in fiscal 2005, 2004 and 2003, respectively)

Our recorded music operations consist of the discovery and development of artists and the related marketing and distribution of recorded music produced by such artists. In addition to the more traditional methods of discovering and developing artists, we have implemented new initiatives to identify and nurture artists earlier in the development process and reduce development costs by leveraging our independent distribution network. We refer to these new business models as incubator initiatives. Asylum and East West are current incubator labels. In addition, we have also entered into strategic ventures with other record labels.

Our recorded music operations also include a catalog division called Rhino Entertainment ("Rhino"), which was formerly called Warner Strategic Marketing. Rhino specializes in marketing our music catalog through compilations and reissuances of previously released music and video titles, as well as in the licensing of tracks to/from third parties for various uses, including film and television soundtracks.

Our principal recorded music distribution operations include Warner-Elektra-Atlantic Corporation ("WEA Corp."), which primarily distributes our music products to retailers and wholesale distributors in the United States; a 90% interest in Alternative Distribution Alliance ("ADA"), a distribution company which primarily distributes the products of independent record labels to retailers and wholesale distributors; various distribution centers and ventures operated internationally; and an 80% interest in Word Entertainment, whose distribution operations specialize in the distribution of music products in the Christian retail marketplace.

We play an integral role in virtually all aspects of the music value chain from discovering and developing talent, to producing albums and promoting artists and their product. After an artist has entered into a contract

with one of our record labels, a master recording of the artist's music is created. The recording is then replicated for sale to consumers primarily in the CD format, and now, in digital formats. In the U.S., WEA Corp. and ADA market, sell and deliver product, either directly or through sub-distributors and wholesalers, to thousands of record stores, mass merchants and other retailers throughout the country. Our recorded music products are also sold in physical form to Internet physical retailers such as Amazon.com and barnesandnoble.com and in digital form to Internet digital retailers like Apple's iTunes and musicmatch.com.

In the United States, our recorded music operations are conducted principally through our major record labels—Warner Bros. Records and The Atlantic Records Group.

In markets outside the U.S., our recorded music activities are conducted through WMI and its various subsidiaries, affiliates and non-affiliated licensees. WMI produces revenues in more than 50 countries outside the U.S. and engages in the same activities as our U.S. labels: discovering and signing artists and distributing, marketing and selling their recorded music. In most cases, WMI also markets and distributes the records of those artists for whom our domestic record labels have international rights. In certain countries, WMI licenses to unaffiliated third-party record labels the right to distribute its records.

Artists and Repertoire ("A&R")

We have a decades-long history of identifying and contracting with recording artists who become commercially successful. Our ability to select artists who are likely to be successful is a key element of our Recorded Music business strategy. Our ability to select artists spans all music genres and all major geographies and includes artists who achieve national, regional and international success. We believe that this success is directly attributable to our experienced global team of A&R executives, to the longstanding reputation and relationships that we have nurtured in the artistic community and to our effective management of this vital business function.

In the U.S., our major record labels identify potentially successful recording artists, sign them to recording agreements, collaborate with them to develop recordings of their work and market and sell these finished recordings to retail stores and legitimate online channels. Our labels scout and sign talent across all major music genres, including pop, rock, jazz, country, R&B, hip-hop, rap, reggae, Latin, alternative, folk, blues, gospel and other Christian music. WMI markets and sells U.S. and local repertoire from its own network of affiliates and numerous licensees in more than 50 countries. With a roster of local artists performing in 25 languages, WMI has an ongoing commitment to developing local talent aimed at achieving national, regional, or international success.

We continue to realize significant success in the acquisition of new artists and the development of new content. In 2005, we have already upstreamed five urban and three rock artists to our major labels through our incubator initiative, four of whom have debuted in the top 10 in Billboard's Top 200 chart (Mike Jones, Paul Wall, Webbie and Bun-B). We have also had a number of artists with releases in 2005 that debuted at the #1 spot in the Billboard Top 200 Chart including Staind, Disturbed and Faith Hill. Other artists that have seen success in 2005 include Green Day, Linkin Park, Michel Bublé, Simple Plan, Rob Thomas, Big & Rich, and Shinedown. We also released top-selling albums from other new artists such as James Blunt, The Click Five and My Chemical Romance, and the major-label debuts of artists including Death Cab for Cutie, Rilo Kiley and Cowboy Troy in 2005.

A significant number of our recording artists have continued to appeal to audiences long after we cease to release their new recordings. Our catalog includes the U.S. best-selling album of all time, *The Eagles: Their Greatest Hits 1971-1975*, which has sold 28 million units to date. We have an efficient process for generating continued sales across our catalog releases, as evidenced by the fact that catalog albums generate approximately 40% of our recorded music sales. Relative to our new releases, we spend comparatively small amounts on marketing for catalog sales.

We maximize the value of our catalog of recorded music through our Rhino business unit and through activities of each of our record labels. We use our catalog as a source of material for re-releases, compilations, box sets and special package releases, which provide consumers with incremental exposure to familiar songs and artists. Recent examples include packages such as "*No Thanks!—The 70's Punk Rebellion*," greatest hits collections from artists such as The Eagles, Crosby, Stills & Nash, Joni Mitchell, Sugar Ray, Rickie Lee Jones, Brandy and Emmylou Harris, box sets by Ray Charles, ZZ Top, Talking Heads, Jerry Garcia, The Faces, Black Sabbath and The Grateful Dead, and DVDs of Live Aid, Led Zeppelin's *"How the West Was Won"*, Ray Charles' "*O—Genio: Ray Charles Live in Brazil, 1963*", the George Harrison tribute, "*The Concert for George*", The Ramones documentary, "*End of the Century: The Story of The Ramones*" and The Eagles *"Farewell I Tour—Live From Melbourne"* and the multi-artist box set of 80's songs, "*Left of the Dial: Dispatches from the 80's Underground*".

Representative Worldwide Recorded Music Artists

Avenged Sevenfold	Cowboy Troy	Green Day	Metallica	Seal
Big & Rich	Damien Rice	David Gray	Luis Miguel	Sean Paul
Bjork	The Darkness	Mike Jones	Missy Elliott	Shinedown
James Blunt	Craig David	Josh Groban	Alanis Morissette	Simple Plan
Boyz N Da Hood	Death Cab for Cutie	Jet	My Chemical Romance	Staind
Michelle Branch	Diddy	Jewel	Muse	Sugar Ray
Michael Bublé	Disturbed	Kid Rock	Notorious B.I.G.	Rob Thomas
Ryan Cabrera	The Eagles	Led Zeppelin	Laura Pausini	T.I.
Tracy Chapman	Enya	Linkin Park	P.O.D.	Twista
Cher	Fabolous	Madonna	Red Hot Chili Peppers	Uncle Kracker
Eric Clapton	Faith Hill	Maná	R.E.M.	Paul Wall
Phil Collins	Fleetwood Mac	matchbox twenty	Rilo Kiley	Westernhagen
The Corrs	Goo Goo Dolls	MC Solaar	Alejandro Sanz	Neil Young

Artists' Contracts

Our artists' contracts define the commercial relationship between our recording artists and our record labels. We negotiate recording agreements with artists that define our right to use the artists' copyrighted recordings in sales and licenses of our recorded music products worldwide. In accordance with the terms of the contract, the artists receive royalties based on sales and other forms of exploitation of the artists' recorded works. We customarily provide up-front payments to artists called advances, which are recoupable by us from future royalties otherwise payable to artists. We also typically pay costs associated with the recording and production of albums, which are treated in certain countries as advances recoupable from future royalties. Our typical contract for a new artist covers a single initial album and provides us a series of exclusive options to acquire subsequent albums from the artist. Royalty rates are often increased for optional albums. Many of our contracts contain a commitment from the record label to fund video production costs, at least a portion of which is generally an advance recoupable from future royalties.

Our established artists' contracts generally provide for greater advances and higher royalty rates. Typically, established artists' contracts entitle us to fewer albums, and, of those, fewer are optional albums. In contrast to new artists' contracts, which typically give us ownership in the artist's work for the full term of copyright, some established artists' contracts provide us with an exclusive license for some fixed period of time. It is not unusual for us to renegotiate contract terms with a successful artist during a term of an existing agreement, sometimes in return for an increase in the number of albums that the artist is required to deliver.

We are also experimenting with other forms of business models with artists to adapt to changing industry conditions. For example, Cordless Recordings, our digital-only e-label will pioneer a new business model allowing for regular release of song "clusters". The label will allow artists to retain masters of their work and copyright ownership in certain cases. Our incubator labels, Asylum and East West, also enter into deals designed to provide a variety of services to labels and artists, such as marketing, distribution and sales services.

Marketing and Promotion

WEA Corp. and ADA market and sell our recorded music product in the U.S. Our approach to marketing and promoting our artists and their recordings is comprehensive. Our goal is to maximize the likelihood of success for new releases as well as stimulate the success of previous releases. We seek to maximize the value of each artist and release, and to help our artists develop an image that maximizes appeal to consumers.

We work to raise the profile of our artists, through an integrated marketing approach that covers all aspects of their interactions with music consumers. These activities include helping the artist develop creatively in each release, strategically scheduling album releases and selecting singles for release, creating concepts for videos that are complementary to the artists' work, and coordinating promotion of albums to radio and television outlets. We are also experimenting with ways to promote our artists through digital channels with such initiatives as experimenting with windowing of content and creating product bundles by combining our existing assets with new assets that are created simultaneously with the album (such as bonus tracks, music videos and "behind the scenes" footage). Through digital distribution channels we have greater marketing flexibility that can be more cost effective. For example, direct marketing is possible through access to consumers via websites and pre-release activity can be customized. When possible, we seek to add an additional personal component to our promotional efforts by facilitating television and radio coverage or live appearances for our key artists. Our corporate and label websites provide additional marketing venues for our artists.

In further preparation for and subsequent to the release of an album, we coordinate and execute a marketing plan that addresses specific retail strategies to promote the album. Aspects of these promotions include in-store appearances, advertising, displays and placement in album listening stations. These activities are overseen by our marketing staff to ensure that maximum visibility is achieved for the artist and the release.

Our approach to the marketing and promotion of recorded music is carefully coordinated to create the greatest sales momentum, while maintaining strict fiscal discipline. We have significant experience in our marketing and promotion departments, which we believe allows us to achieve an optimal balance between our marketing expenditure and the eventual sales of our artists' recordings. We use a budget-based approach to plan marketing and promotions, and we monitor all expenditures related to each release to ensure compliance with the agreed-upon budget. These planning processes are informed by updated reports on an artists' retail sales and radio play, so that a promotion plan can be quickly refined in the event of a commercial success or failure.

While marketing efforts extend to our catalog albums, most of the expenditure is directed toward new releases. Rhino specializes in marketing our catalog through compilations and reissues of previously released music and video titles, licensing tracks to third parties for various uses and coordinating film and television soundtrack opportunities with third-party film and television producers and studios.

Manufacturing, Packaging and Physical Distribution

On October 24, 2003, Time Warner sold its CD and DVD manufacturing, packaging and physical distribution operations ("TW Manufacturing") to Cinram for approximately $1.1 billion in cash consideration. The transaction included the sale of the following businesses: WEA Manufacturing Inc., Warner Music Manufacturing Europe GmbH, Ivy Hill Corporation, Giant Merchandising and the physical distribution operations of WEA Corp. The sales and marketing operations of WEA Corp. remain a part of our business.

At the time of the sale of TW Manufacturing to Cinram, we entered into manufacturing, packaging and physical distribution arrangements with Cinram for our CDs and DVDs in the U.S. and Europe. We believe that the terms of the Cinram agreements reflect market rates and are more favorable than our previous arrangements.

Sales

Most of our sales represent purchases by a wholesale or retail distributor. Our return policies are in accordance with wholesale and retailer requirements, applicable laws and regulations, territory- and customer-specific negotiations, and industry practice. We attempt to minimize the return of unsold product by monitoring shipments and sell-through data.

We generate sales from both our roster of current artists and our catalog of recordings. In addition, we actively repackage and remarket music from our catalog to form new compilations. Most of our sales are generated through the CD format, although we also sell our music through both historical formats, such as cassettes and vinyl albums, and newer emerging digital formats and physical formats, including DVD-Audio and DualDisc.

We sell our recorded music products through a variety of different retail and wholesale outlets including music specialty stores, general entertainment specialty stores, supermarkets, mass merchants and discounters, independent retailers, and other traditional retailers. Although some of our retailers are specialized, many of our customers offer a substantial range of products other than music. We work with our customers to ensure optimal product placement and promotion.

We believe that the Internet has become an increasingly important sales channel. Sales through the Internet include sales of traditional physical formats through both the Internet distribution arms of traditional retailers such as walmart.com or hmv.com and online physical retailers such as Amazon.com and barnesandnoble.com. In addition, there has been a proliferation of legitimate online sites which sell digital music on a per album or per track basis and several carriers are also introducing the capability to download music on mobile devices. We currently partner with a broad range of online digital and mobile providers, such as iTunes, MusicNet, musicmatch, Rhapsody, Sprint, Verizon and Cingular and are actively seeking to develop and grow this business. In digital formats, costs related directly to physical products such as manufacturing, distribution, inventory and return costs do not apply. While there are some digital-specific variable costs and infrastructure investments needed to produce, market, and sell digital products, it is reasonable to expect that we will generally derive a higher contribution margin from digital versus physical sales.

Music Publishing (17%, 20% and 17% of consolidated revenues in fiscal 2005, 2004 and 2003, respectively)

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

Warner/Chappell is our global music publishing company headquartered in Los Angeles with operations in over 50 countries through various subsidiaries, affiliates and non-affiliated licensees. We own or control 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, our award-winning catalog includes over 65,000 songwriters and composers and a diverse range of genres including pop, rock, jazz, country, R&B, hip-hop, rap, reggae, Latin, folk, blues, symphonic, soul, Broadway, techno, alternative, gospel and other Christian music. Our best-selling songwriter or song owner and song accounted for less than 2.5% and 1% of our music publishing revenues for the twelve months ended September 30, 2005, respectively. Moreover, our music publishing library includes many standard titles that span multiple music genres and has demonstrated the ability to generate consistent revenues over extended periods of time. For example, over the last ten years, our top ten earning songs, which include such titles as "Happy Birthday to You" and "Winter Wonderland" have generally generated average annual revenues of between $0.5 million and $1.5 million per song. Warner/Chappell also administers the music and soundtracks of several third-party television and film producers and studios, including Lucasfilm, Ltd. and Hallmark Entertainment.

Warner/Chappell also previously owned Warner Bros. Publications ("WBP"), which printed and distributed a broad selection of sheet music, books and educational materials, orchestrations, folios, personality books, and arrangements from the catalogs of Warner/Chappell and other music publishers. On May 31, 2005, we sold our printed sheet music business to Alfred Publishing.

Music Publishing Portfolio

Representative Songwriters

Burt Bacharach
Michelle Branch
Andreas Carlsson
Eric Clapton
Bryan-Michael Cox
Sheryl Crow
Dr. Dre
Dido
Fat Joe
George and Ira Gershwin
Green Day
Don Henley
Michael Jackson
Led Zeppelin
Madonna
Nickelback
Pantera
Cole Porter
Radiohead
The Ramones
Alejandro Sanz
John Shanks
Staind
Timbaland
Van Morrison
Barry White
John Williams

Representative Songs

1950s and Prior

Summertime
Happy Birthday to You
Night and Day
The Lady is a Tramp
Too Marvelous for Words
Dancing in the Dark
Winter Wonderland
Ain't She Sweet
Frosty the Snowman
When I Fall In Love
Misty
The Party's Over
On the Street Where You Live
Blueberry Hill

1960s

People
I Only Want to be With You
When a Man Loves a Woman
I Got a Woman
People Get Ready
Love is Blue
Hey Big Spender
For What It's Worth
Sunny
The Look of Love

1970s

Behind Closed Doors
Ain't No Stopping Us Now
For the Love of Money
A Horse With No Name
Moondance
Peaceful Easy Feeling
Layla
Staying Alive
Star Wars Theme

1980s

Eye of the Tiger
Slow Hand
The Wind Beneath My Wings
Endless Love
Morning Train
What You Need
Beat It
Jump
We Are the World

1990s

Unbelievable
Creep
Macarena
Sunny Came Home
Amazed
This Kiss
Believe
Smooth
Livin' La Vida Loca

2000 and After

It's Been Awhile
Photograph
Complicated
You Got It Bad
Crazy in Love
Cry Me a River
White Flag
Dilemma
Work It
Miss You
Bum
American Idiot
The Reason
Save a Horse (Ride a Cowboy)

Our Music Publishing revenues are derived from four main sources:

- *Mechanical:* the licensor receives royalties with respect to compositions embodied in recordings sold in any format or configuration, including singles, albums, CDs, digital downloads and mobile phone ringtones.
- *Performance:* the licensor receives royalties when the composition is performed publicly (*e.g.*, broadcast radio and television, movie theater, concert, nightclub or Internet and wireless streaming).
- *Synchronization:* the licensor receives royalties or fees for the right to use the composition in combination with visual images (*e.g.*, in films, television commercials and programs and videogames).
- *Other:* the licensor receives royalties from other uses such as stage productions and printed sheet music.

Music Publishing Royalties

Warner/Chappell, as a copyright owner or administrator of copyrighted musical compositions, is entitled to receive royalties for the exploitation of those musical compositions as identified below. Often, a copyright owner will transfer "administration rights" to a third party. Administration rights are the rights to license uses of the composition and collect monies derived therefrom.

Music publishers generally receive royalties pursuant to synchronization, mechanical, public performance and other licenses. Throughout the world, each synchronization license is subject to negotiation with a prospective licensee. By contract, music publishers pay a contractually required percentage of synchronization income to the songwriter(s) (or their heirs) and to any co-publishers. In the U.S., music publishers collect and administer mechanical royalties, and statutory ceilings are established by the U.S. Copyright Act of 1976, as amended, for the royalty rates applicable to musical compositions for sales of recordings embodying those musical compositions. In the U.S., public performance royalties are typically administered and collected by performing rights organizations and in most countries outside the U.S., collection, administration and allocation of both mechanical and performance income are undertaken and regulated by governmental or quasi-governmental authorities. *See "Industry Overview—Music Publishing"*.

Warner/Chappell acquires copyrights (or portions of copyrights) and administration rights from songwriters or other third-party holders of rights in compositions. Typically, in either case, the grantor of rights retains a right to receive a percentage of revenues collected by Warner/Chappell. As an owner and/or administrator of compositions, we promote the use of those compositions by others. For example, we encourage recording artists to record and include our songs on their albums, offer opportunities to include our compositions in filmed entertainment, advertisements and wireless media, and advocate the use of our compositions in live stage productions. Examples of music uses that generate publishing revenues include:

Mechanical: sale of recorded music in various formats

- Physical recordings (*e.g.*, CDs, cassettes, DVDs, video cassettes)
- Internet and wireless downloads
- Mobile phone ringtones

Performance: performance of the song to the general public

- Broadcast of music on television, radio, cable, satellite
- Live performance at a concert or other venue (*e.g.*, arena concerts, nightclubs)
- Broadcast of music at sporting events, restaurants or bars
- Internet and wireless streaming
- Performance of music in staged theatrical productions

Synchronization: use of the song in combination with visual images

- In films or television programs
- In television commercials
- In videogames

Other:

- Use in toys or novelty items
- Sales of sheet music used by orchestras or individuals (prior to our sale of the printed sheet music business in May 2005)

Composers' and Lyricists' Contracts

Warner/Chappell derives its rights through contracts with composers and lyricists (songwriters) or their heirs, and with third-party music publishers. In some instances, those contracts grant either 100% or some lesser percentage of ownership in musical compositions and administration rights. In other instances, those contracts only convey to Warner/Chappell rights to administer and exploit musical compositions for a period of time without retaining an ownership interest. Our contracts grant us exclusive exploitation rights in the territories concerned (excepting any pre-existing arrangements). Many of our contracts grant us rights on a worldwide basis. Contracts cover the entire work product of the writer or composer for the duration of the contract. As a result, Warner/Chappell typically possesses the administration rights for every musical composition created by the writer or composer during the duration of the contract.

While the duration of the contract may vary, many of our contracts grant us ownership and/or administration rights for the duration of copyright. U.S. copyright law permits authors or their estates to terminate an assignment or license of copyright (for the U.S. only) after a set period of time. In addition, in the U.K., rights transferred by an author of certain works created before June 1, 1957 automatically revert to their author's heirs 25 years after the author's death.

Marketing and Promotion

We actively seek, develop and maintain relationships with songwriters.

We actively market our copyrights to end users such as recorded music companies (including our Recorded Music business), filmed entertainment, television and other media companies, advertising and media agencies, event planners and organizers, computer and video game companies and other multimedia producers. We also market our musical compositions for use in live stage productions and merchandising. In addition, we actively seek new and emerging outlets for the exploitation of songs such as ringtones for cellular phones, new wireless and online uses, digital sheet music and Internet webcasting.

We continually add new musical compositions to our catalog, and seek to acquire rights in songs that will generate substantial revenue over long periods of time.

Digital Sales

We have integrated the sale of digital content into all aspects of our Recorded Music and Music Publishing businesses including A&R, marketing, promotion and distribution. Our new media executives work closely with the A&R departments of our labels to make sure that while a record is being made, digital assets are also created with all of our distribution channels in mind. We also work side-by-side with our wireless and online partners to test new concepts. We believe existing digital businesses will be a significant source of growth for the next several years and will provide new opportunities to monetize our assets and create new revenue streams. As a

music content company, we have assets that go beyond our music catalog and copyrights, such as our music video library, that we now have the opportunity to monetize through digital channels. In addition, we can digitally exploit album art, lyrics and B-side tracks that have never been physically released. For example, we have an agreement with MTV Networks for the use of our music videos in original mobile content and programming. In general, digital music content is sold through two primary channels: online and mobile. The proportion of revenues attributed to each distribution channel varies by region, with digital downloads making up the majority of revenues in the U.S. and mobile music currently representing the majority of digital revenues outside of the U.S, especially in Europe and Asia. However, digital music is in the early stages of growth and we expect these proportions to change as the roll-out of new technologies continues. As an owner of musical content, we believe we are well positioned to take advantage of growth in digital distribution and emerging technologies to maximize the value of our assets.

Downloads/Subscription Services

Digital sales of our music content consist primarily of music originally accessed over the Internet or wirelessly through digital download or subscription models, which can then be transferred to a portable music player. We enter into agreements with numerous partners, such as iTunes, MusicNet, musicmatch, Rhapsody, Yahoo! and MSN to provide our content for sale through their music service offerings. Our agreements generally last one to two years. We believe that the short-term nature of our contracts enables us to maintain the flexibility that we need given the infancy of the digital business models. We are also exploring other opportunities to generate revenues through new uses of our content through these developing distribution channels. For example, we have over 20 years of music videos that we have yet to significantly monetize as well as unexploited album art, lyric, and B-side tracks that that have never been physically released.

Mobile

Mobile sales of our music content consists primarily of ringtones, ringback tones and mastertones (a ringtone made from recording by the original artist). We expect the range of products to expand as new technologies continue to be rolled out and to include full track music and full music video downloads, as well as other new businesses from these emerging distribution platforms. We enter into agreements with mobile carriers such as Sprint, Verizon, and France Telecom to provide our content for sale though their music offerings. Our contracts generally last one to two years.

Competition

In both recorded music and music publishing we compete based on price (to retailers in recorded music and to various end users in music publishing), on marketing and promotion (including both how we allocate our marketing and promotion resources as well as how much we spend on a dollar basis) and on recording artist and songwriter signings. We believe we currently compete favorably in these areas. However, there is a threat that the change to the competitive landscape caused by the Universal and Sony BMG duopoly could increase the costs of artist signings and the costs of marketing and promoting records to our detriment. See "*Industry Overview—Recorded Music*" and "*Industry Overview—Music Publishing.*"

Our Recorded Music business is also dependent on technological development, including access to, selection and viability of new technologies, and is subject to potential pressure from competitors as a result of their technological developments. In recent years, due to the growth in piracy, we have been forced to compete with illegal channels such as unauthorized Internet peer-to-peer file-sharing and downloading and industrial duplication. See "*Industry Overview—Piracy.*" Additionally, we compete, to a lesser extent, with alternative forms of entertainment such as motion pictures on home devices (e.g., VHS and DVD) or at the box office and with videogames for disposable consumer income.

Intellectual Property

Copyrights

Our business, like that of other companies involved in music publishing and recorded music, rests on our ability to maintain rights in musical works and recordings through copyright protection. In the U.S., copyright protection for works created as "works made for hire" (e.g., works of employees or specially-commissioned works) after January 1, 1978 lasts for 95 years from first publication or 120 years from creation, whichever expires first. The period of copyright protection for musical compositions and sound recordings that are not "works made for hire" lasts for the life of the author plus 70 years for works created on or after January 1, 1978. U.S. works created prior to January 1, 1978 generally enjoy a total copyright life of 95 years, subject to compliance with certain statutory provisions including notice and renewal. In the U.S., sound recordings created prior to February 15, 1972 are not subject to copyright protection but are protected by common law rights or state statutes, where applicable. Copyright in the European Union has recently been harmonized such that the period of copyright protection for musical compositions in all Member States lasts for the life of the author plus 70 years. In certain European Union countries, such as the U.K., the period of protection for musical compositions was recently extended from 50 years to 70 years, which has restored copyright protection in certain compositions in which our rights lapsed. In the European Union, the term of copyright for sound recordings lasts for 50 years from the date of release.

We are largely dependent on legislation in each territory to protect our rights against unauthorized reproduction, distribution, public performance or rental. In all territories where we operate, our products receive some degree of copyright protection, although the period of protection varies widely. In a number of developing countries, the protection of copyright remains inadequate. The U.S. enacted the Digital Millennium Copyright Act of 1998, creating a powerful framework for the protection of copyrights covering musical compositions and recordings in the digital world.

The potential growth of new delivery technologies, such as digital broadcasting, the Internet and entertainment-on-demand has focused attention on the need for new legislation that will adequately protect the rights of producers. We actively lobby in favor of industry efforts to increase copyright protection and support the efforts of organizations such as the World Intellectual Property Organization ("WIPO").

In December 1996, two global copyright treaties, the WIPO Copyright Treaty and the WIPO Performances and Phonograms Treaty, were signed securing the basic legal framework for the international music industry to trade and invest in online music businesses. The WIPO treaties have been ratified by the requisite number of countries, including the U.S.

The European Union has implemented these treaties through the European Copyright Directive, which was adopted by the EU in 2001. Legislation implementing the Directive in each of the member states is underway. The Directive harmonizes copyright laws across Europe and extends substantial protection for copyrights online. The European Union has also put forward legislation aimed at assuring cross border coordination of the enforcement of laws related to counterfeit goods, including musical recordings.

Trademarks

An important part of our business is our trademarks. Our major trademarks are registered in every country where we believe the protection of these trademarks is important for our business. Our major trademarks include Atlantic, Elektra, Sire, Reprise and Warner/Chappell. We use certain trademarks pursuant to royalty-free license agreements. The duration of the license relating to the WARNER and WARNER MUSIC marks and a "W" logo is perpetual. The duration of the license relating to the WARNER BROS. RECORDS mark and WB & Shield designs is fifteen years from February 29, 2004. Each of the licenses may be terminated under certain limited circumstances, which include material breaches of the agreement, certain events of insolvency, and certain change of control events if we were to become controlled by a major filmed entertainment company. We actively monitor and protect against activities that might infringe, dilute, or otherwise harm our trademarks.

Joint Ventures

We have entered into joint venture arrangements pursuant to which we or our various subsidiary companies manufacture, distribute and market (in most cases, domestically and internationally) recordings owned by the joint ventures. An example of these arrangements is Bad Boy Records, a joint venture between us and Sean "Diddy" Combs.

Employees

As of September 30, 2005, we employed approximately 4,000 persons worldwide, including temporary and part-time employees. None of our employees in the U.S. are subject to collective bargaining agreements, although certain employees in our non-domestic companies are covered by national labor agreements. We believe that our relationship with our employees is good.

Environmental Matters

Our wholly and partially owned pick, pack and ship facilities throughout the world, which are not a significant part of our business, are subject to laws and regulations and international agreements governing the protection of the environment, natural resources, human health and safety and the use, management and disposal of hazardous substances. In particular, our operations are subject to stringent requirements for packaging content and recycling, air and water emissions, and waste management. We believe that we comply substantially with all applicable environmental requirements. Although the costs of maintaining such compliance have not materially affected us to date, we cannot predict the costs of complying with requirements that may be imposed in the future. In connection with some of our existing facilities, we also have been, and may become again, responsible for the costs of investigating or cleaning up contaminated properties. Such costs or related third-party personal injury or property damage claims could have a material adverse affect on our business, results of operations or financial condition.

Financial Information About Segments and Foreign and Domestic Operations

Financial and other information by segment and relating to foreign and domestic operations for each of the last three fiscal years is set forth in Note 23 to the Consolidated and Combined Audited Financial Statements.

INDUSTRY OVERVIEW

Recorded Music

Recorded music is one of the primary mediums of entertainment for consumers worldwide and in calendar 2004, generated $33.6 billion in retail sales.

Recorded music companies play an integral role in virtually all aspects of the music value chain, from discovering and developing talent to producing albums and promoting artists and their product. Revenues are generated through the marketing, sale and licensing of recordings in various physical and digital formats.

The major recorded music companies have built significant recorded music catalogs, which are long-lived assets that are exploited year after year. The sale of catalog material is typically more profitable than that of new releases, given lower development costs and more limited marketing costs. In first three quarters of calendar 2005, 38% of all U.S. physical unit sales were from recordings more than 18-months old, and 25% were from recordings more than three years old. Distribution has been largely stable for the past eight years.

The recorded music industry is highly competitive based on consumer preferences, and is rapidly changing. At its core, the recorded music business relies on the exploitation of artistic talent. As such, competitive strength is predicated upon the ability to continually develop and market new artists whose work gains commercial acceptance. In 2004, the four largest players were Universal, Sony BMG, EMI and WMG, which accounted for approximately 72% of worldwide recorded music sales in 2004. There are many mid-sized and smaller players in

the industry that accounted for the remaining 28%, including independent music companies. Universal was the market leader with a 26% global market share in 2004, followed by Sony BMG with a 22% share. EMI and WMG held a 13% and 11% share of global music sales in 2004, respectively. While market shares change moderately year-to-year, none of these players have gained or lost more than 3 percentage points of share in the last 5 years through 2004 (taking into account combined shares of Sony and BMG for years prior to the formation of Sony BMG in 2004).

The top five territories (U.S., Japan, U.K., Germany and France) accounted for 73% of the recorded music market in 2004. The U.S., which is the most significant exporter of music, is also the largest end-market, constituting 36% of total 2004 recorded music sales. In addition the U.S. and Japan are largely local music markets, with 93% and 72% of their 2004 sales consisting of domestic repertoire, respectively. In contrast, the U.K, German and French markets are made up of a higher percentage of international sales, with domestic repertoire constituting only 51%, 49% and 63% of these markets, respectively.

There has been a major shift in distribution of recorded music from specialty shops towards mass-market and online retailers. Record stores' share of U.S. physical music sales has declined from 53% in 1994 to 33% in 2004. Over the course of the last decade, mass-market and other stores' share grew from 27% to 54%. Online digital distribution currently represents a small portion of overall sales, but is expected to experience significant growth. In terms of genre, rock remains the most popular style of music, representing 24% of 2004 U.S. unit sales, although genres such as rap, hip-hop and Latin music have become increasingly popular.

From 1990 to 1999, the U.S. recorded music industry grew at a compound annual growth rate of 7.6%, twice the rate of total entertainment spending. This growth was driven by demand for music, the replacement of LPs and cassettes with CDs, price increases and strong economic growth and was largely paralleled around the world. The industry began experiencing negative growth rates in 1999, on a global basis, primarily driven by an increase in digital piracy. Other drivers of this decline are the overall recessionary economic environment, bankruptcies of record retailers and wholesalers, growing competition for consumer discretionary spending and retail shelf space, and the maturation of the CD format, which has slowed the historical growth pattern of recorded music sales. Since that time, annual dollar sales of physical music product in the U.S. are estimated to have declined at a CAGR of 4%, although there was a 2.5% year-over-year increase recorded in 2004 (through November 20, 2005 U.S. recorded music sales (excluding sales of digital tracks) are down approximately 7.6% year-over-year, however). Similar declines have occurred in international markets, with the extent of declines driven primarily by differing penetration levels of piracy-enabling technologies, such as broadband Internet access and CD-R technology, and economic conditions.

Notwithstanding these factors, we believe that the music industry could improve based on the recent mobilization of the industry as a whole against piracy and the development of legitimate online music distribution channels. In addition, continued recovery of the world economy and improved consumer expenditures can drive growth in the recorded music industry.

Piracy

One of the industry's biggest challenges is combating piracy. Music piracy exists in two primary forms: digital (which includes illegal downloading and CD-R piracy) and industrial:

- *Digital piracy* has grown dramatically in the last five years, enabled by the increasing penetration of broadband Internet access and the ubiquity of powerful microprocessors, fast optical drives (particularly with writable media, such as CD-R) and large inexpensive disk storage in personal computers. The combination of these technologies has allowed consumers to easily, flawlessly and almost instantaneously make high-quality copies of music using a home computer by "ripping" or converting musical content from CDs into digital files, stored on local disks. These digital files can then be distributed for free over the Internet through anonymous peer-to-peer file sharing networks such as

Limewire, WinMX and KaZaA ("illegal downloading"). Alternatively, these files can be burned onto multiple CDs for physical distribution ("CD-R piracy").

- *Industrial piracy* (also called counterfeiting or physical piracy) involves mass-production of illegal CDs and cassettes in factories. This form of piracy is largely concentrated in developing regions, and has existed for more than a decade. The sale of legitimate recorded music in these developing territories is limited by the dominance of pirated products, which are sold at substantially lower prices than legitimate products. IFPI states that industrial pirated physical music products totaled 1.5 billion units in 2004. IFPI also believes that industrial piracy is most prevalent in Brazil, China, India, Indonesia, Mexico, Pakistan, Paraguay, Russia, Spain and Ukraine.

In 2003, the industry launched an intensive campaign to limit piracy that focused on four key initiatives:

- *Technological:* The technological measures against piracy are geared towards degrading the illegal file-sharing process and tracking providers and consumers of pirated music. These measures include spoofing, watermarking, copy protection, the use of automated webcrawlers and access restrictions. In addition, the industry continues to experiment with new technologies such as DualDisc and DVD-Audio that contain more robust encryption protection.

- *Educational:* Led by RIAA and IFPI, the industry has launched an aggressive campaign of consumer education designed to spread awareness of the illegality of various forms of piracy through aggressive print and television advertisements. Recent surveys confirm the increased consumer awareness of the illegality of piracy. In January 2003, 33% of Americans 10 years of age and older were aware that it is illegal to download copyrighted music for free. By August 2003, that number had risen to 61% and during the latter part of 2004, awareness among Americans 13 years of age and older was measured at 68%.

- *Legal:* In conjunction with its educational efforts, the industry has also begun to take aggressive legal action against file-sharers and is continuing to fight industrial pirates. These actions include civil lawsuits in the U.S. and Europe against individual pirates, arrests of pirates in Japan and raids against file-sharing services in Australia. U.S. lawsuits have largely targeted individuals who share large quantities of illegal music content. RIAA has announced its plans to continue these lawsuits in the U.S. IFPI has brought similar actions in Argentina, Austria, Canada, Denmark, Finland, France, Germany, Iceland, Ireland, Italy, Hong Kong, Netherlands, Singapore, Sweden, Switzerland and the U.K. and it may pursue similar actions in other countries. A number of recent court decisions, including the U.S. Supreme Court decision in Grokster and the Federal Court of Australia's ruling in a case involving KaZaA, have also held that one who distributes a device, such as P2P software, with the object of promoting its use to infringe copyright can be liable for the resulting acts of infringement by third parties using the device regardless of the of the lawful uses of the device.

- *Development of online and mobile alternatives:* We believe that the development and success of legitimate online music channels will be an important driver of recorded music sales going forward, as digital sales represent both an incremental revenue stream and a potential inhibitor of piracy. The music industry has been encouraged by the recent proliferation and early success of legitimate online music distribution options. We believe that these legitimate online distribution channels offer several advantages to illegal peer-to-peer sites, including greater ease of use, higher quality and more consistent music product, faster downloading, better search capabilities, and seamless integration with portable digital music players. For example, legitimate online operations such as Apple's iTunes, MusicNet, musicmatch and Rhapsody have been launched since the beginning of 2003 and offer a variety of models, including per-track pricing, per-album pricing and monthly subscriptions. Already, there are more than 300 legal online music sites providing alternatives to illegal file-sharing in markets around the world.

These efforts are incremental to the longstanding push by organizations such as IFPI to curb industrial piracy around the world. In addition to these actions, the music industry is increasingly coordinating with other similarly impacted industries (such as software and filmed entertainment) to combat piracy.

We believe these actions are beginning to have a positive effect. A survey as of May 2005 conducted by The NPD Group, a market research firm, shows that about one-third of Americans aged 13 or older who had ever downloaded music from a file-sharing service stopped using such file-sharing services over the past year, and an additional 27% reduced their downloading activity.

Music Publishing

Background

Music publishing involves the acquisition of rights to, and licensing of, musical compositions (as opposed to recordings) from songwriters, composers or other rightsholders. Music publishing revenues are derived from four main royalty sources: Mechanical, Performance, Synchronization and Other.

In the U.S., mechanical royalties are collected directly by music publishers from recorded music companies or via The Harry Fox Agency, a non-exclusive licensing agent affiliated with NMPA, while outside the U.S., performing rights organizations and collection societies perform this function. Once mechanical royalties reach the publisher (either directly from record companies or from collection societies), percentages of those royalties are paid to any co-owners of the copyright in the composition and to the writer(s) and composer(s) of the composition. Mechanical royalties are paid at a penny rate of 8.5 cents per song per unit in the U.S. (although recording agreements sometimes contain "controlled composition" provisions pursuant to which artist/songwriters license their rights to their record companies at as little as 75% of this rate) and as a percentage of wholesale price in most other territories. In the U.S., these rates are set pursuant to industry negotiations contemplated by the U.S. Copyright Act and are currently increased at two-year intervals. For example, on January 1, 2004, this rate went from 8 cents per song to 8.5 cents per song. On January 1, 2006, this rate will increase again to 9.1 cents per song. Recordings in excess of 5 minutes attract a higher rate. In international markets, these rates are determined by multi-year collective bargaining agreements.

Throughout the world, performance royalties are typically collected on behalf of publishers and songwriters by performance rights organizations and collection societies. Key performing rights organizations and collection societies include: The American Society of Composers, Authors and Publishers ("ASCAP"), SESAC and Broadcast Music, Inc. ("BMI") in the U.S.; Mechanical-Copyright Protection Society and The Performing Right Society ("MCPS-PRS Alliance") in the U.K.; The German Copyright Society ("GEMA") in Germany and the Japanese Society for Rights of Authors, Composers and Publishers ("JASRAC") in Japan. The societies pay a percentage (which is set in each country) of the performance royalties to the copyright owner(s) or administrators (*i.e.* , the publisher(s)), and a percentage directly to the songwriter(s), of the composition. Thus, the publisher generally retains the performance royalties it receives other than any amounts attributable to co-publishers.

The worldwide music publishing market was estimated to have generated approximately $3.6 billion in revenues in 2004 according to figures contained in the March 2, 2005 issue of *Music & Copyright* . We estimate that mechanical royalties are approximately 30% of 2002 industry revenues; performance royalties, 33%; synchronization, 13%; and other, 23%. Geographically, North America is the largest market representing approximately 40% of the global publishing market.

The top five music publishers collectively account for over 65% of the market. Based on *Music & Copyright's* estimates, EMI Music Publishing ("EMI Publishing") and WMG (Warner/Chappell) are the market leaders in music publishing, holding 16.3% and 16.0% shares of the market in 2004, respectively. They are followed by BMG at 13.8%, Universal at 12.5% and Sony/ATV Music Publishing LLC ("Sony/ATV") at 7.4%. Independent music publishers represent the balance of the market, as well as many individual songwriters who publish their own works.

The music publishing market has proven to be more resilient than the recorded music market in recent years as performance, synchronization and other revenue streams are largely unaffected by piracy, and are benefiting

from additional sources of income from digital exploitation of music in downloads and mobile phone ringtones. Trends in music publishing vary by royalty source:

- *Mechanical:* Although the decline in the recorded music market has begun to have an impact on mechanical royalties, this decline has been partly offset by the regular and predictable statutory increases in the mechanical royalty rate in the U.S. (including an increase from 8 cents to 8.5 cents per song in January 2004, and a further increase from 8.5 cents to 9.1 cents per song to occur in January 2006), the increasing efficiency of local collection societies worldwide and the growth of new revenue sources such as mobile phone ringtones and legitimate Internet and wireless downloads.

- *Performance:* According to an April 2004 report from Enders Analysis, performance royalties experienced steady growth from 1999 to 2001. Continued growth is expected, largely driven by television, live performance and online radio streaming and advertising royalties.

- *Synchronization:* We believe synchronization revenues have experienced strong growth in recent years and will continue to do so, benefiting from the proliferation of media channels, a recovery in advertising, robust videogames sales and growing DVD film sales/rentals.

- *Other:* According to Enders Analysis, print revenues grew steadily from 1999 to 2001. Continued growth in this category is expected as well, as more people can afford musical instruments and lessons and online sheet music sales drive incremental revenues.

In addition, major publishers have the opportunity to generate significant value by the acquisition of small publishers by extracting cost savings (as acquired libraries can be administered with little or no incremental cost) and by increasing revenues through more aggressive marketing efforts.

WHERE YOU CAN FIND MORE INFORMATION

We are required to file annual, quarterly and current reports, proxy statements and other information with the SEC. These filings are not deemed to be incorporated by reference in this report. You may read and copy any documents filed by us at the Public Reference Section of the SEC, 450 Fifth Street, N.W., Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Our filings with the SEC are also available to the public through the SEC's website at *http://www.sec.gov*. Our common stock is listed on the NYSE under the symbol "WMG". You can inspect and copy reports, proxy statements and other information about us at the NYSE's offices at 20 Broad Street, New York, New York 10005. We also maintain an Internet site at *www.wmg.com*. We make available on our Internet website free of charge our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K as soon as practicable after we electronically file such reports with the SEC. In addition, copies of our (i) Corporate Governance Guidelines, (ii) charters for the Audit Committee, Compensation Committee and Executive, Nominating and Corporate Governance Committee and (iii) Code of Conduct which is applicable for all or our employees including our principal executive, financial and accounting officers, are available at our Internet site under "Investor Relations—Corporate Governance." Copies will be provided to any stockholder upon written request to Investor Relations, 75 Rockefeller Plaza, New York, New York 10019, via electronic mail at *Investor.Relations@wmg.com* or by contacting Investor Relations at (212) 275-2000. Our website and the information posted on it or connected to it shall not be deemed to be incorporated by reference into this report.

ITEM 1A. EXECUTIVE OFFICERS OF THE REGISTRANT

The following table sets forth information as to our executive officers as of November 4, 2005, together with their positions and ages.

Name	Age	Position
Edgar Bronfman, Jr.	50	Chairman of the Board and CEO
Lyor Cohen	46	Chairman and CEO, U.S. Recorded Music
Paul-René Albertini	46	Chairman and CEO, Warner Music International
Richard Blackstone	45	Chairman and CEO, Warner/Chappell Music, Inc.
Michael D. Fleisher	40	Executive Vice President and Chief Financial Officer
David H. Johnson	58	Executive Vice President and General Counsel
Caroline Stockdale	42	Executive Vice President, Global Human Resources
Alejandro Zubillaga	37	Executive Vice President, Digital Strategy and Business Development

Our executive officers are appointed by, and serve at the discretion of, the Board of Directors. Each executive officer is an employee of Warner Music Group or one of its subsidiaries. Mr. Zubillaga is the brother-in-law of Mr. Bronfman. There are no other family relationships among any executive officers of Warner Music Group. The following information provides a brief description of the business experience of each of our executive officers.

Edgar Bronfman, Jr. has served as our Chairman of the Board and CEO since March 1, 2004. Before joining Warner Music Group, Mr. Bronfman served as Chairman and CEO of Lexa Partners LLC, a management venture capital group based in New York City. Prior to Lexa Partners, Mr. Bronfman was appointed Executive Vice Chairman of Vivendi Universal in December 2000. He resigned from his position as an officer and executive of Vivendi Universal on March 31, 2002, and resigned as Vice Chairman of Vivendi Universal's Board of Directors on December 2, 2003. Prior to the December 2000 formation of Vivendi Universal, Mr. Bronfman was President and CEO of The Seagram Company Ltd., a post he held since June 1994. During his tenure as the CEO of Seagram, he consummated $85 billion in transactions and transformed the company into one of the world's leading media and communications companies. From 1989 until June 1994, Mr. Bronfman served as President and COO of Seagram. Between 1982 and 1989, he held a series of senior executive positions for The Seagram Company Ltd. in the U.S. and in Europe.

Lyor Cohen has served as the Chairman and CEO of our U.S. Recorded Music operations since March 1, 2004. From 2002 to 2004, Mr. Cohen was the Chairman and CEO of Universal Music Group's Island Def Jam Music Group. Mr. Cohen served as President of Def Jam from 1988 to 2002. Previously, Mr. Cohen served in various capacities at Rush Management, a hip-hop management company, which he founded with partner Russell Simmons. Mr. Cohen is widely credited with expanding Island Def Jam beyond its hip-hop roots to include a wider range of musical genres.

Paul-René Albertini has served as President of Warner Music International since 2002 and currently leads Warner Music International, our international division, as Chairman and CEO. From December 2000 until 2002, Mr. Albertini served as President of Warner Music Europe. He joined Warner Music International from Sony Music Entertainment Europe where he held the post of Executive Vice President from 1999. Prior to that he served as President and CEO Sony Music France between 1994 and 1999. In 1991 he became CEO of PolyGram Disques France. In 1983, Mr. Albertini joined PolyGram as International Label Manager before becoming Marketing Director for Barclay Records. He was named Director of Marketing and Promotion for Phonogram in 1989, and was appointed Managing Director Phonogram France. Mr. Albetini graduated from the Institut Superieur de Gestion in Paris in 1982 and attended the International Senior Management Program from Harvard Business School in 1993.

Richard Blackstone has served as Chairman and CEO of Warner/Chappell Music, Inc. since May 28, 2005. Prior to joining Warner Music Group, Mr. Blackstone was the president of Zomba Music Publishing. Mr. Blackstone joined

Zomba in 1989 as Director of Business Affairs, and was later promoted to the dual role of Head of Creative and Head of Business Affairs. Following the purchase of Zomba by BMG Music in 2002 he was named President of Zomba Music Publishing, and was given oversight responsibility for Brentwood Benson Music Publishing.

Michael D. Fleisher has served as our Executive Vice President and Chief Financial Officer since January 1, 2005. Prior to joining Warner Music Group, Mr. Fleisher was Chairman and Chief Executive Officer of Gartner, Inc. Mr. Fleisher joined Gartner in 1993 and served in several roles including Chief Financial Officer prior to being named CEO in 1999. Previous to Gartner, he was at Bain Capital. Mr. Fleisher serves on the Board of Ameritrade.

David H. Johnson has served as Executive Vice President and General Counsel since 1999. Prior to joining Warner Music Inc., Mr. Johnson spent nine years as Senior Vice President and General Counsel for Sony Music Entertainment. He also held several posts at CBS and was an associate in the law firm Mayer, Nussbaum, Katz & Baker. Mr. Johnson received a B.A. in political science from Yale University, a J.D. from the University of Pennsylvania Law School and an L.L.M. from New York University School of Law.

Caroline Stockdale has served as Executive Vice President, Global Human Resources since August 2005. Prior to joining Warner Music Group, Ms. Stockdale was Senior Vice President, Relationship Leader Human Resources, at American Express Financial Advisors/Global Financial Services since 2002. Before joining American Express Financial Advisors in 2002, Ms. Stockdale held a variety of human resources leadership positions at General Electric (GE) Capital Corporation in Europe and the United States beginning in 1997, including Executive Vice President and Global Human Resources Leader at GE Capital Corporation's Aviation Services division. Ms. Stockdale qualified as a chartered accountant and graduated with a B.A. Honors degree from the University of Sheffield in Sheffield, England.

Alejandro (Alex) Zubillaga has served as Executive Vice President, Digital Strategy and Business Development since August 2005. Prior to being designated as Executive Vice President, Digital Strategy and Business Development, Mr. Zubillaga held various positions with Warner Music Group since joining the company in March 2004, including Senior Vice President, Digital Strategy and Business Development and Vice President, Office of the Chairman. Prior to joining Warner Music Group, Mr. Zubillaga served as managing director and co-founder of Lexa Partners LLC. Previously, Mr. Zubillaga was founder and managing partner of E-Quest Partners. Prior to that, Mr. Zubillaga served as founder, chairman and chief executive officer of NETUNO. Mr. Zubillaga graduated from Babson College with a degree in Business Administration.

ITEM 2. PROPERTIES

We own distribution, studio and office facilities and also lease certain facilities in the ordinary course of business. Our executive offices are located at 75 Rockefeller Plaza, New York, NY 10019. In addition, we have a ten-year lease ending on July 31, 2014 for our headquarters at 75 Rockefeller Plaza, New York, New York 10019. We also have a seventeen-year lease ending on December 31, 2020, for office space in a building located at 3400 West Olive Avenue, Burbank, California 91505, used primarily by our Recorded Music business, and an approximately sixteen year lease ending on June 30, 2012 for office space at 1290 Avenue of the Americas, New York, New York 10104, used primarily by our Recorded Music business. We consider our properties adequate for our current needs.

ITEM 3. LEGAL PROCEEDINGS

On September 7, 2004, November 22, 2004 and March 31, 2005, Eliot Spitzer, the Attorney General of the State of New York, served us with requests for information in the form of subpoenas duces tecum in connection with an industry-wide investigation of the relationship between music companies and radio stations, including the use of independent promoters and accounting for any such payments. The investigation was pursuant to New York Executive Law §63(12) and New York General Business Law §349, both of which are consumer fraud statutes. On November 22, 2005 we reached a settlement with the Attorney General in connection with this

investigation. As part of such settlement, we agreed to make $5 million in charitable payments and to abide by a list of permissible and impermissible promotional activities. On July 25, 2005, Sony BMG reached a settlement with the Attorney General in connection with the same industry-wide investigation. Subsequent to the settlement by Sony BMG, TSR Records, an independent label, filed an antitrust suit against Sony BMG alleging that the label's radio promotion activities are anticompetitive. While it is too soon to predict the outcome of these recent developments on us, any litigation we may become involved in as a result of our settlement with the Attorney General, regardless of the merits of the claim, could be costly and would divert the time and resources of management.

We are involved in litigation arising in the normal course of our business. Management does not believe that any legal proceedings pending against us will have, individually, or in the aggregate, a material adverse effect on our business. However, we cannot predict with certainty the outcome of any litigation or the potential for future litigation. Regardless of the outcome, litigation can have an adverse impact on us, including our brand value, because of defense costs, diversion of management resources and other factors.

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

No matter was submitted to a vote of security holders of Warner Music Group Corp. during the fourth quarter of 2005.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Warner Music Group Corp.'s common stock was listed on the New York Stock Exchange under the symbol "WMG" on May 10, 2005. Prior to that time, there was no public market for our common stock. The following table presents the high and low closing prices for the common stock on the New York Stock Exchange during the periods indicated and the dividends declared during such periods:

	High	Low	Dividends Paid
2005:			
Third Quarter (commencing May 10, 2005)	$ 16.95	$ 15.23	—
Fourth Quarter	$ 18.71	$ 14.75	—
2006:			
First Quarter (ending November 24, 2005)	$ 18.95	$ 15.25	$ 0.13

As of November 24, 2005 there were approximately 35 registered holders of record for the common stock and 148,460,622.724 shares outstanding. Because many of our shares of common stock are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these record holders. The closing price of the common stock on the New York Stock Exchange on November 24, 2005, was 18.05.

Dividend Policy

On October 3, 2005 the Board of Directors of Warner Music Group declared a quarterly dividend of $0.13 per share of common stock, representing an aggregate quarterly dividend of approximately $19.3 million (based on outstanding shares of 148,455,312.724 as of September 30, 2005). The dividend was paid November 23, 2005, to stockholders of record as of the close of business on October 24, 2005. The portion of the dividend with respect to unvested restricted stock of approximately $1 million will be paid at such time as such shares become vested.

As previously announced, we intend to continue paying quarterly dividends on our common stock outstanding in an amount not to exceed $80 million per year in the aggregate. The Board will evaluate whether to pay a dividend on a quarterly basis and will base its decisions on, among other things, our results of operations, cash requirements, financial condition, contractual restrictions and other factors the Board of Directors may deem relevant.

The amounts available to us to pay further cash dividends will be restricted by our subsidiary WMG Acquisition Corp.'s senior secured credit agreement and the indentures governing our outstanding notes, including the indenture governing WMG Holdings Corp.'s outstanding 9.5% Senior Discount Notes due 2014 and the indenture governing WMG Acquisition Corp.'s 7 1/8 % Senior Subordinated Dollar Notes due 2014 and 8 1/8 % Senior Subordinated Sterling Notes due 2014. Under Acquisition Corp.'s senior secured credit agreement, generally neither Holdings nor Holdings' subsidiaries may pay dividends or otherwise transfer their assets to us. However, Acquisition Corp.'s senior secured credit agreement permits such restricted payments in an amount not to exceed $10.0 million, subject to increase up to $50.0 million if the leverage ratio is less than 3.5 to 1, and subject to additional increase in an amount equal to 50% of excess cash flow that is not otherwise applied pursuant to Acquisition Corp.'s senior secured credit agreement and allows distributions not in excess of $90 million in any fiscal year to be applied to pay regular quarterly cash dividends to holders of our common stock. The indentures governing the Holdings Notes and the Acquisition Corp. Notes also limit the ability of Holdings, Acquisition Corp. and their subsidiaries to pay dividends to us. Under such indentures, generally our subsidiaries may pay dividends or make other restricted payments depending on a formula based on 50% of consolidated net income. In addition, Acquisition Corp. may also make such restricted payments if, on a pro forma basis after giving effect to any such payment, it has a net indebtedness to adjusted EBITDA ratio of no greater than 3.75 to 1.0 and a net senior indebtedness to adjusted EBITDA ratio of no greater than 2.5 to 1.0, and Holdings may make such restricted payments if, on a pro forma basis after giving effect to any such payment, it has a net indebtedness to adjusted EBITDA ratio of no greater than 4.25 to 1.0. Acquisition Corp. and Holdings may also make restricted payments under the indentures of up to $45.0 million and $75.0 million, respectively, without regard to any such provisions. The Holdings indenture permits Holdings to dividend up to 6% per annum from proceeds of our initial public offering received by Holdings. See "Management's Discussion and Analysis of Financial Condition and Results of Operations—Financial Condition and Liquidity—Liquidity."

Use of Proceeds from Sales of Registered Securities

On May 10, 2005, we registered 37,490,000 shares of our common stock for an aggregate offering price of $897,760,000 in our initial public offering. On May 13, 2005 we closed the sale by us of a total of 32,600,000 shares of our common stock in our initial common stock offering at a price of $17.00 per share in a firm commitment underwritten initial public offering. This offering was effected pursuant to a Registration Statement on Form S-1 (File No. 333-123249), which the Securities and Exchange Commission declared effective on May 10, 2005. Goldman, Sachs & Co. and Morgan Stanley & Co. Inc. were the joint global coordinators and, together with Lehman Brothers Inc. and Deutsche Bank Securities Inc., served as joint book-running managers in the offering. Banc of America Securities LLC and Citigroup Global Markets Inc. acted as joint lead managers in the offering. Of the $554.2 million of gross proceeds raised in the offering:

- approximately $26.3 million was paid to the underwriters in connection with the underwriting discount;
- approximately $10.9 million was used in connection with offering expenses, printing fees, listing fees, filing fees, accounting fees and legal fees; and
- approximately $517 million was used in connection with the redemption of 100% of WMG Holdings Corp.'s Floating Rate Senior Notes due 2011 and Floating Rate Senior PIK Notes due 2014 and 35% of the aggregate principal amount of its outstanding 9.5% Senior Discount Notes due 2014 on June 15, 2005.

Equity Compensation Plan Information

The following table provides information as of September 30, 2005 with respect to shares of our common stock that may be issued under our existing equity compensation plans.

Plan Category	Number of Securities to be Issued upon Exercise of Outstanding Options	Weighted Exercise Price of Outstanding Options	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (excluding securities reflected in first column)
Equity Compensation Plans Approved by Stockholders (1)	6,383,629	$ 2.90	2,089,420

(1) Consists of the 2005 Omnibus Stock Plan, as well as individual LTIP and individual stock option agreements.

LTIP and Individual Stock Option Agreements

In 2004, the Company's board of directors approved a form of LTIP stock option agreement for grants of options to eligible individuals. Eligible individuals include any employee, director or consultant of the Company or any of its affiliates, or any other entity designated by Warner Music Group's board of directors in which the Company has an interest, who is selected by the Company's compensation committee to receive an award. The board authorized the granting of options to purchase up to 1,355,066 shares of our common stock pursuant to the LTIP program. The Company has granted options and may grant additional stock options under the LTIP stock option agreements to certain members of our current or future management. The board also approved the granting of options to purchase 3,701,850 shares of our common stock under stock option agreements with certain members of our management. Individual option agreements and options granted under the LTIP program generally will have a 10-year term and the exercise price will equal at least 100% of the fair market value on the date of the grant. With respect to each option granted pursuant to individual option agreements or a LTIP stock option agreement, one-third of the shares covered by the option generally vest and become exercisable in four equal installments on the day prior to each of first through fourth anniversaries of the effective date of the LTIP stock option agreement, subject to the employee's continued employment. Two-thirds of the shares covered by the option generally vest and become exercisable based on the occurrence of both a service condition (which is the same as the service condition described with respect to the service-based portion of the option) and a performance condition. The performance condition is met if, following an initial public offering or certain other events (including a change in control), a specified investment return is achieved by the investors (one-half of such shares require one return level and the other one-half of such shares require a different return level). The performance-based portion of the option also vests, subject to the employee's continued employment, on the day prior to the seventh anniversary of the effective date of the individual or LTIP stock option agreement and the service condition applicable to the performance-based option will be deemed to have been attained upon certain terminations following or in anticipation of a change in control.

2005 Omnibus Stock Plan

In May 2005, we adopted the 2005 Omnibus Stock Plan, or 2005 Plan, which authorized the granting of stock based awards to purchase up to 3,416,133 shares of our common stock. Under the 2005 Plan, our board of directors or the compensation committee will administer the plan and has the power to make awards, to determine when and to whom awards will be granted, the form of each award, the amount of each award, and any other terms or conditions of each award consistent with the terms of the 2005 Plan. Awards may be made to employees, directors and others as set forth in the 2005 Plan. The types of awards that may be granted include restricted and unrestricted stock, incentive and non-statutory stock options, stock appreciation rights, performance units and other stock based awards. Each award agreement specifies the number and type of award, together with any other terms and conditions as determined by the board of directors or the compensation committee in their sole discretion. Eligible employees include any employee who does not already have any other equity participation in our company. The Company has granted options and may grant additional awards under the 2005 Plan to certain member of our current or future management. Options granted generally have a 10-year term, the exercise price will equal at least 100% of the fair market value on the date of the grant and generally vest in four equal installments on the day prior to each of first through fourth anniversaries of the effective date of the stock option agreement, subject to the employee's continued employment.

ITEM 6. SELECTED FINANCIAL DATA

Our summary balance sheet data as of September 30, 2005 and 2004, and the statement of operations and other data for each of (i) the twelve-month fiscal year ended September 30, 2005; (ii) the seven months ended September 30, 2004, (iii) the three months ended February 29, 2004, and (iv) the twelve-month fiscal year ended November 30, 2003 have been derived from our audited financial statements included or incorporated by reference herein. Our summary statement of operations and other data for each of the ten months ended September 30, 2003 and the five months ended February 29, 2004 have been derived from our unaudited financial statements included or incorporated by reference herein. Our summary balance sheet data as of (i) February 29, 2004 (ii) November 30, 2003 and (iii) November 30, 2002 and the statement of operations and other data for the year ended November 30, 2002 are derived from our audited financial statements that are not included in this annual report. Our summary balance sheet data as of (i) September 30, 2003 and (ii) November 30, 2001 and the statement of operations and other data for the year ended November 30, 2001 are derived from our unaudited financial statements that are not included in this annual report.

The comparability of our historical financial data has been affected by a number of significant events and transactions. These include the acquisition of substantially all of our recorded music and music publishing businesses from Time Warner effective March 1, 2004 for approximately $2.6 billion (the "Acquisition") in 2004, a change in our fiscal year to September 30 from November 30, which was enacted in 2004, and the AOL Time Warner Merger in 2001. For all periods prior to the Acquisition, the recorded music and music publishing businesses formerly owned by Time Warner are referred to as "Old WMG" or the "Predecessor." For all periods subsequent to the Acquisition, the business is referred to as the "Company" or the "Successor." Due to the change in our year-end, financial information for 2004 reflects a shortened ten-month period ended September 30, 2004 and is separated into two pre-acquisition and post-acquisition periods as a result of the change in accounting basis that occurred relating to the Acquisition.

In connection with the Acquisition, a new accounting basis was established for the Company as of the acquisition date based upon an allocation of the purchase price to the underlying net assets acquired. As such, financial information for the twelve months ended September 30, 2004 is separated into pre-acquisition and post-acquisition periods as a result of the change in accounting basis that occurred relating to the Acquisition. That is for the twelve-month period ended September 30, 2004, we have presented our operating results and cash flows separately for the pre-acquisition five-month period ended February 29, 2004 and the post-acquisition, seven-month period ended September 30, 2004. The financial information for the ten months ended September 30, 2004 is separated into the pre-acquisition three-month period ended February 29, 2004 and the post-acquisition, seven-month period ended September 30, 2004.

The split presentation mentioned above is required under GAAP in situations when a change in accounting basis occurs. This is because the new accounting basis requires that the historical carrying value of assets acquired and liabilities assumed be adjusted to fair value, which may yield results that are not strictly comparable on a period-to-period basis due to the different, and sometimes higher, cost basis associated with the allocation of the purchase price.

We believe that this split presentation may impede the ability of users of our financial information to understand our operating and cash flow performance. Consequently, in order to enhance an analysis of our operating results and cash flows, we have presented our operating results and cash flows on a combined basis for the full ten-month period and twelve-month period ended September 30, 2004. The combined presentation for the twelve-month period ended September 30, 2004 simply represents the mathematical addition of the pre-acquisition, five-month period ended February 29, 2004 and the post-acquisition, seven-month period ended September 30, 2004 and the combined presentation for the ten-month period ended September 30, 2004 represents the mathematical addition of the pre-acquisition three-month period ended February 29, 2004 and the post-acquisition seven-month period ended September 30, 2004. These are not intended to represent what our operating results would have been had the Acquisition occurred at the beginning of the period.

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The following table sets forth our selected historical financial and other data as of the dates and for the periods indicated.

	Fiscal Years Ended November 30,			Ten Months Ended Sept. 30, 2003	Three Months Ended Feb. 29, 2004	Five Months Ended Feb. 29, 2004	Seven Months Ended Sept. 30, 2004	Ten Months Ended Sept. 30 2004	Twelve Months Ended Sept. 30 2004	Twelve Months Ended Sept. 30, 2005
	2001	2002	2003							
	Predecessor						Successor	Combined		Successor
	(unaudite	(audited)	(audited)	(unaudited)	(audited)	(unaudited)	(audited)	(unaudited)	(unaudited)	(audited)
	(in millions, except per share data)									
Statement of Operations Data:										
Revenues	$ 3,226	$ 3,290	$ 3,376	$ 2,487	$ 779	$ 1,668	$ 1,769	$ 2,548	$ 3,437	$ 3,502
Cost of revenues	(1,731)	(1,873)	(1,940)	(1,449)	(415)	(906)	(944)	(1,359)	(1,850)	(1,850)
Selling, general and administrative expenses	(1,402)	(1,282)	(1,286)	(995)	(319)	(610)	(677)	(996)	(1,287)	(1,301)
Impairment of goodwill and other intangible assets	—	(1,500)	(1,019)	—	—	(1,019)	—	(1,019)	—	—
Depreciation and amortization	(868)	(249)	(328)	(272)	(72)	(128)	(140)	(212)	(268)	(238)
Operating (loss) income	(766)	(1,542)	(1,158)	(197)	(11)	(972)	18	7	(954)	84
Interest expense, net	(34)	(23)	(5)	(5)	(2)	(2)	(80)	(82)	(82)	(182)
(Loss) income before cumulative effect of accounting change	(910)	(1,230)	(1,353)	(201)	(32)	(1,184)	(238)	(270)	(1,422)	(169)
Net (loss) income	$ (910)	$ (6,026)	$ (1,353)	$ (201)	$ (32)	$ (1,184)	$ (238)	$ (270)	$ (1,422)	$ (169)
Net income (loss) per common share (1):										
Basic	—	—	—	—	—	—	$ (2.21)	—	—	$ (1.40)
Diluted	—	—	—	—	—	—	$ (2.21)	—	—	$ (1.40)
Average common share (1):										
Basic	—	—	—	—	—	—	107.5	—	—	120.9
Diluted	—	—	—	—	—	—	107.5	—	—	120.9
Segment Data:										
Revenues:										
Recorded Music	$ 2,701	$ 2,752	$ 2,839	$ 2,039	$ 630	$ 1,430	$ 1,429	$ 2,059	$ 2,855	$ 2,924
Music Publishing	547	563	563	467	157	253	348	505	601	607
Corporate and eliminations	(22)	(25)	(26)	(19)	(8)	(15)	(8)	(16)	(21)	(29)
Total revenues	$ 3,226	$ 3,290	$ 3,376	$ 2,487	$ 779	$ 1,668	$ 1,769	$ 2,548	$ 3,437	$ 3,502
Operating income (loss):										
Recorded Music	$ (733)	$ (1,206)	$ (1,130)	$ (181)	$ (9)	$ (958)	$ 24	$ 15	$ (934)	$ 215
Music Publishing	23	(273)	23	19	17	21	53	70	74	82
Corporate and eliminations	(56)	(63)	(51)	(35)	(19)	(35)	(59)	(78)	(94)	(213)
Total operating income (loss)	$ (766)	$ (1,542)	$ (1,158)	$ (197)	$ (11)	$ (972)	$ 18	$ 7	$ (954)	$ 84
OIBDA (2):										
Recorded Music	$ 73	$ 173	$ 116	$ 8	$ 38	$ 146	$ 120	$ 158	$ 266	$ 380
Music Publishing	81	88	107	88	38	57	87	125	145	141
Corporate and eliminations	(52)	(54)	(34)	(21)	(15)	(28)	(49)	(64)	(77)	(199)
Total OIBDA (2)	$ 102	$ 207	$ 189	$ 75	$ 61	$ 175	$ 158	$ 219	$ 333	$ 322
Cash Flow Data:										
Cash flows provided by (used in):										
Operating activities	$ (122)	$ (13)	$ 278	$ 257	$ 321	$ 352	$ 86	$ 407	$ 438	$ 205
Investing activities	(175)	(365)	(65)	(73)	14	17	(2,663)	(2,649)	(2,646)	(54)
Financing activities	227	385	(121)	(151)	(10)	18	2,661	2,651	2,675	(416)
Capital expenditures	(91)	(88)	(51)	(30)	(3)	(24)	(15)	(18)	(39)	(30)

	Fiscal Years Ended November 30,					Five Months Ended Feb. 29, 2004	Seven Months Ended Sept. 30, 2004			
	2001	2002	2003	Ten Months Ended Sept. 30, 2003	Three Months Ended Feb. 29, 2004			Ten Months Ended Sept. 30 2004	Twelve Months Ended Sept. 30 2004	Twelve Months Ended Sept. 30, 2005
	Predecessor						Successor	Combined		Successor
	(unaudite	(audited)	(audited)	(unaudited)	(audited)	(unaudited)	(audited)	(unaudited	(unaudited)	(audited)
	(in millions, except per share data)									
Balance Sheet Data (at period end):										
Cash and equivalents	$ 34	$ 41	$ 144	$ 80	$ 471	$ 471	$ 555	$ 555	$ 555	$ 288
Total assets	17,642	15,679	4,484	5,255	4,560	4,560	5,090	5,090	5,090	4,498
Total debt (including current portion of long-term debt)	115	101	120	115	132	132	1,840	1,840	1,840	2,246
Shareholders' equity	14,388	3,001	1,587	2,673	1,691	1,691	280	280	280	89

(1) Net income (loss) per share is calculated by dividing net income (loss) by the weighted average common shares outstanding.

(2) We evaluate segment and consolidated performance based on several factors, of which the primary measure is operating income (loss) before non-cash depreciation of tangible assets, non-cash amortization of intangible assets and non-cash impairment charges to reduce the carrying value of goodwill and intangible assets (which we refer to as "OIBDA"). See "Use of OIBDA" under "Management's Discussion and Analysis of Financial Condition and Results of Operations". Note that OIBDA is different from Adjusted EBITDA as defined in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Financial Condition and Liquidity—Covenant Compliance", which is presented on a consolidated and combined basis therein as a covenant compliance measure. The following is a reconciliation of operating income, which is a GAAP measure of our operating results, to OIBDA.

Operating income (loss)	$ (766)	$ (1,542)	$ (1,158)	$ (197)	$ (11)	$ (972)	$ 18	$ 7	$ (954)	$ 84
Depreciation and amortization expense	868	249	328	272	72	128	140	212	268	238
Impairment of goodwill and other intangible assets	—	1,500	1,019	—	—	1,019	—	—	1,019	—
OIBDA	$ 102	$ 207	$ 189	$ 75	$ 61	$ 175	$ 158	$ 219	$ 333	$ 322

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our results of operations and financial condition includes periods prior to the consummation of our acquisition of substantially all of Time Warner Inc.'s recorded music and music publishing businesses and related financing (the "Transactions"). Accordingly, the discussion and analysis of operating results for the ten months and twelve months ended September 30, 2004 do not reflect the full impact that the Transactions have had on us, including significantly increased financing costs. You should read the following discussion of our results of operations and financial condition with the audited financial statements included elsewhere in this Annual Report on Form 10-K for the fiscal year ended September 30, 2005 (the "Annual Report").

"SAFE HARBOR" STATEMENT UNDER PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This Annual Report includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements other than statements of historical facts included in this Annual Report, including, without limitation, statements regarding our future financial position, business strategy, budgets, projected costs, savings and plans and objectives of management for future operations, are forward-looking statements. In addition, forward-looking statements generally can be identified by the use of forward-looking terminology such as "may," "will," "expect," "intend," "estimate," "anticipate," "believe" or "continue" or the negative thereof or variations thereon or similar terminology. Such statements include, among others, statements regarding our ability to develop talent and attract future talent, to reduce future capital expenditures, to monetize our music content, including through new distribution channels and formats, to effectively deploy our capital, the development of digital music and the effect of digital distribution channels on our business, including whether or not the Internet will become an important sales channel and whether we will be able to achieve higher margins from digital sales, our success in limiting piracy, our ability to compete in the highly competitive markets in which we operate, the growth of the music industry and the effect of our and the music industry's efforts to combat piracy on the industry and the effect of litigation on us. Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to have been correct.

There are a number of risks and uncertainties that could cause our actual results to differ materially from the forward-looking statements contained in this Annual Report. Additionally important factors could cause our actual results to differ materially from the forward-looking statements we make in this Annual Report. As stated elsewhere in this Annual Report, such risks, uncertainties and other important factors include, among others:

- the impact of our substantial leverage on our ability to raise additional capital to fund our operations, on our ability to react to changes in the economy or our industry and on our ability to meet our obligations under our indebtedness;
- the continued decline in the global recorded music industry and the rate of overall decline in the music industry;
- our ability to continue to identify, sign and retain desirable talent at manageable costs;
- the threat posed to our business by piracy of music by means of home CD-R activity and Internet peer-to-peer file-sharing;
- the significant threat posed to our business and the music industry by organized industrial piracy;
- the impact of our restructuring plan on our business (including our ability to generate revenues and attract desirable talent);
- the popular demand for particular recording artists and/or songwriters and albums and the timely completion of albums by major recording artists and/or songwriters;

- the diversity and quality of our portfolio of songwriters;
- the diversity and quality of our album releases;
- significant fluctuations in our results of operations and cash flows due to the nature of our business;
- our involvement in intellectual property litigation;
- the possible downward pressure on our pricing and profit margins;
- the seasonal and cyclical nature of recorded music sales;
- our ability to continue to enforce our intellectual property rights in digital environments;
- the ability to develop a successful business model applicable to a digital environment;
- the ability to maintain product pricing in a competitive environment;
- the impact of heightened and intensive competition in the recorded music and music publishing businesses and our inability to execute our business strategy;
- risks associated with our non-U.S. operations, including limited legal protections of our intellectual property rights and restrictions on the repatriation of capital;
- the possible unexpected loss of artists and key employees and our market share as a result of our restructuring plan;
- the impact of legitimate music distribution on the Internet or the introduction of other new music distribution formats;
- the impact of rate regulations on our Music Publishing business;
- risks associated with the fluctuations in foreign currency exchange rates;
- our ability and the ability of our joint venture partners to operate our existing joint ventures satisfactorily;
- the enactment of legislation limiting the terms by which an individual can be bound under a "personal services" contract could impair our ability to retain the services of key artists;
- potential loss of catalog if it is determined that recording artists have a right to recapture recordings under the U.S. Copyright Act;
- changes in law and government regulations;
- legal or other developments related to pending litigation or the industry-wide investigation of the relationship between music companies and radio stations by the Attorney General of the State of New York;
- trends that affect the end uses of our musical compositions (which include uses in broadcast radio and television, film and advertising businesses);
- the growth of other products that compete for the disposable income of consumers;
- risks inherent in relying on one supplier for manufacturing, packaging and distribution services in North America and Europe;
- risks inherent in our acquiring or investing in other businesses;
- the possibility that our owners' interests will conflict with ours or yours;
- our ability to act as a stand-alone company;
- increased costs and diversion of resources associated with complying with the internal control reporting or other requirements of Sarbanes-Oxley;

- weaknesses in our internal controls related to U.S. royalties that could affect our ability to ensure reliable financial reports;
- the effects associated with the formation of Sony BMG Music Entertainment; and
- failure to attract and retain key personnel.

There may be other factors not presently known to us or which we currently consider to be immaterial that may cause our actual results to differ materially from the forward-looking statements.

All forward-looking statements attributable to us or persons acting on our behalf apply only as of the date of this Annual Report and are expressly qualified in their entirety by the cautionary statements included in this Annual Report. We disclaim any duty to publicly update or revise forward-looking statements to reflect events or circumstances after the date made or to reflect the occurrence of unanticipated events.

INTRODUCTION

Warner Music Group Corp. (the "Company" or "Parent") was formed by a private equity consortium of Investors (the "Investor Group") on November 21, 2003. The Company is the direct parent of WMG Holdings Corp. ("Holdings"), which is the direct parent of WMG Acquisition Corp. ("New WMG" or "Acquisition Corp."). New WMG is the successor to substantially all of the interests of the recorded music and music publishing businesses of Time Warner Inc. ("Time Warner"). Such predecessor interests formerly owned by Time Warner are hereinafter referred to as "Old WMG" or the "Predecessor." Effective March 1, 2004, Acquisition Corp. acquired Old WMG from Time Warner for approximately $2.6 billion (the "Acquisition").

Warner Music Group Corp. is a holding company that conducts substantially all of its business operations through its subsidiaries. The Company's only asset is its ownership of all outstanding shares of Holdings, and Holdings' only asset is its ownership of all the outstanding shares of Acquisition Corp. The terms "we," "us," "our," "ours," and the "Company" refer collectively to Warner Music Group Corp. and its consolidated subsidiaries, except where otherwise indicated.

Management's discussion and analysis of results of operations and financial condition ("MD&A") is provided as a supplement to the audited financial statements and footnotes included elsewhere herein to help provide an understanding of our financial condition, changes in financial condition and results of our operations. MD&A is organized as follows:

- *Overview.* This section provides a general description of our business, as well as recent developments that we believe are important in understanding our results of operations and financial condition and in anticipating future trends.
- *Results of operations.* This section provides an analysis of our results of operations for the twelve-month periods ended September 30, 2005 and 2004 and for the ten-month periods ended September 30, 2004 and 2003. This analysis is presented on both a consolidated and segment basis.
- *Financial condition and liquidity.* This section provides an analysis of our cash flows for the twelve-month periods ended September 30, 2005 and 2004, as well as a discussion of our financial condition and liquidity as of September 30, 2005. The discussion of our financial condition and liquidity includes (i) our available financial capacity under the revolving credit portion of our senior secured credit facility and (ii) a summary of our key debt compliance measures under our indenture agreements.

Use of OIBDA

We evaluate our operating performance based on several factors, including our primary financial measure of operating income (loss) before non-cash depreciation of tangible assets, non-cash amortization of intangible

assets and non- cash impairment charges to reduce the carrying value of goodwill and other intangible assets (which we refer to as "OIBDA"). We consider OIBDA to be an important indicator of the operational strengths and performance of our businesses, including the ability to provide cash flows to service debt. However, a limitation of the use of OIBDA as a performance measure is that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in our businesses. Accordingly, OIBDA should be considered in addition to, not as a substitute for, operating income (loss), net income (loss) and other measures of financial performance reported in accordance with U.S. GAAP.

Change in Fiscal Year and Basis of Presentation

In 2004, in connection with the Acquisition, the Company changed its fiscal year-end to September 30 from November 30. As such, we restated our prior quarters starting October 1, 2003, under the new fiscal year format, to enhance comparability between periods. Due to this change in fiscal year-end, our 2004 fiscal year consists of the ten-months ended September 30, 2004, while our 2005 fiscal year is the full twelve-month period ending September 30, 2005. Our discussion of the current twelve-month fiscal year ended September 30, 2005 is presented as the comparison of the twelve-month fiscal year ended September 30, 2005 to the twelve-month period ended September 30, 2004. The twelve months ended September 30, 2004 are unaudited and were derived from the audited fiscal year financial results for the ten months ended September 30, 2004 and the audited fiscal year financial results for the fiscal year ended November 30, 2003. Our discussion of the prior ten-month fiscal year is presented as the comparison of the ten months ended September 30, 2004 to the ten months ended September 30, 2003. The ten months ended September 30, 2003 are unaudited and were derived from the audited fiscal year financial results for the twelve months ended November 30, 2003.

In connection with the Acquisition, a new accounting basis was established for the Company as of the acquisition date based upon an allocation of the purchase price to the underlying net assets acquired. As such, financial information for each of the ten and the twelve months ended September 30, 2004 is separated into pre-acquisition and post-acquisition periods as a result of the change in accounting basis that occurred relating to the Acquisition. That is for the twelve-month period ended September 30, 2004, we have presented our operating results and cash flows separately for the pre-acquisition five-month period ended February 29, 2004 and the post-acquisition, seven-month period ended September 30, 2004. The financial information for the ten months ended September 30, 2004 is separated into the pre-acquisition three-month period ended February 29, 2004 and the post-acquisition, seven-month period ended September 30, 2004.

The split presentation mentioned above is required under GAAP in situations when a change in accounting basis occurs. This is because the new accounting basis requires that the historical carrying value of assets acquired and liabilities assumed be adjusted to fair value, which may yield results that are not strictly comparable on a period-to-period basis due to the different, and sometimes higher, cost basis associated with the allocation of the purchase price.

We believe that this split presentation may impede the ability of users of our financial information to understand our operating and cash flow performance. Consequently, in order to enhance an analysis of our operating results and cash flows, we have presented our operating results and cash flows on a combined basis for the full ten-month period and twelve-month period ended September 30, 2004. The combined presentation for the twelve-month period ended September 30, 2004 simply represents the mathematical addition of the pre-acquisition, five-month period ended February 29, 2004 and the post-acquisition, seven-month period ended September 30, 2004 and the combined presentation for the ten-month period ended September 30, 2004 represents the mathematical addition of the pre-acquisition three-month period ended February 29, 2004 and the post-acquisition seven-month period ended September 30, 2004. These are not intended to represent what our operating results would have been had the Acquisition occurred at the beginning of the period. Reconciliations showing the mathematical combination of our operating results for such periods are included herein.

Though we believe that the combined presentation is most meaningful for the twelve-month period ended September 30, 2004 and the ten-month period ended September 30, 2004, it is not in conformity with GAAP. As

such, we have supplemented our historical operating results for periods, as appropriate, with pro forma financial information and have further highlighted in our discussions that follow any significant effects from the Acquisition to facilitate an understanding of a comparison of our operating results from period-to-period.

OVERVIEW

Description of Business

We are one of the world's major music content companies. Effective as of March 1, 2004, substantially all of Time Warner Inc.'s music division was acquired from Time Warner by us for approximately $2.6 billion.

We classify our business interests into two fundamental areas: Recorded Music and Music Publishing. A brief description of each of those operations is presented below.

Recorded Music Operations

Our Recorded Music business consists of the discovery and development of artists and the related marketing, distribution and licensing of recorded music produced by such artists. In the U.S., our operations are conducted principally through our major record labels—Warner Bros. Records Inc. and The Atlantic Records Group. Internationally, our Recorded Music operations are conducted through our Warner Music International division ("WMI"), which includes various subsidiaries, affiliates and non-affiliated licensees in more than 50 countries outside the United States. In addition to the more traditional methods of discovering and developing artists, we have implemented new initiatives to identify and nurture artists earlier in the development process and reduce development costs by leveraging our independent distribution network. We refer to these new business models as incubator initiatives. Asylum and East West are current incubator labels. In addition, we have also entered into strategic ventures with other record labels.

Our Recorded Music operations also include a catalog division named Rhino Entertainment ("Rhino"), formerly known as Warner Strategic Marketing. Rhino specializes in marketing our music catalog through compilations and reissuances of previously released music and video titles, as well as in the licensing of recordings to/from third parties for various uses, including film and television soundtracks.

Our principal Recorded Music distribution operations include Warner-Elektra-Atlantic Corporation ("WEA Corp."), which primarily markets and sells music products to retailers and wholesale distributors in the U.S.; a 90% interest in Alternative Distribution Alliance, an distribution company that primarily distributes the products of independent labels to retail and wholesale distributors in the United States; various distribution centers and ventures operated internationally; and an 80% interest in Word Entertainment, whose distribution operations specialize in the distribution of music products in the Christian retail marketplace.

Our principal recorded music revenue sources are sales of CDs, digital downloads and other recorded music products and license fees received for the ancillary uses of our recorded music catalog. The principal costs associated with our Recorded Music operations are as follows:

- artist and repertoire costs—the costs associated with (i) signing and developing artists, (ii) creating master recordings in the studio, (iii) creating artwork for album covers and liner notes and (iv) paying royalties to artists, producers, songwriters, other copyright holders and trade unions;
- manufacturing, packaging and distribution costs—the costs to manufacture and distribute product to wholesale and retail distribution outlets;
- marketing and promotion costs—the costs associated with the promotion of artists and recorded music products, including costs to produce music videos for promotional purposes and artist tour support; and
- administration costs—the costs associated with general overhead and other administrative costs, as well as costs associated with anti-piracy initiatives.

Music Publishing Operations

Our Music Publishing operations include Warner/Chappell Music, Inc. and its wholly owned subsidiaries, and certain other music publishing affiliates of the Company. We own or control the rights to more than one million musical compositions, including numerous pop music hits, American standards, folk songs and motion picture and theatrical compositions. Our Music Publishing operations also formerly included Warner Bros. Publications ("WBP"), which marketed printed versions of our music throughout the world. On May 31, 2005, we sold WBP to Alfred Publishing. The sale is not expected to have a material effect on our future operating results and financial condition.

Publishing revenues are derived from four main royalty sources:

- *Mechanical:* the licensor receives royalties with respect to compositions embodied in recordings sold in any format or configuration, including singles, albums, CDs, digital downloads and mobile phone ringtones.
- *Performance:* the licensor receives royalties if the composition is performed publicly (e.g., broadcast radio and television, movie theater, concert, nightclub or Internet and wireless streaming).
- *Synchronization:* the licensor receives royalties or fees for the right to use the composition in combination with visual images (e.g., in films, television commercials and programs and videogames).
- *Other:* the licensor receives royalties from other uses such as stage productions.

The principal costs associated with our Music Publishing operations are as follows:

- artist and repertoire costs—the costs associated with (i) signing and developing songwriters and (ii) paying royalties to songwriters, co-publishers and other copyright holders in connection with income generated from the exploitation of their copyrighted works;
- manufacturing, packaging and distribution costs—the costs to manufacture and distribute sheet music and songbooks to retail distribution outlets and schools; and
- administration costs—the costs associated with general overhead and other administrative costs.

Factors Affecting Results of Operations and Financial Condition

Market Factors

Over the past five years, the recorded music industry has been unstable, which has adversely affected our operating results. The industry-wide decline can be attributed primarily to digital piracy. Other drivers of this decline are the bankruptcies of record retailers and wholesalers, growing competition for consumer discretionary spending and retail shelf space, and the maturation of the CD format, which has slowed the historical growth pattern of recorded music sales. While new formats for selling recorded music product have been created, including the legal downloading of digital music using the Internet and DVD-Audio formats and the distribution of music on mobile devices, significant revenue streams from these new markets are just beginning to emerge. As of November 20, 2005, year-to-date U.S. recorded music sales (excluding sales of digital tracks) are down approximately 7.6% year-over-year. The recorded music industry performance may continue to negatively impact our operating results. In addition, a declining recorded music industry could continue to have an adverse impact on the music publishing business. This is because our music publishing business generates a significant portion of its revenues from mechanical royalties received from the sale of music in recorded music formats such as the CD.

Restructuring

Due in part to the development of the new channels mentioned above and ongoing anti-piracy initiatives, we believe that the recorded music industry is positioned to improve over the coming years. However, the industry

may relapse into a period of decline. In addition, there can be no assurances as to the timing or the extent of any improvement in the industry. Accordingly, we have executed a number of cost-saving initiatives over the past few years in an attempt to realign our cost structure with the changing economics of the industry. These initiatives have included significant headcount reductions from the consolidation of operations and the streamlining of corporate and label overhead, exiting certain leased facilities in an effort to consolidate locations and the sale of our manufacturing, packaging and physical distribution operations. We have now completed substantially all of our restructuring efforts and have streamlined the Company to achieve approximately $250 million in annual cost savings.

Transactions with Time Warner and its Affiliates

As previously described, prior to March 1, 2004, Old WMG was owned and operated by Time Warner. As such, in the normal course of conducting our business, Old WMG had various commercial and financing arrangements with Time Warner and its affiliates. In particular, Old WMG purchased manufacturing packaging and physical distribution services from affiliates of Time Warner, and Time Warner funded its operating and capital requirements. See Note 20 to our audited financial statements for a summary of the principal transactions between Old WMG and Time Warner and its affiliates.

Time Warner sold its CD and DVD manufacturing, packaging and physical distribution operations to Cinram at the end of October 2003. Prior to the sale, these operations were under the control of Time Warner and Old WMG's management. As such, pricing for such services was not negotiated on an arms-length basis and did not reflect market rates. As part of the sale, Time Warner and Old WMG entered into arrangements with Cinram, under which Cinram will provide manufacturing, packaging and physical distribution services for our products in the U.S. and Europe at favorable, market-based rates that were negotiated on an arms-length basis.

With respect to the financing arrangements with Time Warner, all cash received or paid by Old WMG was included in, or funded by, clearing accounts or shared international cash pools within Time Warner's centralized cash management system. Some of those arrangements were interest-bearing and others were not. Accordingly, historical net interest expense is not representative of the amounts incurred by us under our new leveraged capital structure created in connection with the Acquisition.

Charges and Payments Relating to Executive Compensation

We determined that certain shares of restricted stock issued in 2004 and early 2005 may have been sold at prices below fair market value on the applicable date of sale and certain options to purchase shares of the Company's stock granted may have had exercise prices below fair market value on the applicable date of grant. As a result, certain U.S. employee holders of the restricted stock who made elections under Section 83(b) of the Internal Revenue Code will be subject to additional ordinary income tax to the extent of the fair market value of the restricted stock received over the purchase price they paid for such stock. In other cases, certain employees who did not make such an election will be subject to higher taxes on their restricted shares at the time of vesting than would have been the case had they purchased the shares for fair market value. In addition, under the provisions of the American Jobs Creation Act of 2004, signed into law in October 22, 2004, U.S. employee option holders whose options vest with exercise prices below fair market value on the date of grant are subject to significant penalties under new Section 409A of the Internal Revenue Code. IRS Notice 2005-1 provides transitional guidance on the application of Section 409A which, among other things, permits options with exercise prices below the fair market value of the underlying stock on the date of grant to be amended or replaced with new options having an exercise price at least equal to the fair market value on the grant date. Non-U.S. employee holders of restricted stock or options may be subject to similar or other related issues. In order for us to address these issues our Board of Directors, based on a re-assessment of fair market values on the applicable dates, approved the actions discussed below.

Restricted Stock. We were authorized to pay each employee, who purchased restricted stock at prices that were below fair market value on the date of purchase, a cash bonus. The cash bonus payable to those employees

who made a Section 83(b) election is an amount equal to the tax liability incurred by the employee as of the date of purchase based on any difference between the re-determined purchase date fair market value and the amount originally paid by the employee, plus an amount necessary to pay the taxes on the bonus. The bonuses that are payable to each of those employees who did not make a Section 83(b) election or the applicable foreign equivalent is an amount reflecting an estimate of the additional tax which would be payable by the employee at the time the restricted stock is scheduled to vest due to that taxable amount being subject to ordinary income rather than capital gains tax rates, and assuming that the re-determined value of the stock remains constant over the vesting period, adjusted down to reflect a present value discount based on the earliest possible vesting dates. We will pay these employees an amount necessary to pay the taxes on the bonus. This will result in total cash payments of approximately $10 million, which the Company has expensed in the fiscal year ended September 30, 2005.

Options. We have revised the exercise prices of certain options to purchase our common stock to prices equal to the applicable re-determined fair market values of the common stock on the dates of the respective grants. To compensate the grantees for the loss of value represented by this adjustment to the option exercise prices, we will pay each affected employee a cash bonus in an amount equal to the excess of the adjusted aggregate exercise price of the employee's options over the original aggregate exercise price of the employee's options, adjusted down to reflect a present value discount based on the earliest possible exercise dates. We have treated the revision of the exercise prices of certain option grants as a modification of such grants. This will result in total cash bonuses paid of approximately $9 million. We have recorded expense of $6 million in the fiscal year ended September 30, 2005 related to this modification of certain grants.

Additional Charges and Payments to Employees

Option Adjustments as a Result of Dividend to Investors. Further, in connection with the $100.5 million cash dividend we declared and paid to holders of our common stock consisting of the Investor Group and certain members of management who held shares of common stock prior to our initial common stock offering, we have made an adjustment to all options outstanding at the time of declaration of the dividend. The adjustment consists of a cash make-whole payment consisting of an amount equal to the pro rata amount that would have been received per share had all outstanding options been exercised at the time of the declaration of the dividend adjusted down to reflect a present value discount based on the earliest possible exercise dates. We have expensed approximately $3 million of expense related to such payments in the fiscal year ended September 30, 2005.

Employee Bonus Plan. We paid a special one-time bonus upon consummation of our initial common stock offering to all or substantially all of our employees, excluding senior management and certain employees with an equity participation in our company. The amount of the award granted to an employee was equal to approximately 4% of the employee's annual salary. We have paid and recorded expense of $10 million in the fiscal year ended September 30, 2005 related to such bonus.

Of the amounts related to restricted stock and options, all but $3 million has been paid as of September 30, 2005.

Initial Common Stock Offering

In May 2005, we completed the initial public offering of our common stock (the "Initial Common Stock Offering"). Prior to the consummation of the Initial Common Stock Offering, we, among other things, renamed all of our outstanding shares of Class A Common Stock as common stock and authorized an approximately 1,139 for 1 split of our common stock. We contributed the net proceeds from the Initial Common Stock Offering of $517 million to Holdings as an equity capital contribution. Holdings used all of such funds and approximately $57 million of cash received through dividends from Acquisition Corp. to redeem its outstanding notes as discussed below.

In addition, in connection with the Initial Common Stock Offering, we among others things, repurchased the warrants issued as part of the initial purchase price consideration for the Acquisition from Time Warner for $138 million, we declared and paid a dividend to our stockholders prior to the Initial Common Stock Offering of $100.5 million, and terminated our management agreement as discussed below.

Holdings Refinancing and Redemption

In December 2004, Holdings issued $847 million principal amount of debt. The $847 million principal amount of Holdings' debt consisted of (i) $250 million principal amount of Floating Rate Senior Notes due 2011 (the "Holdings Floating Rate Notes"), (ii) $397 million principal amount at maturity of 9.5% Senior Discount Notes due 2014, which had an initial issuance discount of $147 million (the "Holdings Discount Notes") and (iii) $200 million principal amount of Floating Rate Senior PIK Notes due 2014 (the "Holdings PIK Notes", and collectively, the "Holdings Notes").

In connection with the Initial Common Stock Offering, we used $517 million of proceeds from the offering along with $57 million of available cash to redeem certain of the Holdings Notes outstanding. As of September 30, 2005, Holdings had $174 million of debt on its balance sheet relating to such securities, net of issuance discounts.

The Holdings Floating Rate Notes were redeemed in full on June 15, 2005. From the issuance date through the redemption date, the notes bore interest at a quarterly floating rate based on three-month LIBOR rates plus a margin equal to 4.375%. Interest was payable quarterly in cash beginning on March 15, 2005.

The Holdings Discount Notes were issued at a discount and had an initial accreted value of $630.02 per $1,000 principal amount at maturity. Prior to December 15, 2009, no cash interest payments are required. However, interest accrues on the Holdings Discount Notes in the form of an increase in the accreted value of such notes such that the accreted value of the Holdings Discount Notes will equal the principal amount at maturity on December 15, 2009. Thereafter, cash interest on the Holdings Discount Notes is payable semiannually at a fixed rate of 9.5% per annum. The Holdings Discount Notes mature on December 15, 2014. The Company redeemed 35% of the Holdings Discount Notes on June 15, 2005.

The Holdings PIK Notes were redeemed in full on June 15, 2005. From the date of issuance through the date of redemption, the notes bore interest at a semi-annual floating rate based on six-month LIBOR rates plus a margin equal to 7%. Interest was accrued in the form of additional PIK notes at the election of the Company. Such amounts were also repaid in connection with the redemption.

In connection with the redemption of the Holdings Floating Rate Notes and 35% of the Holdings Discount Notes, we were required to pay redemption premiums of $10 million and $9 million, respectively, which we paid on June 15, 2005. We also wrote off the remaining balance of debt-issuance costs of $12 million related to the notes redeemed and the remaining unamortized original issue discount of $4 million related to the Holdings PIK Notes. These amounts were recorded as a loss on the repayment of the notes in the consolidated statement of operations for the year ended September 30, 2005.

We were also required to pay all accrued interest as of the redemption date related to the Holdings Notes that were redeemed. This amount consisted of $5 million related to the Holdings Floating Rate Notes, $9 million related to the Holdings PIK Notes, and $4 million in accreted value of the 35% of Holdings Discount Notes redeemed. These amounts have been expensed in the consolidated statement of operations for the year ended September 30, 2005.

Termination of Management/ Monitoring Agreement

As described in Note 20 to our audited consolidated financial statements included herein, we entered into a management monitoring agreement (the "Management Agreement") with the Investor Group in connection with the Acquisition.

Under the Management Agreement, we were required to pay the Investor Group an aggregate annual fee of $10 million per year (the "Periodic Fees") in consideration for ongoing consulting and management advisory services. In addition, in the case of future services provided in connection with any future acquisition, disposition, or financing transactions involving the Company or its subsidiaries, the Management Agreement required the Company, Holdings and Acquisition Corp. to pay the Investor Group an aggregate fee of one percent of the gross transaction value of each such transaction ("Subsequent Fees"). The Management Agreement also requires the Company, Holdings and Acquisition Corp. to pay the reasonable expenses of the Investor Group in connection with, and indemnify them for liabilities arising from, the Management Agreement, the Acquisition and any related transactions, their equity investment in the Company, Holdings or Acquisition Corp., their operations, and the services they provide to the Company, Holdings and Acquisition Corp.

The Management Agreement provided that it would continue in full force and effect until December 30, 2014, provided, however, that the Investor Group could cause the agreement to terminate at any time. In the event of the termination of the Management Agreement, the Company, Holdings and Acquisition Corp. were required by the terms of the agreement to pay each of the Investor Group any unpaid portion of the Periodic Fees, any Subsequent Fees and any expenses due with respect to periods prior to the date of termination plus the net present value (using a discount rate equal to the then yield on U.S. Treasury Securities of like maturity) of the Periodic Fees that would have been payable with respect to the period from the date of termination until December 30, 2014.

The Investor Group terminated the Management Agreement and on May 16, 2005, we paid the Investor Group a $73 million termination fee, which was reflected in our statement of operations for the fiscal year ended September 30, 2005.

Stock-based Compensation

Effective March 1, 2004, in connection with the Acquisition, the Company adopted the fair value recognition provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("FAS 123") to account for all stock-based compensation plans adopted subsequent to the Acquisition. Under the fair value recognition provisions of FAS 123, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the vesting period.

Prior to the Acquisition, certain employees of Old WMG participated in various Time Warner stock option plans. In accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and related interpretations, compensation cost for stock options or other equity-based awards granted to employees was recognized in income based on the excess, if any, of the quoted market price of the stock at the grant date of the award over the amount an employee must pay to acquire the stock. Generally, the exercise price for stock options granted to employees equaled or exceeded the fair market value of Time Warner common stock at the date of grant, thereby resulting in no recognition of compensation expense by Old WMG.

We recognized $25 million of stock-based compensation expense in the twelve months ended September 30, 2005, compared to $1 million in the twelve months ended September 30, 2004.

Lava Records Restructuring

The co-chairman of The Atlantic Records Group left our employ in August 2005 and we acquired the remaining interest of the Lava Records joint venture. As a result, in order to streamline our operations, we integrated the Lava operations into the operations of The Atlantic Records Group. In connection with the integration, certain employees were involuntarily terminated and certain artist contracts were terminated, which resulted in the recognition of $7 million in restructuring costs and we also incurred other non-recurring charges of $24 million, specifically related to the departure of the co-chairman of The Atlantic Records Group and the expensing of certain other amounts, in the twelve months ended September 30, 2005. Approximately $20 million of these charges were non-cash.

Settlement

We recorded $5 million of expense related to the settlement of a government investigation into radio promotion practices by New York State Attorney General Eliot Spitzer in the twelve months ended September 30, 2005.

RESULTS OF OPERATIONS

Twelve Months Ended September 30, 2005 Compared to Twelve Months Ended September 30, 2004

The following table summarizes our historical results of operations. The financial data for the twelve months ended September 30, 2005 and the seven months ended September 30, 2004 have been derived from our audited financial statements included elsewhere herein and the financial data for the five months ended February 29, 2004 are unaudited and are derived from the audited financial statements included elsewhere herein. See "Change in Fiscal Year and Basis of Presentation" presented earlier herein for a discussion of the use of financial information for the combined twelve-month period ended September 30, 2004.

	Successor	Combined	Successor	Predecessor
	Twelve Months Ended September 30, 2005	Twelve Months Ended September 30, 2004	Seven Months Ended September 30, 2004	Five Months Ended February 29, 2004
	(audited)	(unaudited)	(audited)	(unaudited)
		(in millions)		
Revenues	$ 3,502	$ 3,437	$ 1,769	$ 1,668
Costs and expenses:				
Cost of revenues	(1,850)	(1,850)	(944)	(906)
Selling, general and administrative expenses[1]	(1,301)	(1,287)	(677)	(610)
Impairment of goodwill and other intangible assets	—	(1,019)	—	(1,019)
Amortization of intangible assets	(187)	(201)	(104)	(97)
Loss on termination of management agreement	(73)	—	—	—
Restructuring costs	(7)	(34)	(26)	(8)
Total costs and expenses	(3,418)	(4,391)	(1,751)	(2,640)
Operating income (loss)	84	(954)	18	(972)
Interest expense, net	(182)	(82)	(80)	(2)
Net investment-related gains (losses)	1	(9)	—	(9)
Equity in the losses of equity-method investees, net	(1)	(13)	(2)	(11)
Deal related transaction and other costs	—	(63)	—	(63)
Loss on repayment of Holdings Notes	(35)	—	—	—
Loss on repayment of bridge loan	—	(6)	(6)	—
Unrealized gain (loss) on warrants	17	(120)	(120)	—
Minority interest expense	(5)	(14)	(14)	—
Other income (expense), net	7	(11)	(4)	(7)
Loss before income taxes	(114)	(1,272)	(208)	(1,064)
Income tax expense	(55)	(150)	(30)	(120)
Net loss	$ (169)	$ (1,422)	$ (238)	$ (1,184)

(1) Includes depreciation expense of: $51 million for the twelve months ended September 30, 2005, $36 million for the seven months ended September 30, 2004, and $31 million for the five months ended February 29, 2004.

Consolidated Historical Results

Revenues

Our revenues increased 2% to $3.502 billion for the twelve months ended September 30, 2005, compared to $3.437 billion for the twelve months ended September 30, 2004. Excluding a $106 million benefit of foreign currency exchange rates, total revenue declined by $41 million. Digital revenues increased significantly from $36 million in the twelve months ended September 30, 2004 to $157 million in the twelve months ended September 30, 2005. The increases in digital revenues resulted from our efforts to build our digital business, including efforts to further monetize existing content through new formats and new distribution channels and the development and increased consumer usage of legal, online distribution channels for the music industry. International operations represented $1.827 billion of consolidated revenue for the twelve months ended September 30, 2005, compared to $1.825 billion of consolidated revenues for the twelve months ended September 30, 2004, comprising 52% and 53% of total revenues, respectively. See "Business Segment Results" presented hereinafter for a discussion of revenues by business segment.

Cost of revenues

Our cost of revenues was $1.850 billion for both the twelve months ended September 30, 2005 and 2004. Expressed as a percentage of revenues, cost of revenues was approximately 53% and 54% for the twelve months ended September 30, 2005 and 2004, respectively. Excluding the negative impact of foreign currency exchange rates, product costs decreased by $8 million, primarily due to the increased usage of digital distribution channels which were more profitable as the absence of certain manufacturing and distribution costs create a better contribution margin. Artist and repertoire costs declined from the prior twelve-month period by $28 million, which was primarily due to pre-acquisition write-offs of advance royalty payments deemed to be unrecoverable, offset by an increase in royalty expense due to changes in product mix and increases in sales. Licensing expense also decreased as a result of declines in certain areas of our Music Publishing business.

Selling, general and administrative expenses

Our selling, general and administrative expenses increased by $14 million to $1.301 billion for the twelve months ended September 30, 2005, compared to $1.287 billion for the twelve months ended September 30, 2004. Expressed as a percentage of revenues, selling, general and administrative expenses were 37% for both of the twelve months ended September 30, 2005 and 2004. The increase in selling, general and administrative expenses relates primarily to certain non-recurring expenses that occurred in 2005, including (i) $29 million in compensation expense, consisting of a $10 million one-time bonus to employees related to the Company's Initial Common Stock Offering and $19 million of one-time payments to holders of the Company's restricted stock and stock options, primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date and (ii) $24 million of expense in the quarter ended September 30, 2005, related to the departure of the co-chairman of The Atlantic Records Group and the expensing of certain amounts paid in connection with the acquisition of Lava Records. Additionally, our expense related to our stock-based awards increased by $24 million to $25 million for the twelve months ended September 30, 2005, as compared to $1 million for the twelve months ended September 30, 2004. Excluding the impact of the items previously described and the negative impact of foreign currency exchange rates of $29 million, selling, general and administrative expenses in the twelve months ended September 30, 2005 decreased $92 million as compared to the twelve months ended September 30, 2004, and were approximately 34% of total revenues. This decrease in selling, general and administrative expenses related primarily to (i) reductions in sales and marketing costs of $59 million, primarily as a result of our cost-savings initiatives completed in 2005 in connection with our restructuring plan, (ii) reductions in distribution costs of $25 million due to the decline in year over year physical sales as well as the increase in sales through digital distribution methods, lower bad debt expense and the impact of our cost-savings initiatives and (iii) a decrease in depreciation of $16 million due to lower post-Acquisition capital spending and lower depreciation of software development costs in the current year.

Loss on termination of management agreement

Concurrent with our Initial Common Stock Offering, the Investor Group terminated the Management Agreement. Under the Management Agreement, we were required to pay the Investor Group annual fees in consideration for ongoing consulting and management advisory services and transaction based fees for services provided in connection with any future acquisition, disposition, or financing. The Investor Group terminated the Management Agreement on May 10, 2005 and on May 16, 2005, we paid a $73 million termination fee.

Restructuring costs

We recognized $7 million in restructuring costs in the twelve months ended September 30, 2005 compared to $34 million in restructuring costs in the twelve months ended September 30, 2004. The restructuring costs recognized in 2005 related to termination benefits paid to certain employees who were involuntarily terminated and the costs of terminating certain artist contracts. These activities occurred in connection with the integration of Lava Records' operations into the operations of The Atlantic Records Group subsequent to our acquisition of the remaining interest in the Lava Records joint venture. The restructuring costs in 2004 principally related to costs associated with the implementation of a cost-savings incentive compensation plan designed to incentivize management to reduce operating costs.

Reconciliation of Consolidated Historical OIBDA to Operating Income (Loss) and Net Loss

As previously described, we use OIBDA as our primary measure of financial performance. The following table reconciles OIBDA to operating income (loss), and further provides the components from operating income (loss) to net loss for purposes of the discussion that follows (in millions):

	Successor	Combined	Successor	Predecessor
	Twelve Months Ended September 30, 2005	Twelve Months Ended September 30, 2004	Seven Months Ended September 30, 2004	Five Months Ended February 29, 2004
	(audited)	(unaudited)	(audited)	(unaudited)
OIBDA	$ 322	$ 333	$ 158	$ 175
Depreciation expense	(51)	(67)	(36)	(31)
Amortization expense	(187)	(201)	(104)	(97)
Impairment of goodwill and other intangible assets	—	(1,019)	—	(1,019)
Operating income (loss)	84	(954)	18	(972)
Interest expense, net	(182)	(82)	(80)	(2)
Net investment-related gains (losses)	1	(9)	—	(9)
Equity in the losses of equity-method investees, net	(1)	(13)	(2)	(11)
Deal-related transaction and other costs	—	(63)	—	(63)
Loss on repayment of Holdings Notes	(35)	—	—	—
Loss on repayment of bridge loan	—	(6)	(6)	—
Unrealized gain (loss) on warrants	17	(120)	(120)	—
Minority interest expense	(5)	(14)	(14)	—
Other income (expense), net	7	(11)	(4)	(7)
Loss before income taxes	(114)	(1,272)	(208)	(1,064)
Income tax expense	(55)	(150)	(30)	(120)
Net loss	$ (169)	$ (1,422)	$ (238)	$ (1,184)

OIBDA

Our OIBDA decreased to $322 million for the twelve months ended September 30, 2005, compared to $333 million for the twelve months ended September 30, 2004. Expressed as a percentage of revenues, total OIBDA

margin was 10% for both the twelve months ended September 30, 2005 and 2004. The decrease in OIBDA was primarily a result of certain one-time items, including (i) the $73 million loss on termination of the Management Agreement described above, (ii) $10 million of one-time bonuses paid in connection with the initial public offering, (iii) $19 million of one-time payments associated with our restricted stock and stock option awards granted at prices below fair value, (iv) $24 million of non-recurring charges incurred in connection with the departure of the co-chairman of The Atlantic Records Group and the expensing of certain amounts paid in connection with the acquisition of the remaining interest in the Lava Records joint venture, as well as a $24 million increase in stock-based compensation expense. Excluding the one-time items, the increase in stock-based compensation, and a decrease in restructuring costs of $27 million, OIBDA for the twelve months ended September 30, 2005 as compared to the twelve months ended September 30, 2004 increased by $112 million, which was primarily related to the decreases in costs of revenues and selling, general and administrative expenses discussed above and expressed as a percentage of revenues, total OIBDA margin was 14%. See "Business Segment Results" presented hereinafter for a discussion of OIBDA by business segment.

Depreciation expense

Our depreciation expense decreased by $16 million to $51 million for the twelve months ended September 30, 2005, compared to $67 million for the twelve months ended September 30, 2004. The decrease was principally related to lower post-Acquisition capital spending and lower depreciation of software development costs in the current year.

Amortization expense

Our amortization expense decreased by $14 million to $187 million for the twelve months ended September 30, 2005 compared to $201 million for the twelve months ended September 30, 2004. The decrease related to the new basis of accounting recorded in connection with the Acquisition, which resulted in a lower revaluation of the historical cost bases of our identifiable intangible assets. This was offset, in part, by the acquisition of additional recorded music catalog, music publishing copyrights and artist contracts during 2005.

Impairment of goodwill and other intangible assets

We recognized impairment charges to reduce the carrying value of goodwill and other intangible assets of $1.019 billion during the twelve months ended September 30, 2004. Such amounts primarily reflected declines in the valuation of music-related businesses due largely to the industry-wide effects of piracy and were recorded in November 2003.

Operating income (loss)

Our operating income for the twelve months ended September 30, 2005 was $84 million compared to an operating loss of $954 million for the twelve months ended September 30, 2004. This improvement was primarily due to an impairment charge of $1.019 billion, recorded in November 2003, to reduce the carrying value of our goodwill and other intangible assets to fair value. Additionally, the prior twelve-month period reflected an additional $27 million of restructuring costs as compared to the current twelve-month period, as described above. Although our operating income increased as a result of these non-recurring items in the prior twelve-month period, our fiscal year 2005 operating income included the effect of certain one-time items, including (i) the $73 million loss on termination of the Management Agreement described above, (ii) $10 million of one-time bonuses paid in connection with the initial public offering, (iii) $19 million of one-time payments associated with our restricted stock and stock option awards granted at prices below fair value and (iv) $24 million of non-recurring charges incurred in connection with the departure of the co-chairman of The Atlantic Records Group and the expensing of certain amounts paid in connection with the acquisition of the remaining interest in the Lava Records joint venture, as well as a $24 million increase in stock-based compensation expense. Excluding the one-time items, the increase in stock-based compensation, and the decrease in

restructuring costs and impairment charges previously discussed, operating income for the twelve months ended September 30, 2005 as compared to the twelve months ended September 30, 2004 increased $142 million, which was primarily related to the decreases in costs of revenues and selling, general and administrative expenses discussed above. See "Business Segment Results" presented hereinafter for a discussion of operating income (loss) by business segment.

Interest expense, net

Our net interest expense increased to $182 million in the twelve months ended September 30, 2005, compared to $82 million for the twelve months ended September 30, 2004. The increase in interest expense is due to higher average debt balances in 2005 as compared to 2004, primarily due to the financing of the Acquisition in March 2004, the April 2004 refinancing, the borrowing of an additional term loan in May 2005 and the new debt issued by Holdings of approximately $696 million in December 2004, offset by the subsequent repayment of all but approximately $170 million of the Holdings Notes in June 2005. See "—Financial Condition and Liquidity" for more information.

Net investment-related gains (losses)

We recognized a $1 million investment-related gain for the twelve months ended September 30, 2005 primarily related to the sale of our interest in an equity-method investment. For the twelve-months ended September 30, 2004, we recognized $9 million of net investment-related losses principally related to reductions in the carrying values of certain equity-method investments.

Deal-related transaction and other costs

During the twelve months ended September 30, 2004, in connection with the Acquisition and Time Warner's prior pursuit of other strategic ventures or dispositions, including our businesses, that did not occur, we incurred $63 million of costs. These costs consisted of (i) $23 million of transaction costs, primarily relating to legal, accounting and investment-banking fees, (ii) a $15 million loss in connection with the pension curtailment for employees covered under Time Warner's U.S. pension plans that ultimately occurred upon the closing of the Acquisition and (iii) a $25 million loss relating to certain executive contractual obligations that were ultimately triggered upon the closing of the Acquisition.

Equity in the losses of equity-method investees, net

Our equity in the losses of equity-method investees was $1 million for the twelve months ended September 30, 2005, compared to $13 million for the twelve months ended September 30, 2004. The lower losses principally related to the fact that certain of our former loss-generating investees, such as our former interest in MusicNet, were retained by Time Warner and were not part of the assets acquired by us in the Acquisition.

Loss on repayment of Holdings Notes

In June 2005 we redeemed all of the outstanding Holdings Floating Rate Notes, all of the outstanding Holdings PIK Notes and 35% of the outstanding Holdings Discount Notes. In connection with the redemption, we paid approximately $19 million of redemption premiums and wrote off approximately $12 million related to the carrying value of the unamortized debt issuance costs related to our Holdings Notes and approximately $4 million related to the carrying value of the unamortized discount on the issuance of the Holdings Notes. See "—Financial Condition and Liquidity" for more information.

Loss on repayment of bridge loan

We recognized a $6 million loss during the twelve months ended September 30, 2004 to write off the carrying value of the unamortized debt issuance costs related to our bridge loan, which we repaid in April 2004.

Unrealized gain (loss) on warrants

We recognized a $17 million unrealized gain in the twelve months ended September 30, 2005, compared to a $120 million unrealized loss in the twelve months ended September 30, 2004 on stock warrants issued to Time Warner in connection with the Acquisition. In connection with the Company's Initial Common Stock Offering in May 2005, we repurchased the three-year warrants at a cost of approximately $138 million, which approximated fair value at that date.

Minority interest expense

We recognized minority interest expense of $5 million for the twelve months ended September 30, 2005, compared to $14 million for the twelve months ended September 30, 2004. This expense related to dividends on preferred stock of Holdings that was held directly by the Investor Group and was issued in connection with the initial funding of the purchase price for the Acquisition effective March 1, 2004. The preferred stock was fully repaid in December 2004 from the proceeds of the Holdings Notes.

Other income (expense), net

We recognized other income of $7 million for the twelve months ended September 30, 2005, compared to other expense of $11 million for the twelve months ended September 30, 2004. Other income includes gains and losses related to foreign currency exchange rates movements, associated with inter-company receivables and payables that are not of a long-term investment nature, and as such, are required by U.S. GAAP to be reported in the statement of operations.

Income tax expense

We provided income tax expense of $55 million for the twelve months ended September 30, 2005 compared to $150 million for the twelve months ended September 30, 2004. The income tax provisions are not entirely comparable due to the changes in our tax profile that occurred in connection with the Acquisition. Prior to the closing of the Acquisition, we were a member of the Time Warner U.S. consolidated tax group and were able to recognize deferred tax benefits on U.S. domestic tax losses incurred. However, in connection with the Acquisition, our membership in the Time Warner U.S. consolidated tax group terminated along with our ability to recognize these deferred tax benefits. Accordingly, the income tax expense in 2005 primarily relates to the tax provisions on foreign income. There was no offsetting income tax benefit in 2005 on U.S. and certain foreign jurisdiction tax losses incurred due to the uncertainty of the realization of those deferred tax assets.

Net loss

We recognized a net loss of $169 million for the twelve months ended September 30, 2005, compared to a net loss of $1.422 billion for the twelve months ended September 30, 2004. The decrease in net loss relates primarily to the impairment charge recorded in the twelve months ended September 30, 2004 of $1.019 billion. The twelve months ended September 30, 2005 reflect the effects of certain one-time items, including (i) the $73 million loss on termination of the Management Agreement described above, (ii) $10 million of one-time bonuses paid in connection with the initial public offering, (iii) $19 million of one-time payments associated with our restricted stock and stock option awards granted at prices below fair value, (iv) $24 million of non-recurring charges incurred in connection with the departure of the co-chairman of The Atlantic Records Group and the expensing of certain amounts paid in connection with the acquisition of the remaining interest in the Lava Records joint venture and (v) the $35 million loss on repayment of the Holdings Notes described above. Excluding the one-time items included in the twelve months ended September 30, 2005, the $24 million increase in stock-based compensation, the $27 million decrease in restructuring, and the effects of one-time items included in the twelve months ended September 30, 2004, which included (i) the impairment charges, (ii) the $6 million loss on repayment of bridge loan described above and (iii) the $63 million of deal-related and other transaction costs described above, net income for the twelve months ended September 30, 2005 as compared to

the twelve months ended September 30, 2004 increased $323 million. This increase is primarily related to the increases in operating income and unrealized gains on warrants and the decrease in income tax expense, all described above.

Business Segment Results

Revenue, OIBDA and operating income (loss) by business segment are as follows (in millions):

	Successor	Combined	Successor	Predecessor
	Twelve Months Ended September 30, 2005	Twelve Months Ended September 30, 2004	Seven Months Ended September 30, 2004	Five Months Ended February 29, 2004
	(audited)	(unaudited)	(audited)	(unaudited)
Recorded Music				
Revenue	$ 2,924	$ 2,859	$ 1,429	$ 1,430
OIBDA[1]	$ 380	$ 266	$ 120	$ 146
Operating income (loss)[1]	$ 215	$ (934)	$ 24	$ (958)
Music Publishing				
Revenue	$ 607	$ 601	$ 348	$ 253
OIBDA[1]	$ 141	$ 144	$ 87	$ 57
Operating income (loss)[1]	$ 82	$ 74	$ 53	$ 21
Intersegment Eliminations				
Revenue eliminations	$ (29)	$ (23)	$ (8)	$ (15)
OIBDA[1]	$ (199)	$ (77)	$ (49)	$ (28)
Operating income (loss)[1]	$ (213)	$ (94)	$ (59)	$ (35)
Total				
Revenue	$ 3,502	$ 3,437	$ 1,769	$ 1,668
OIBDA[1]	$ 322	$ 333	$ 158	$ 175
Operating income (loss)[1]	$ 84	$ (954)	$ 18	$ (972)

(1) OIBDA and operating income for the twelve months ended September 30, 2005 and 2004 have been reduced by $7 million and $34 million of restructuring costs, respectively. Of such amounts, $7 million related to Recorded Music for the twelve months ended September 30, 2005 and $24 million related to Recorded Music, $1 million related to Music Publishing, and $9 million related to Corporate for the twelve months ended September 30, 2004.

Recorded Music

Recorded Music revenues increased by $65 million to $2.924 billion for the twelve months ended September 30, 2005, compared to $2.859 billion for the twelve months ended September 30, 2004. Recorded Music revenues represented approximately 83% of consolidated revenues for the twelve months ended September 30, 2005 and 2004. The increase in Recorded Music revenue was primarily due to the increase in digital sales of $105 million to $137 million in the twelve months ended September 30, 2005. The increase in revenues from the sale of music in digital formats related to the development and increased consumer usage of legal, online distribution channels for the music industry. For the twelve months ended September 30, 2005, digital sales increased to 5% of Recorded Music revenues. Digital sales in the U.S. increased by $79 million to $105 million or 7% of U.S. Recorded Music revenues, and more than offset the decline in fiscal 2005 U.S physical unit sales. International sales of music in digital formats rose by $26 million to $32 million or 2% of international Recorded Music revenues.

Excluding the increase in digital sales and an approximate $86 million favorable impact of foreign currency exchange rates, physical sales of Recorded Music formats declined by approximately $124 million in the twelve

months ended September 30, 2005 as compared with the twelve months ended September 30, 2004. The decline reflected the continued impact of industry-wide piracy, particularly in our international Recorded Music Business where $111 million of this decline occurred. U.S. Recorded Music experienced a less significant decline in physical sales of $13 million, primarily due to numerous key commercial releases in the twelve months ended September 30, 2005 that sold in excess of one million units, including albums from artists such as James Blunt, Luis Miguel, Michael Bublé, Rob Thomas, Simple Plan, T.I., Faith Hill and Mike Jones.

Recorded Music OIBDA increased by $114 million to $380 million for the twelve months ended September 30, 2005, compared to $266 million for the twelve months ended September 30, 2004. Expressed as a percent of Recorded Music revenues, Recorded Music OIBDA was 13% and 9% for the twelve-month periods ended September 30, 2005 and 2004 respectively. Excluding a $1 million benefit of foreign currency exchange rates Recorded Music OIBDA benefited principally from the revenue increases described above, and from decreases in expenses including (i) a decrease in variable selling and marketing expenses of $58 million as a result of our cost savings initiatives, (ii) a decrease in artist and repertoire costs of $34 million, as the prior year reflected pre-acquisition write-offs of advance royalty payments deemed to be unrecoverable and (iii) a decrease in distribution costs of $25 million due to the decline in year over year physical sales, the increases in sales in digital formats, lower bad debt expenses and the impact of cost-savings initiatives. These benefits were offset by (i) $20 million of one-time compensation expenses related to employee bonuses paid in connection with the Initial Common Stock Offering and payments associated with our restricted stock and stock option awards granted at prices below fair value and (ii) $24 million of non-recurring charges incurred in connection with the departure of the co-chairman of The Atlantic Records Group and the expensing of certain amounts paid in connection with the acquisition of the remaining interest in the Lava Records joint venture. Excluding these items and a $17 million decrease in restructuring costs, Recorded Music OIBDA increased by $141 million to $431 million and was 15% of Recorded Music revenues for the year ended September 30, 2005.

Recorded Music operating income was $215 million for the twelve months ended September 30, 2005, compared to an operating loss of $934 million for the twelve months ended September 30, 2004. Recorded Music operating income (loss) included the following components:

	Successor	Combined	Successor	Predecessor
	Twelve Months Ended September 30, 2005	Twelve Months Ended September 30, 2004	Seven Months Ended September 30, 2004	Five Months Ended February 29, 2004
	(audited)	(unaudited)	(audited)	(unaudited)
OIBDA	$ 380	$ 266	$ 120	$ 146
Depreciation and amortization	(165)	(181)	(96)	(85)
Impairment of goodwill and other intangible assets	—	(1,019)	—	(1,019)
Operating income (loss)	$ 215	$ (934)	$ 24	$ (958)

The $934 million operating loss in the prior twelve-month period reflects an impairment charge of $1.019 billion recorded to reduce the carrying value of our goodwill and other intangible assets to fair value. Excluding this charge, operating income for the twelve months ended September 30, 2005 improved by $130 million. This improvement related to a decrease in depreciation of $13 million, a decrease in amortization of $3 million, and the $114 million increase in OIBDA described above.

Music Publishing

Music Publishing revenues increased by $6 million to $607 million for the twelve months ended September 30, 2005, compared to $601 million for the twelve months ended September 30, 2004, and represented approximately 17% of consolidated revenues for the twelve months ended September 30, 2005 and

2004. After a benefit from the favorable impact of foreign currency exchange rates of $20 million, Music Publishing revenues declined by $14 million. This decline primarily related to a $15 million decrease in revenues as a result of the sale of our printed sheet music business to a third party on May 31, 2005.

Excluding print revenues through the sale date of $35 million, Music Publishing revenues for the twelve months ended September 30, 2005 consisted of mechanical revenues of $258 million, performance revenues of $192 million, synchronization revenues of $97 million, $20 million of digital revenues and other revenue of $5 million. Music Publishing digital revenues grew by $16 million, to $20 million, as compared to $4 million for the twelve months ended September 30, 2004. Excluding the impact of foreign currency, synchronization revenues increased by approximately $18 million due to favorable market opportunities, such as movie, video game and advertisement deals and continued increases in sales in newer formats. This increase was offset by decreases in performance revenues and mechanical revenues of $16 million and $4 million, respectively. These declines were a direct result of the decline in physical sales, timing of artist and repertoire investments as well as fewer key commercial releases in prior periods.

Music Publishing OIBDA decreased to $141 million for the twelve months ended September 30, 2005, compared to $144 million for the twelve months ended September 30, 2004. Excluding a $2 million benefit from changes in foreign currency exchange rates and $1 million of one-time compensation expenses related to employee bonuses paid in connection with the Initial Common Stock Offering, OIBDA was principally impacted by the revenue decreases explained above, offset by reduced costs as a result of our continued cost-savings initiatives.

Music Publishing operating income increased to $82 million in the twelve months ended September 30, 2005, compared to $74 million in the twelve months ended September 30, 2004. Music Publishing operating income includes the following components:

	Successor	Combined	Successor	Predecessor
	Twelve Months Ended September 30, 2005	Twelve Months Ended September 30, 2004	Seven Months Ended September 30, 2004	Five Months Ended February 29, 2004
	(audited)	(unaudited)	(audited)	(unaudited)
OIBDA	$ 141	$ 144	$ 87	$ 57
Depreciation and amortization	(59)	(70)	(34)	(36)
Operating income	$ 82	$ 74	$ 53	$ 21

The $8 million increase in operating income related to an $11 million decrease in depreciation and amortization offset by the $3 million decrease in OIBDA described above.

Corporate expenses

Corporate expenses before depreciation and amortization expense increased by $122 million to $199 million for the twelve months ended September 30, 2005, compared to $77 million for the twelve months ended September 30, 2004. Corporate expenses for the twelve months ended September 30, 2005 include (i) a $73 million loss on termination of management agreement, more fully described above, (ii) $8 million of one-time compensation expenses consisting of a one-time bonus to employees related to the Company's Initial Common Stock Offering and one-time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date and (iii) a $5 million increase in stock-based compensation expense. Additional increases resulted from higher professional and legal costs associated with pending litigation and investigations and Sarbanes-Oxley compliance and higher costs associated with operating as an independent company.

Ten Months Ended September 30, 2004 Compared to Ten Months Ended September 30, 2003

The following table summarizes our historical results of operations. The financial data for the seven months ended September 30, 2004 and the three months ended February 29, 2004 have been derived from our audited financial statements included elsewhere herein. The financial data for the ten months ended September 30, 2003 are unaudited and are derived from the audited financial statements included elsewhere herein. See "Change in Fiscal Year and Basis of Presentation" presented earlier herein for a discussion of the use of financial information for the combined ten-month period ended September 30, 2004.

	Successor	Predecessor	Combined	Predecessor
	Seven Months Ended September 30, (audited)	Three Months Ended February 29, 2004 (audited)	Ten Months Ended September 30, 2004 (unaudited)	Ten Months Ended September 30, 2003 (unaudited)
	(in millions)			
Revenues	$ 1,769	$ 779	$ 2,548	$ 2,487
Costs and expenses:				
Cost of revenues[1]	(944)	(415)	(1,359)	(1,449)
Selling, general and administrative expenses[1]	(677)	(319)	(996)	(995)
Amortization of intangible assets	(104)	(56)	(160)	(201)
Loss on sale of physical distribution assets	—	—	—	(12)
Restructuring costs	(26)	—	(26)	(27)
Total costs and expenses	(1,751)	(790)	(2,541)	(2,684)
Operating income (loss)	18	(11)	7	(197)
Interest expense, net	(80)	(2)	(82)	(5)
Net investment-related losses	—	—	—	(17)
Equity in the losses of equity-method investees, net	(2)	(2)	(4)	(32)
Deal related transaction and other costs	—	—	—	(7)
Loss on repayment of bridge loan	(6)	—	(6)	—
Unrealized loss on warrants	(120)	—	(120)	—
Other expense, net	(4)	—	(4)	(10)
Minority interest expense	(14)	—	(14)	—
Loss before income taxes	(208)	(15)	(223)	(268)
Income tax benefit (expense)	(30)	(17)	(47)	67
Net loss	$ (238)	$ (32)	$ (270)	$ (201)

(1) Includes depreciation expense of: $36 million for the seven months ended September 30, 2004, $16 million for the three months ended February 29, 2004, $52 million for the ten months ended September 30, 2004 and $71 million for the ten months ended September 30, 2003.

Consolidated Pro Forma Results

As previously discussed, the above table presents our historical operating results separately for each of the pre-acquisition, three-month period ended February 29, 2004 and the post-acquisition, seven-month period ended September 30, 2004. As such, it does not reflect all of the significant effects of the Transactions on our operating results for the entire combined ten-month period ended September 30, 2004. Had the Transactions occurred on December 1, 2003, our pro forma results for the ten months ended September 30, 2004 would have been as follows:

	Pro Forma Ten Months Ended September 30, 2004
	(in millions, unaudited)
Revenue	$ 2,548
OIBDA	217
Depreciation and amortization	(201)
Operating income	16
Interest expense, net	(112)
Net income (loss)	(286)

A discussion of our consolidated historical results follows.

Consolidated Historical Results

Revenues

Our revenues increased to $2.548 billion for the ten months ended September 30, 2004, compared to $2.487 billion for the ten months ended September 30, 2003. The increase was largely driven by a $20 million increase in Recorded Music revenues and a $38 million increase in Music Publishing revenues.

Recorded Music revenues benefited principally from a $110 million favorable impact of foreign currency exchange rates, and an approximate $30 million increase in revenues from digital sales of Recorded Music product relating to the development and increased consumer usage of legal, online distribution channels for the music industry. These benefits more than offset a decline in physical worldwide music sales due to the continuing industry-wide impact of piracy, lower sales volume associated with a fewer number of key commercial releases that sold in excess of one million units and the effects from our cost-savings initiative to consolidate two of our U.S. record labels. Substantially all of the decline in physical worldwide music sales resulted from lower unit sales volume.

Music Publishing revenues benefited principally from a $33 million favorable impact of foreign currency exchange rates and an aggregate $15 million increase in mechanical, performance and synchronization royalties. These benefits more than offset a $10 million decline in revenues from the sale of print-related products partially relating to the closure of certain of our smaller print operations in connection with our cost-savings initiatives.

See "Business Segment Results" presented hereinafter for a discussion of revenues by business segment.

Cost of revenues

Our cost of revenues decreased to $1.359 billion for the ten months ended September 30, 2004, compared to $1.449 billion for the ten months ended September 30, 2003. Expressed as a percentage of revenues, cost of revenues was approximately 53% for the ten months ended September 30, 2004, compared to 58% for the ten months ended September 30, 2003. The decrease in cost of revenues principally related to approximately $98 million of lower manufacturing costs due, in part, to lower pricing under the new Cinram agreements that went into effect in October 2003, approximately $88 million of lower artist and repertoire-related costs

associated with our lower sales volume and cost savings associated with our restructuring plan that was implemented in 2004 in connection with the Acquisition. These cost reductions were partially offset by an approximate $90 million unfavorable impact of foreign currency exchange rates.

Selling, general and administrative expenses

Our selling, general and administrative expenses were $996 million for the ten months ended September 30, 2004, compared to $995 million for the ten months ended September 30, 2003. Expressed as a percentage of revenues, selling, general and administrative expenses were approximately 39% for the ten months ended September 30, 2004, compared with 40% for the ten months ended September 30, 2003. Selling, general and administrative expenses increased as a result of an approximate $50 million unfavorable impact of foreign currency exchange rates, approximately $6 million of management advisory fees paid to the Investor Group and $43 million of higher corporate expenses as discussed further below, including higher costs associated with operating as an independent company. These increases were offset by decreases due to lower marketing and divisional overhead costs associated with our cost-savings initiatives.

Restructuring costs

We recognized $26 million of restructuring-related costs in the ten months ended September 30, 2004, compared to $27 million of restructuring-related costs in the ten months ended September 30, 2003. The restructuring costs in 2004 principally related to costs associated with the implementation of a cost-savings incentive compensation plan designed to incentivize management to reduce operating costs. The restructuring costs in 2003 principally related to reductions in worldwide headcount, costs to exit certain leased facilities, and costs associated with the restructuring of U.S. and Canadian distribution operations.

Reconciliation of Consolidated Historical OIBDA to Operating Income (Loss) and Net Loss

As previously described, we use OIBDA as our primary measure of financial performance. The following table reconciles OIBDA to operating income (loss), and further provides the components from operating income (loss) to net loss for purposes of the discussion that follows (in millions):

	Successor	Predecessor	Combined	Predecessor
	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2004	Ten Months Ended September 30, 2003
	(audited)	(audited)	(unaudited)	(unaudited)
OIBDA	$ 158	$ 61	$ 219	$ 75
Depreciation expense	(36)	(16)	(52)	(71)
Amortization expense	(104)	(56)	(160)	(201)
Operating (loss) income	18	(11)	7	(197)
Interest expense, net	(80)	(2)	(82)	(5)
Net investment-related losses	—	—	—	(17)
Equity in the losses of equity-method investees, net	(2)	(2)	(4)	(32)
Deal-related transaction and other costs	—	—	—	(7)
Loss on repayment of bridge loan	(6)	—	(6)	—
Unrealized loss on warrants	(120)	—	(120)	—
Other expense, net	(4)	—	(4)	(10)
Minority interest expense	(14)	—	(14)	—
Loss before income taxes	(208)	(15)	(223)	(268)
Income tax benefit (expense)	(30)	(17)	(47)	67
Net loss	$ (238)	$ (32)	$ (270)	$ (201)

OIBDA

Our OIBDA increased to $219 million for the ten months ended September 30, 2004, compared to $75 million for the ten months ended September 30, 2003. The increase related to a $150 million increase in Recorded Music OIBDA and a $37 million increase in Music Publishing OIBDA, offset in part by a $43 million increase in Corporate expenses.

Recorded Music OIBDA benefited principally from lower marketing and overhead costs associated with our cost-savings initiatives, approximately $94 million of lower manufacturing costs due, in part, to lower pricing under the new Cinram agreements that went into effect in October 2003, a $1 million favorable impact from foreign currency exchange rates and the absence of a $12 million loss on the sale of physical distribution assets recognized in 2003. These benefits more than offset the loss of margin contributions related to lower worldwide recorded music sales.

Music Publishing OIBDA benefited principally from lower overhead costs associated with our cost-savings initiatives, approximately $18 million of lower advance write-offs and a $4 million favorable impact from foreign currency exchange rates.

Corporate expenses increased due to higher costs associated with operating as an independent company and a change in the allocation of corporate-related costs. As discussed in Note 20 to the audited financial statements, $47 million of corporate-related costs were allocated in 2003 to Time Warner's former CD and DVD manufacturing and printing operations because such operations were managed by Old WMG. Such operations were sold by Time Warner in October 2003, and accordingly, such costs were no longer allocable. The incrementally higher level of costs was partially offset by lower overhead costs associated with our cost-savings initiatives.

See "Business Segment Results" presented hereinafter for a discussion of OIBDA by business segment.

Depreciation expense

Our depreciation expense decreased to $52 million for the ten months ended September 30, 2004, compared to $71 million for the ten months ended September 30, 2003. The decrease principally related to lower capital spending requirements and lower depreciation of software development costs.

Amortization expense

Our amortization expense decreased to $160 million for the ten months ended September 30, 2004, compared to $201 million for the ten months ended September 30, 2003. The decrease related to the new basis of accounting recorded in connection with the Acquisition, which resulted in a lower revaluation of the historical cost bases of our identifiable intangible assets.

Operating income (loss)

Our operating income increased to $7 million for the ten months ended September 30, 2004, compared to an operating loss of $197 million for the ten months ended September 30, 2003. The improvement in operating income related to a $144 million increase in OIBDA, a $19 million decrease in depreciation expense, and a $41 million decrease in amortization expense, all as previously described above. See "Business Segment Results" presented hereinafter for a discussion of operating income (loss) by business segment.

Interest expense, net

Our net interest expense increased to $82 million for the ten months ended September 30, 2004, compared to $5 million for the ten months ended September 30, 2003. The increase primarily related to the approximately $1.8 billion of debt issued in 2004 in connection with the capitalization of the Company.

Net investment-related losses

We did not recognize any investment-related losses for the ten months ended September 30, 2004. However, for the ten months ended September 30, 2003, we recognized $17 million of net investment-related losses. These losses principally related to reductions in the carrying values of certain equity-method investments.

Equity in the losses of equity-method investees, net

Our equity in the losses of equity-method investees was $4 million for the ten months ended September 30, 2004, compared to $32 million in the ten months ended September 30, 2003. The lower losses partially related to the fact that certain of our former loss-generating investees, such as our former interest in MusicNet, were retained by Time Warner and were not part of the assets acquired in the Acquisition.

Deal-related transaction costs

We did not recognize any deal-related transaction costs for the ten months ended September 30, 2004. However, for the ten months ended September 30, 2003, we recognized $7 million of deal-related transaction costs. These costs primarily related to transaction costs associated with the prior pursuit of other strategic ventures or dispositions of Old WMG's businesses in 2003 by Time Warner that did not occur.

Loss on repayment of bridge loan

We recognized a $6 million loss during the ten months ended September 30, 2004 to write off the carrying value of the unamortized debt issuance costs related to our bridge loan which we repaid in April 2004.

Unrealized loss on warrants

We recognized a $120 million unrealized loss on stock warrants issued to Historic TW in connection with the Acquisition for the ten months ended September 30, 2004. Because the ten-month period ended September 30, 2003 was pre-Acquisition, the stock warrants were not outstanding and no comparable charge was recognized for that period.

Other expense, net

We recognized other expense, net, of $4 million for the ten months ended September 30, 2004, compared to other expense, net, of $10 million for the ten months ended September 30, 2003. The $4 million of costs in 2004 relate to unfavorable foreign currency exchange rate movements associated with intercompany receivables and payables that are not of a long-term investment nature, and as such, are required to be reported in the statement of operations in accordance with GAAP. The $10 million of costs in 2003 primarily related to losses on foreign currency exchange contracts that were used by Time Warner to hedge exposures to changes in foreign currency exchange rates. As discussed in Note 22 to the audited financial statements included elsewhere herein, we are in the process of evaluating our hedging practices and no significant foreign exchange contracts were entered into in 2004.

Minority interest expense

We recognized minority interest expense of $14 million for the ten months ended September 30, 2004. This expense related to dividends on preferred stock of Holdings that was held directly by the Investor Group and was issued in connection with the initial funding of the purchase price for the Acquisition. Because the ten-month period ended September 30, 2003 was pre-Acquisition, the subsidiary preferred stock was not outstanding and no comparable charge was recognized for that period.

Income tax benefit (expense)

We provided income tax expense of $47 million for the ten months ended September 30, 2004, compared to an income tax benefit of $67 million for the ten months ended September 30, 2003. The income tax provisions

and benefits are not entirely comparable due to the changes in our tax profile relating to the closing of the Acquisition. In particular, prior to the closing of the Acquisition, we were a member of the Time Warner consolidated tax return and were able to recognize U.S.-based deferred tax benefits on domestic-source net operating losses incurred. However, upon the closing of the Acquisition, our membership in the Time Warner consolidated tax group terminated along with our ability to recognize similar, U.S.-based deferred tax benefits. Accordingly, the income tax expense in 2004 primarily related to the tax provisions on foreign-source income. There was no offsetting income tax benefit on domestic-source losses recognized in 2004 due to the uncertainty of realization of those deferred tax assets.

Net loss

We recognized a net loss of $270 million for the ten months ended September 30, 2004, compared to a net loss of $201 million for the ten months ended September 30, 2003. As described more fully above, the higher net loss in 2004 principally related to $14 million of higher minority interest charges, $77 million of higher net interest costs, a $114 million higher income tax provision associated with the improvement in pretax losses and $120 million of unrealized losses on the warrants. These losses were offset, in part, by a $204 million increase in operating income (including $60 million of lower depreciation and amortization expense) and $45 million of lower investment-related losses.

Business Segment Results

Revenue, OIBDA and operating income (loss) by business segment are as follows (in millions):

	Successor	Predecessor	Combined	Predecessor
	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2004	Ten Months Ended September 30, 2003
	(audited)	(audited)	(unaudited)	(unaudited)
Recorded Music				
Revenue	$ 1,429	$ 630	$ 2,059	$ 2,039
OIBDA[1]	$ 120	$ 38	$ 158	8
Operating income (loss)[1]	$ 24	$ (9)	$ 15	(181)
Music Publishing				
Revenue	$ 348	$ 157	$ 505	467
OIBDA[1]	$ 87	$ 38	$ 125	88
Operating income (loss)[1]	$ 53	$ 17	$ 70	19
Corporate and Revenue Eliminations				
Revenue eliminations	$ (8)	$ (8)	$ (16)	(19)
OIBDA[1]	$ (49)	$ (15)	$ (64)	(21)
Operating income (loss)[1]	$ (59)	$ (19)	$ (78)	(35)
Total				
Revenue	$ 1,769	$ 779	$ 2,548	2,487
OIBDA[1]	$ 158	$ 61	$ 219	75
Operating income (loss)[1]	$ 18	$ (11)	$ 7	(197)

(1) OIBDA and operating income for the ten months ended September 30, 2004 have each been reduced by $26 million of restructuring costs. Of such amount, $17 million related to Recorded Music, $1 million related to Music Publishing, and $8 million related to Corporate. For the ten months ended September 30, 2003, OIBDA and operating income (loss) have each been reduced by $39 million of losses related to restructuring costs and the loss on the sale of physical distribution assets. Of such amount, $36 million related to Recorded Music and $3 million related to Music Publishing.

Recorded Music

Recorded Music revenues increased to $2.059 billion for the ten months ended September 30, 2004, compared to $2.039 billion for the ten months ended September 30, 2003. Revenues benefited principally from a $110 million favorable impact of foreign currency exchange rates and an approximate $30 million increase in revenues from digital sales of recorded music product relating to the development and increased consumer usage of legal, online distribution channels for the music industry. These benefits more than offset a decline in physical worldwide music sales due to the continuing industry-wide impact of piracy, lower sales volume associated with a fewer number of key commercial releases that sold in excess of one million units and the effects from our cost-savings initiative to consolidate two of our U.S. record labels. Substantially all of the decline in physical worldwide music sales resulted from lower unit sales volume.

Recorded Music OIBDA increased to $158 million for the ten months ended September 30, 2004, compared to $8 million for the ten months ended September 30, 2003. The $150 million increase in OIBDA principally related to lower marketing and overhead costs associated with our cost-savings initiatives, approximately $94 million of lower manufacturing costs due, in part, to lower pricing under the new Cinram agreements that went into effect in October 2003, a $1 million favorable impact from foreign currency exchange rates and the absence of $12 million loss on the sale of physical distribution assets recognized in 2003. These benefits more than offset the loss of margin contributions related to lower worldwide recorded music sales.

Recorded Music operating income improved to $15 million for the ten months ended September 30, 2004, compared to a loss of $181 million for the ten months ended September 30, 2003. Recorded Music operating loss included the following components (in millions):

	Successor	Predecessor	Combined	Predecessor
	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2004	Ten Months Ended September 30, 2003
	(audited)	(audited)	(unaudited)	(unaudited)
OIBDA	$ 120	$ 38	$ 158	$ 8
Depreciation and amortization	(96)	(47)	(143)	(189)
Operating income (loss)	$ 24	$ (9)	$ 15	$ (181)

The $196 million improvement in operating loss primarily related to the $150 million improvement in OIBDA discussed above and a $46 million decrease in depreciation and amortization expense. The decrease in depreciation and amortization expense principally related to $29 million of lower amortization resulting from a lower revaluation of the historical cost bases of our identifiable intangible assets in connection with the allocation of purchase price as part of the Acquisition. In addition, depreciation expense declined by $17 million principally relating to lower capital spending requirements and lower depreciation of software development costs.

Music Publishing

Music Publishing revenues increased to $505 million for the ten months ended September 30, 2004, compared to $467 million for the ten months ended September 30, 2003. Revenues benefited principally from a $33 million favorable impact of foreign currency exchange rates, and an aggregate $15 million increase in mechanical, performance and synchronization royalties. These benefits more than offset a $10 million decline in revenues from the sale of print-related products partially relating to the closure of certain of our smaller print operations in connection with our cost-savings initiatives.

The aggregate $15 million increase in royalties noted above consisted of a $4 million increase in mechanical royalties, a $6 million increase in synchronization royalties and a $5 million increase in performance royalties. Mechanical and synchronization revenues increased as a result of our breadth and number of top-performing songs, as well as an increase in sales in newer formats, such as music DVDs and mobile phone ringtones. Performance revenues increased due in large part to an increase in media channels.

Music Publishing OIBDA increased to $125 million for the ten months ended September 30, 2004, compared to $88 million for the ten months ended September 30, 2003. The $37 million increase in OIBDA principally related to lower overhead costs associated with our cost-saving initiatives, approximately $18 million of lower advance write-offs and a $4 million favorable impact from foreign currency exchange rates.

Music Publishing operating income increased to $70 million in the ten months ended September 30, 2004, compared to $19 million in the ten months ended September 30, 2003. Music Publishing operating income includes the following components (in millions):

	Successor	Predecessor	Combined	Predecessor
	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2004	Ten Months Ended September 30, 2003
	(audited)	(audited)	(unaudited)	(unaudited)
OIBDA	$ 87	$ 38	$ 125	$ 88
Depreciation and amortization	(34)	(21)	(55)	(69)
Operating income	$ 53	$ 17	$ 70	$ 19

The $51 million increase in operating income primarily related to a $14 million decrease in depreciation and amortization expense, and the $37 million increase in OIBDA discussed above. The decrease in depreciation and amortization expense principally related to $12 million of lower amortization expense resulting from a lower revaluation of the historical cost bases of our identifiable intangible assets in connection with the allocation of purchase price as part of the Acquisition.

Corporate expenses

Corporate expenses before depreciation and amortization expense increased to $64 million for the ten months ended September 30, 2004, compared to $21 million for the ten months ended September 30, 2003. Corporate expenses increased due to higher costs associated with operating as an independent company and a change in the allocation of corporate-related costs. As discussed in Note 20 to the audited financial statements, $47 million of corporate-related costs were allocated in 2003 to Time Warner's former CD and DVD manufacturing and printing operations because such operations were managed by Old WMG. Such operations were sold by Time Warner in October 2003, and accordingly, such costs were no longer allocable. The incrementally higher level of costs was partially offset by lower overhead costs associated with our cost-savings initiatives.

Corporate depreciation and amortization expense was $14 million in each period.

FINANCIAL CONDITION AND LIQUIDITY

Financial Condition at September 30, 2005

At September 30, 2005, we had $2.246 billion of debt, $288 million of cash and equivalents (net debt of $1.958 billion, defined as total debt less cash and equivalents) and $89 million of shareholders' equity. This compares to $1.840 billion of debt, $555 million of cash and equivalents (net debt of $1.285 billion) and $280 million of shareholders' equity at September 30, 2004. The increase in debt resulted from the issuance of $697 million of Holdings debt in December 2004, of which all but $170 million was redeemed on June 15, 2005 (carrying value of $174 million as of September 30, 2005), and the borrowing of an additional $250 million of term loans under the Company's senior secured credit facility, offset by our quarterly repayment of our term loans under the senior secured credit facility.

The $191 million reduction in shareholders' equity that occurred during the twelve months ended September 30, 2005 principally related to a return of capital of $422 million paid in December 30, 2004 from the

proceeds of the Holdings Notes, a return of capital of $50 million paid in installments in March and May of 2005, a dividend of $100.5 million paid to our common shareholders immediately prior the Company's Initial Common Stock Offering, a payment of the remaining preference amount of the Class L Common Stock of $8.5 million (after which, such stock converted to Class A Common Stock), the termination of the Management Agreement resulting in a $73 million termination fee and the charges of $35 million incurred in relation to the repayment of certain of the Holdings Notes on June 15, 2005. Such reductions were offset, in part, by the Company's Initial Common Stock Offering, which resulted in additional equity of $522 million.

Cash Flows

The following table summarizes our historical cash flows. The financial data for the twelve months ended September 30, 2005, the seven months ended September 30, 2004 and the year ended November 30, 2003 have been derived from our audited financial statements included elsewhere herein. The financial data for the five and three months ended February 29, 2004 are unaudited and are derived from our interim financial statements. The financial data for the ten months ended September 30, 2003 are unaudited and are derived from the audited financial statements included elsewhere herein. See "Change in Fiscal Year and Basis of Presentation" presented earlier herein for a discussion of the use of financial information for the combined twelve-month and ten-month periods ended September 30, 2004.

	Successor	Combined	Combined	Successor	Predecessor		
	Twelve Months Ended September 30, 2005	Twelve Months Ended September 30, 2004	Ten Months Ended September 30, 2004	Seven Months Ended September 30, 2004	Five Months Ended February 29, [illegible]	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2003
	(audited)	(unaudited)	(unaudited)	(audited)	(unau	(audited)	(unaudited)
				(in millions)			
Operating activities	$ 205	$ 438	$ 407	$ 86	$ 352	$ 321	$ 257
Investing activities	(54)	(2,646)	(2,649)	(2,663)	17	14	(73)
Financing activities	(416)	2,679	2,651	2,661	18	(10)	(151)

Operating Activities

Cash provided by operations was $205 million for the twelve months ended September 30, 2005, compared to cash provided by operations of $438 million for the twelve months ended September 30, 2004. The $233 million decrease in cash provided by operations resulted primarily from the payment of a $73 million fee as a result of the termination of the Management Agreement and $88 million of higher interest payments associated with our leveraged capital structure. The decrease also reflects cash paid of $10 million to our employees in connection with the our Initial Common Stock Offering and cash paid of $16 million for certain of the other one-time special bonuses paid to certain holders of restricted stock and stock options, as well as the timing of the funding of our working capital requirements.

Investing Activities

Cash used in investing activities was $54 million for the twelve months ended September 30, 2005, compared to $2.646 billion for the twelve months ended September 30, 2004. The decrease in cash used in investing activities primarily related to the cash purchase price of $2.638 billion, including transaction costs, paid in connection with the Acquisition. Cash paid in investing activities for the twelve months ended September 30, 2005 primarily relates to amounts paid to acquire an interest in Bad Boy Records, an additional interest in Maverick, cash paid to fund various investments and to acquire additional music publishing copyrights, offset by the proceeds from the sale of our printed sheet music business. Cash used in investing activities also reflects $30 million of capital expenditures.

Financing Activities

Cash used in financing activities was $416 million for the twelve months ended September 30, 2005, compared to $2.679 billion of cash provided for the twelve months ended September 30, 2004. Cash flows from financing activities are not comparable from period to period. We began operating as an independent company on March 1, 2004. However, prior to March 1, 2004, we were owned by Time Warner and, as such, all of our cash requirements were funded by Time Warner and Time Warner received most of the cash generated by us through a centralized cash management system or use of shared international cash pooling arrangements. Consequently, except for principal payments on capital leases and certain net borrowings of third-party debt, which were not significant, all financing activities for the historical 2004 period related to movement of cash between Time Warner and us.

Cash provided by financing activities for 2004 principally reflected activities to fund the purchase price paid in connection with the Acquisition, settle intercompany receivables and payables for the period preceding the Acquisition, and modify our initial capital structure by returning a portion of the initial capital contributed by the Investor Group. In particular, we borrowed $1.650 billion, which was used primarily to fund a portion of the purchase price paid in connection with the Acquisition (including transaction costs) and to pay $78 million of financing-related debt issuance costs. We also received capital contributions of $1.250 billion from the Investor Group to fund a portion of the purchase price paid in connection with the Acquisition. In April 2004, we refinanced certain of our debt at the Acquisition Corp. level, including the repayment of the remaining balance of the bridge loan of $506 million, the issuance of the U.S. dollar and Sterling denominated notes by Acquisition Corp. for approximately $650 million, and additional term loan borrowings under our senior secured credit facility of approximately $50 million. With respect to the pre-acquisition, five-month period ended February 29, 2004, $290 million of net funding was received by Time Warner and used, in part, to repay $124 million of third-party indebtedness.

Cash used in financing activities for the twelve months ended September 30, 2005 primarily relates to the repayment of a portion of the Holdings Notes for $574 million, quarterly term loan debt repayments of $14 million, the returns of capital and dividends paid to the Investor Group of $917 million, the $209 million redemption of subsidiary preferred stock as part of the Holdings Refinancing, and $138 million paid to repurchase the three-year warrants from Time Warner. These uses of cash were offset principally by $522 million of net proceeds after stock-issuance costs from the Company's Initial Common Stock Offering, $681 million of net proceeds after debt-issuance costs from the issuance of Holdings debt as part of the Holdings Refinancing and $247 million of net proceeds after debt-issuance costs from the additional term loan borrowings under the senior secured credit facility.

Liquidity

Our primary sources of liquidity are the cash flow generated from our subsidiaries' operations, availability under the $250 million (less $4 million of outstanding letters of credit as of September 30, 2005) revolving credit portion of our senior secured credit facility and available cash and equivalents. These sources of liquidity are needed to fund our debt service requirements, working capital requirements, capital expenditure requirements, regular quarterly dividends and the remaining one-time costs associated with the execution of our restructuring plan. We believe that our existing sources of cash will be sufficient to support our existing operations over the next twelve months.

As of September 30, 2005, our long-term debt consisted of $1.430 billion of borrowings (including $17 million of debt that is classified as a current obligation) under the term loan portion of our senior secured credit facility, $642 million of Acquisition Corp. Subordinated Notes and $174 million of Holdings Notes. There were no borrowings under the revolving portion of our senior secured credit facility as of September 30, 2005.

Senior Secured Credit Facility

The senior secured credit facility consists of a $1.430 billion outstanding term loan portion and a $250 million revolving credit portion. During the twelve months ended September 30, 2005 we borrowed an additional

$250 million under the credit facility, which resulted in an increase in the outstanding term loan balance as compared to September 30, 2004. The term loan portion of the facility, including the $250 million of new borrowings, matures in February 2011. We are required to prepay outstanding term loans, subject to certain exceptions and conditions, with excess cash flow or in the event of certain asset sales and casualty and condemnation events and incurrence of debt. We are required to make minimum repayments under the term loan portion of our facility in quarterly principal amounts of approximately $4.2 million through November 2010, with a remaining balloon payment in February 2011. The revolving credit portion of the senior secured credit facility matures in February 2010. There are no mandatory reductions in borrowing availability for the revolving credit portion of the facility through its term.

Borrowings under both the term loan and revolving credit portion of the senior secured credit facility currently bear interest at a rate equal to an applicable margin plus, at our option, either (a) a base rate determined by reference to the higher of (1) the prime rate of Bank of America, N.A. and (2) the federal funds rate plus 1/2 of 1% or (b) a LIBOR rate determined by reference to the costs of funds for deposits in the currency of such borrowing for the interest period relevant to such borrowing adjusted for certain additional costs. As of September 30, 2005, the applicable margins with respect to base rate borrowings and LIBOR borrowings were 1.25% and 2.25%, respectively, for borrowings under the revolving credit facility. The applicable margins are variable subject to changes in certain leverage ratios. For borrowings under the term loan facility, the margins with respect to the base rate borrowings and LIBOR borrowings are 1.00% and 2.00%, respectively, but will be 0.75% and 1.75%, respectively if the senior secured debt of Acquisition Corp. is rated at least BB by S&P and Ba2 by Moody's.

In addition to paying interest on outstanding principal under the senior secured credit facility, we are required to pay a commitment fee to the lenders under the revolving credit facility in respect of the unutilized commitments. The initial commitment fee rate was 0.5%. As of September 30, 2005, the commitment fee rate was 0.375%. The commitment fee rate is variable subject to changes in certain of our leverage ratios. We also are required to pay customary letter of credit fees, as necessary.

The senior secured credit facility contains a number of covenants that, among other things, restrict, subject to certain exceptions, our ability and the ability of our subsidiaries to sell assets, incur additional indebtedness or issue preferred stock, repay other indebtedness, pay dividends and distributions or repurchase capital stock, create liens on assets, make investments, loans or advances, make certain acquisitions, engage in mergers or consolidations, engage in certain transactions with affiliates, amend certain material agreements, change the business conducted by us and enter into agreements that restrict dividends from subsidiaries. In addition, the senior secured credit facility requires us to maintain the following financial covenants: a maximum total leverage ratio and a minimum interest coverage ratio, both tested quarterly, and a maximum annual capital expenditures limitation.

Senior Subordinated Notes of Acquisition Corp.

Acquisition Corp. has outstanding two tranches of senior subordinated notes due 2014: $465 million principal amount of U.S. dollar-denominated notes and £100 million principal amount of Sterling-denominated notes (collectively, the "Subordinated Notes"). The Subordinated Notes mature on April 15, 2014. The Subordinated Notes bear interest at a fixed rate of 7 3/8 % per annum on the $465 million dollar notes and 8 3/8 % per annum on the £100 million sterling notes. The indenture governing the notes limits our ability and the ability of our restricted subsidiaries to incur additional indebtedness or issue certain preferred shares; to pay dividends on or make other distributions in respect of its capital stock or make other restricted payments; to make certain investments; to sell certain assets; to create liens on certain debt without securing the notes; to consolidate, merge, sell or otherwise dispose of all or substantially all of our assets; to enter into certain transactions with affiliates; and to designate our subsidiaries as unrestricted subsidiaries. Subject to certain exceptions, the indenture governing the notes permits us and our restricted subsidiaries to incur additional indebtedness, including secured indebtedness, and to make certain restricted payments and investments.

Holdings Notes

In December 2004, Holdings issued $847 million principal amount of debt. The $847 million principal amount of Holdings' debt consisted of (i) $250 million principal amount of Floating Rate Senior Notes due 2011 (the "Holdings Floating Rate Notes"), (ii) $397 million principal amount at maturity of 9.5% Senior Discount Notes due 2014, which had an initial issuance discount of $147 million (the "Holdings Discount Notes") and (iii) $200 million principal amount of Floating Rate Senior PIK Notes due 2014 (the "Holdings PIK Notes", and collectively, the "Holdings Notes").

In connection with the Company's Initial Common Stock Offering, we used $517 million of proceeds from the offering along with $57 million of available cash to redeem certain of the Holdings Notes outstanding. As of September 30, 2005, Holdings had $174 million of debt on its balance sheet relating to such securities, net of issuance discounts.

The Holdings Floating Rate Notes were redeemed in full on June 15, 2005. From the issuance date through the redemption date, the notes bore interest at a quarterly floating rate based on three-month LIBOR rates plus a margin equal to 4.375%. Interest was payable quarterly in cash beginning on March 15, 2005.

The Holdings Discount Notes were issued at a discount and had an initial accreted value of $630.02 per $1,000 principal amount at maturity. Prior to December 15, 2009, no cash interest payments are required. However, interest accrues on the Holdings Discount Notes in the form of an increase in the accreted value of such notes such that the accreted value of the Holdings Discount Notes will equal the principal amount at maturity on December 15, 2009. Thereafter, cash interest on the Holdings Discount Notes is payable semiannually at a fixed rate of 9.5% per annum. The Holdings Discount Notes mature on December 15, 2014. The Company redeemed 35% of the Holdings Discount Notes on June 15, 2005.

The Holdings PIK Notes were redeemed in full on June 15, 2005. From the date of issuance through the date of redemption, the notes bore interest at a semi-annual floating rate based on six-month LIBOR rates plus a margin equal to 7%. Interest was accrued in the form of additional PIK notes at the election of the Company. Such amounts were also repaid in connection with the redemption.

The terms of the indentures governing the Acquisition Corp. Subordinated Notes and Holdings Notes significantly restrict Acquisition Corp., Holdings and other subsidiaries from paying dividends and otherwise transferring assets to us. For example, the ability of Acquisition Corp. and Holdings to make such payments is governed by a formula based on 50% of each of their consolidated net income (which, as defined in the indentures governing such notes, excludes goodwill impairment charges and any after-tax extraordinary, unusual or nonrecurring gains and losses) accruing from June 1, 2004 and July 1, 2004, respectively. In addition, as a condition to making such payments to us based on such formula, Acquisition Corp. and Holdings must each have an adjusted EBITDA to interest expense ratio of at least 2.0 to 1 after giving effect to any such payments. Acquisition Corp. may also make a restricted payment prior to April 15, 2009 if, immediately after giving pro forma effect to such restricted payment and any indebtedness incurred to finance such restricted payment, its net indebtedness to adjusted EBITDA ratio would not exceed 3.75 to 1 and its net senior indebtedness to adjusted EBITDA ratio would not exceed 2.50 to 1. In addition, Holdings may make a restricted payment if, immediately after giving pro forma effect to such restricted payment and any indebtedness incurred to finance such restricted payment, its net indebtedness to adjusted EBITDA ratio would not exceed 4.25 to 1.0. Notwithstanding such restrictions, the indentures permit an aggregate of $45.0 million and $75.0 million of such payments to be made by Acquisition Corp. and Holdings, respectively, whether or not there is availability under the formula or the conditions to its use are met. Acquisition Corp.'s senior secured credit agreement permits Acquisition Corp. to make additional restricted payments to Holdings, the proceeds of which may be utilized by Holdings to make additional restricted payments, in an aggregate amount not to exceed $10.0 million (such amount subject to increase to $35.0 million if the leverage ratio as of the last day of the immediately preceding four fiscal quarters was less than 4.0 to 1 and to $50.0 million if the leverage ratio as of the last day of the immediately preceding four fiscal quarters was less than 3.5 to 1), and subject to further increase in an amount equal to 50% of

cumulative excess cash flow that is not otherwise applied pursuant to Acquisition Corp.'s senior secured credit agreement, and, in addition, permits Acquisition Corp. to make restricted payments to Holdings, the proceeds of which may be utilized by Holdings to make additional restricted payments not to exceed $90 million in any fiscal year, provided that the proceeds of such restricted payments shall be applied soley to pay cash dividends on the common stock of Warner Music Group Corp. Furthermore, Holdings' subsidiaries will be permitted under the terms of Acquisition Corp.'s existing senior secured credit agreement, as it may be amended, and under other indebtedness, to incur additional indebtedness that may restrict or prohibit the making of distributions, the payment of dividends or the making of loans by such subsidiaries to Holdings.

Initial Common Stock Offering

In May 2005, we completed the Initial Common Stock Offering. Prior to the consummation of the Initial Common Stock Offering, we, among other things, renamed all of our outstanding shares of Class A Common Stock as common stock and authorized an approximately 1,139 for 1 split of our common stock. We contributed the net proceeds from the Initial Common Stock Offering of $517 million to Holdings as an equity capital contribution. Holdings used all of such funds and approximately $57 million of cash received through dividends from Acquisition Corp. to redeem all outstanding Holdings Floating Rate Notes, all outstanding Holdings PIK Notes and 35% of the aggregate principal amount of the outstanding Holdings Discount Notes, including redemption premiums and interest obligations through the date of redemption.

Dividends

We intend to pay regular quarterly dividends on our common stock outstanding in an amount not to exceed $80 million per year. Any decision to declare and pay dividends in the future will be made at the discretion of our board of directors and will depend on, among other things, our results of operations, cash requirements, financial condition, contractual restrictions and other factors our board of directors may deem relevant.

On October 3, 2005, the Company declared a dividend on its outstanding common stock. The dividend was paid on November 23, 2005, to shareholders of record as of October 24, 2005, at a rate of $0.13 per share, representing a dividend of approximately $19.3 million in the aggregate (based on outstanding shares of 148,455,312.724 as of September 30, 2005). The portion of the dividend with respect to unvested restricted stock of approximately $1 million will be paid at such time as such shares become vested.

Covenant Compliance

Our borrowing arrangements, including the senior secured credit facility, the Holding Notes and the Acquisition Corp. Subordinated Notes contain certain financial covenants which are tied to ratios based on Adjusted EBITDA, which is defined under the indentures governing the notes as "EBITDA." Adjusted EBITDA (as defined in the indentures) differs from the term "EBITDA" as it is commonly used. In addition to adjusting net income to exclude interest expense, income taxes, and depreciation and amortization, Adjusted EBITDA (as defined in the indentures) also adjusts net income by excluding items or expenses not typically excluded in the calculation of "EBITDA" such as, among other items, (1) any reasonable expenses or charges related to any issuance of securities, investments permitted, permitted acquisitions, recapitalizations, asset sales permitted or indebtedness permitted to be incurred; (2) the amount of any restructuring charges or reserves, subject to certain limitations; (3) any non-cash charges (including any impairment charges); (4) any gain or loss resulting from hedging currency exchange risks; (5) the amount of management, monitoring, consulting and advisory fees paid to the Investor Group; and (6) any net after-tax income or loss from discontinued operations.

Adjusted EBITDA is presented herein because it is a material component of the covenants contained within the aforementioned agreements. Non-compliance with those covenants could result in the requirement to immediately repay all amounts outstanding under those agreements which could have a material adverse effect on our results of operations, financial position and cash flow. Adjusted EBITDA does not represent net income or cash flow from operations as those terms are defined by GAAP and does not necessarily indicate whether cash

flows will be sufficient to fund cash needs. While Adjusted EBITDA and similar measures are frequently used as measures of operations and the ability to meet debt service requirements, these terms are not necessarily comparable to other similarly titled captions of other companies due to the potential inconsistencies in the method of calculation. Adjusted EBITDA does not reflect the impact of earnings or charges resulting from matters that we may consider not to be indicative of our ongoing operations. In particular, the definition of Adjusted EBITDA in the indentures allows us to add back certain non-cash, extraordinary, unusual or non-recurring charges that are deducted in calculating net income. However, these are expenses that may recur, vary greatly and are difficult to predict. Further, our debt instruments require that it be calculated for the most recent four fiscal quarters. As a result, the measure can be disproportionately affected by a particularly strong or weak quarter. Further, it may not be comparable to the measure for any subsequent four-quarter period or any complete fiscal year.

The following is a reconciliation of net loss, which is a GAAP measure of our operating results, to Adjusted EBITDA as defined, and the calculation of fixed charge coverage and Net Indebtedness and not senior indebtedness to Adjusted EBITDA ratios under our indentures governing the notes of Acquisition Corp. and Holdings for the most recently ended four fiscal quarters ended September 30, 2005. The terms and related calculations are defined in the indenture (in millions, except ratios).

	Twelve Months Ended September 30, 2005
Net loss of Warner Music Group	$ (169)
Minority interest expense	(5)
Warrant mark-to-market—Warner Music Group Corp.	17
Interest expense—Warner Music Group Corp.	(1)
Net loss of WMG Holdings Corp.	(180)
Loss on repayment of Holdings Notes—WMG Holdings Corp	(35)
Interest expense—WMG Holdings Corp	(35)
Net loss of WMG Acquisition Corp.	(110)
Interest expense, net	146
Income tax expense	55
Depreciation and amortization	238
Management fees(a)	79
Restructuring costs(b)	7
Equity in losses of equity method investees(c)	(1)
Net investment-related gains(d)	1
Non-cash compensation expense(e)	25
Adjusted EBITDA(f)	$ 440
Fixed Charges—WMG Acquisition Corp(g)	$ 111
Fixed Charges—WMG Holdings(h)	$ 121
Net Indebtedness—WMG Acquisition Corp.	$ 1,824
Net Indebtedness—WMG Holdings Corp.	$ 1,998
Fixed charges coverage ratio—WMG Acquisition Corp(i)	3.96x
Fixed charges coverage ratio—WMG Holdings(i)	3.63x
Net Indebtedness to Adjusted EBITDA ratio—WMG Acquisition Corp.(j)	4.15x
Net Senior Indebtedness to Adjusted EBITDA ratio—WMG Acquisition Corp.(j)	2.69x
Net Indebtedness to Adjusted EBITDA ratio—WMG Holdings(j)	4.54x

(a) Reflects management fees paid to the Investors for management advisory services.

(b) Reflects costs associated with restructurings.

(c) Represents our share of the net income of investments in companies accounted for using the equity method.

(d) Represents the gain on the sale of an equity method investment.

(e) Reflects costs of stock-based compensation accounted for under FAS 123.

(f) Includes certain non-recurring items, which we are not permitted to add back to net income under the indentures, including (i) $10 million of one-time bonuses paid in connection with the Initial Common Stock Offering, (ii) $19 million of one-time payments associated with our restricted stock and stock option awards granted at prices below the fair market value and (iii) a $24 million incurred in connection with the departure of the co-chairman of The Atlantic Records Group and the expensing of certain amounts paid in connection with the acquisition of the remaining interests of the Lava Records joint venture.

(g) Fixed charges is defined in the indenture governing the Acquisition Corp. Subordinated Notes as consolidated interest expense excluding certain noncash interest expense.

(h) Fixed charges is defined in the indenture governing the Holdings Notes as consolidated interest expense excluding certain noncash interest expense. Pro forma effect has been given to fixed charges for the Holdings Notes as if they had been issued as of October 1, 2004.

(i) In order to be in compliance with certain debt covenants, the Fixed Charge coverage ratio needs to exceed a 2.0x ratio.

(j) In order for Acquisition Corp. to make certain restricted payments, including payments to Holdings on a pro forma basis after giving effect to such payments, its Net Indebtedness to Adjusted EBITDA ratio needs to be lower than 3.75x, and its Net Senior Indebtedness to Adjusted EBITDA ratio needs to be lower than 2.5x. In order for Holdings to make certain restricted payments, including payments to Warner Music Group Corp., its Net Indebtedness to Adjusted EBITDA ratio needs to be lower than 4.25x. Acquisition Corp. and Holdings may make additional restricted payments using certain other exceptions provided for in the indenture governing the Acquisition Corp. Notes and Holdings Notes, respectively.

The indentures governing the notes, subject to certain exceptions, also require the applicable issuer to have a Fixed Charge Coverage Ratio of at least 2.0 to 1.0 in order to incur additional debt.

Summary

Management believes that future funds generated from our operations and available borrowing capacity will be sufficient to fund our debt service requirements, working capital requirements, capital expenditure requirements, payment of regular dividends on our common stock and the remaining one-time costs associated with the execution of the restructuring plan for the foreseeable future. However, our ability to continue to fund these items and to reduce debt may be affected by general economic, financial, competitive, legislative and regulatory factors, as well as other industry-specific factors such as the ability to control music piracy.

Contractual and Other Obligations

Firm Commitments

The following table summarizes the Company's aggregate contractual obligations at September 30, 2005, and the estimated timing and effect that such obligations are expected to have on the Company's liquidity and cash flow in future periods. We expect to fund the firm commitments with operating cash flow generated in the normal course of business and availability under the $250 million (including $4 million of letters of credit) revolving credit portion of the senior secured credit facility.

	Fiscal years			
Firm Commitments and Outstanding Debt	2006	2007-2009	2010 and Thereafter	Total
	(in millions)			
Term loan facility	$ 17	$ 51	$ 1,362	$ 1,430
Acquisition Corp. Notes	—	—	642	642
Holdings Notes	—	—	174	174
Operating leases	34	104	225	363
Artist, songwriter and co-publisher commitments	74	221	74	369
Minimum funding commitments to investees and other obligations	10	38	2	50
Total firm commitments and outstanding debt	$ 135	$ 414	$ 2,479	$ 3,028

The following is a description of our firmly committed contractual obligations at September 30, 2005:

- Operating lease obligations primarily relate to the minimum lease rental obligations for our real estate and operating equipment in various locations around the world. These obligations have been presented without the benefit of $16 million of sublease income expected to be received under non-cancelable agreements.

- We enter into long-term commitments with artists, songwriters and co-publishers for the future delivery of music product. Aggregate firm commitments to such talent approximated $369 million across hundreds of artists, songwriters, publishers, songs and albums at September 30, 2005. Such commitments, which are unpaid advances across multiple albums and songs, are payable principally over a ten-year period, generally upon delivery of albums from the artists or future musical compositions by songwriters and co-publishers. Because the timing of payment, and even whether payment occurs, is dependent upon the timing of delivery of albums and musical compositions from talent, the timing and amount of payment of these commitments as presented in the above summary can vary significantly.

- We have minimum funding commitments and other related obligations to support the operations of various investments.

MARKET RISK MANAGEMENT

We are exposed to market risk arising from changes in market rates and prices, including movements in foreign currency exchange rates and interest rates.

Foreign Currency Risk

We have significant transactional exposure to changes in foreign currency exchange rates relative to the U.S. dollar due to the global scope of our operations. For the twelve months ended September 30, 2005, approximately $1.8 billion, or 52%, of our revenues were generated outside of the U.S. The top five revenue-producing international countries are the U.K., France, Germany, Japan and Italy, which use the British pound sterling, euro and Japanese yen as currencies, respectively. See Note 23 to our audited financial statements included elsewhere herein for information on our operations in different geographical areas.

Historically, we have used (and continue to use) foreign exchange contracts, primarily to hedge the risk that unremitted or future royalties and license fees owed to our 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. In addition, we hedge foreign currency risk associated with financing transactions such as third party and inter-company debt.

We focus on managing the level of exposure to the risk of foreign current exchange rate fluctuations on our major currencies, which include the British pound sterling, euro, Japanese yen, Canadian dollar, and Australian dollar. Additionally, prior to the closing of the Acquisition, Old WMG and Time Warner used foreign exchange contracts to manage this risk. See Note 22 to our audited financial statements included elsewhere herein for additional information.

The Company also is exposed to foreign currency exchange rate risk with respect to its £100 million principal amount of sterling-denominated notes that were issued in April 2004. These sterling notes mature on April 15, 2014. As of September 30, 2005, these sterling notes had a fair value of approximately $185 million, compared to a carrying value of $176 million. Based on the principal amount of sterling-denominated notes outstanding as of September 30, 2005 and assuming that all other market variables are held constant (including the level of interest rates), a 10% weakening or strengthening of the U.S. dollar compared to the British pound sterling would not have an impact on the fair value of these sterling notes, since these notes are completely hedged as of September 30, 2005.

Interest Rate Risk

We had $2.246 billion of total debt outstanding as of September 30, 2005, of which $1.430 billion was variable rate debt. As such, we are exposed to changes in interest rates. In order to manage this exposure, and consistent with the requirement under our senior secured credit facility to maintain a fixed-to-floating debt ratio of at least 50% of our actual funded debt though at least April 2007, we entered into interest rate swap agreements to hedge notional debt amounts of $300 million in 2004 and $597 million in 2005. Under these interest rate swap agreements, we agreed to receive floating-rate payments (based on three-month LIBOR rates) in exchange for fixed-rate payments.

Based on the amount of our floating-rate debt and our interest rate swap agreements outstanding as of September 30, 2005, each 25 basis point increase or decrease in interest rates would increase or decrease our annual interest expense and cash outlay by approximately $1.3 million. This potential increase or decrease is based on the simplified assumption that the level of floating-rate debt remains constant with an immediate across the board increase or decrease as of September 30, 2005 with no subsequent change in rates for the remainder of the period. This increase or decrease in rates would partially be mitigated by an increase or decrease in interest income earned on the Company's cash balances, almost all of which are invested in short-term variable interest rate earning assets.

In addition to our $1.430 billion of variable-rate debt, we had approximately $816 million of fixed-rate debt outstanding at September 30, 2005. Based on the level of interest rates prevailing at September 30, 2005, the fair value of this fixed-rate debt was approximately $834 million. Further, based on the amount of our fixed-rate debt and our related $897 million of interest rate swap agreements noted above that were outstanding at September 30, 2005, a 25 basis point increase or decrease in the level of interest rates would increase or decrease the fair value of the fixed-rate debt by approximately $16.6 million. This potential increase or decrease is based on the simplified assumption that the level of fixed-rate debt remains constant with an immediate across the board increase or decrease in the level of interest rates with no subsequent changes in rates for the remainder of the period.

We monitor our positions with, and the credit quality of, the financial institutions that are party to any of our financial transactions. Credit risk relating to the interest rate swaps is considered low because the swaps are entered into with strong, credit-worthy counterparties, and the credit risk is confined to the net settlement of the interest over the remaining life of the swaps.

CRITICAL ACCOUNTING POLICIES

The SEC's Financial Reporting Release No. 60, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies" ("FRR 60"), suggests companies provide additional disclosure and commentary on those accounting policies considered most critical. FRR 60 considers an accounting policy to be critical if it is important to our financial condition and results, and requires significant judgment and estimates on the part of management in our application. We believe the following list represents the critical accounting policies of us as contemplated by FRR 60. For a summary of all of our significant accounting policies, see Note 3 and Note 4 to our audited financial statements included elsewhere herein.

Purchase Accounting

We account for our business acquisitions under the purchase method of accounting. The total cost of acquisitions is allocated to the underlying identifiable net assets based on their respective estimated fair values. The excess of the purchase price over the estimated fair values of the net assets acquired is recorded as goodwill. Determining the fair value of assets acquired and liabilities assumed requires management's judgment and often involves the use of significant estimates and assumptions, including assumptions with respect to future cash inflows and outflows, discount rates, asset lives and market multiples, among other items. In addition, reserves have been established on our balance sheet related to acquired liabilities and qualifying restructuring costs based on assumptions made at the time of acquisition. We evaluate these reserves on a regular basis to determine the adequacy or accuracy of the amounts estimated.

Accounting for Goodwill and Other Intangible Assets

We account for our goodwill and other indefinite-lived intangible assets under Statement of Accountings Standards No. 142, Goodwill and Other Intangible Assets ("FAS 142"). Under FAS 142 the Company no longer amortizes goodwill, including the goodwill included in the carrying value of investments accounted for using the equity method of accounting, and certain other intangible assets deemed to have an indefinite useful life. FAS 142 requires that goodwill and certain intangible assets be assessed for impairment using fair value measurement techniques on an annual basis and when events occur that may suggest that the fair value of such assets cannot support the carrying value. Goodwill impairment is tested using a two-step process. The first step of the goodwill impairment test is used to identify potential impairment by comparing the fair value of a reporting unit with its net book value (or carrying amount), including goodwill. If the fair value of a reporting unit exceeds its carrying amount, goodwill of the reporting unit is considered not impaired and the second step of the impairment test is unnecessary. If the carrying amount of a reporting unit exceeds its fair value, the second step of the goodwill impairment test is performed to measure the amount of impairment loss, if any. The second step of the goodwill impairment test compares the implied fair value of the reporting unit's goodwill with the carrying amount of that goodwill. If the carrying amount of the reporting unit's goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized in an amount equal to that excess. The implied fair value of goodwill is determined in the same manner as the amount of goodwill recognized in a business combination. That is, the fair value of the reporting unit is allocated to all of the assets and liabilities of that unit (including any unrecognized intangible assets) as if the reporting unit had been acquired in a business combination and the fair value of the reporting unit was the purchase price paid to acquire the reporting unit. The impairment test for other intangible assets consists of a comparison of the fair value of the intangible asset with its carrying value. If the carrying value of the intangible asset exceeds its fair value, an impairment loss is recognized in an amount equal to that excess.

Determining the fair value of a reporting unit under the first step of the goodwill impairment test and determining the fair value of individual assets and liabilities of a reporting unit (including unrecognized intangible assets) under the second step of the goodwill impairment test is judgmental in nature and often involves the use of significant estimates and assumptions. Similarly, estimates and assumptions are used in determining the fair value of other intangible assets. These estimates and assumptions could have a significant impact on whether or not an impairment charge is recognized and also the magnitude of any such charge. To assist in the process of determining goodwill impairment, we obtain appraisals from independent valuation firms when necessary. In addition to the use of independent valuation firms, we perform internal valuation analyses and considers other market information that is publicly available. Estimates of fair value are primarily determined using discounted cash flows, market comparisons and analysis of recent transactions. These approaches use significant estimates and assumptions including projected future cash flows (including timing), discount rate reflecting the risk inherent in future cash flows, perpetual growth rate, determination of appropriate market comparables and the determination of whether a premium or discount should be applied to comparables.

We test our goodwill and other indefinite lived intangible assets for impairment on an annual basis in September of each fiscal year. We tested our goodwill and other indefinite lived intangible assets for impairment in the fourth quarter of 2005 and noted that no impairment occurred.

During the fourth quarter of 2003, in connection with Time Warner's agreement to sell us, we recorded a $1.019 billion impairment charge to reduce the carrying value of our intangible assets to fair value based on the consideration to be exchanged in the transaction. The impairment charge is classified as a component of operating loss in our combined statement of operations. The charge consisted of a reduction in the carrying value of goodwill by $5 million, brands and trademarks by $766 million, recorded music catalog by $208 million and other intangible assets by $40 million. Because the 2003 impairment charge was based principally on the difference between the negotiated purchase price of Warner Music Group and the historical book value of the net assets acquired, the amount of the charge was readily determinable.

As of September 30, 2005, Warner Music Group has recorded goodwill in the amount of $869 million, primarily related to the Acquisition. See Note 5 and Note 10 to our audited financial statements included herein for a further discussion of Warner Music Group's goodwill.

Equity Method and Cost Method Investments

For non-publicly traded investments, management's assessment of fair value is based on valuation methodologies including discounted cash flows, estimates of sales proceeds and external appraisals, as appropriate. The ability to accurately predict future cash flows, especially in developing and unstable markets, may impact the determination of fair value.

In the event a decline in fair value of an investment occurs, management may be required to determine if the decline in market value is other than temporary. Management's assessments as to the nature of a decline in fair value are based on the valuation methodologies discussed above and our ability and intent to hold the investment. We consider our equity method investees to be strategic long-term investments; therefore, we generally complete our assessments with a long-term viewpoint. If the fair value of any of our equity method or cost method investments is less than the carrying value and the decline in value is considered to be other than temporary, an impairment charge is recorded to write down the carrying value of the investment to its fair value. Management's assessments of fair value in accordance with these valuation methodologies represent our best estimates as of the time of the impairment review and are consistent with our internal planning. If different fair values were estimated, this could have a material impact on the financial statements.

Revenue and Cost Recognition

Sales Returns and Uncollectible Accounts

In accordance with practice in the recorded music industry and as customary in many territories, certain products (such as compact discs and cassettes) are sold to customers with the right to return unsold items. Under Statement of Accounting Standards No. 48, Revenue When Right of Return Exists, revenues from such sales are recognized when the products are shipped based on gross sales less a provision for future estimated returns.

In determining the estimate of product sales that will be returned, management analyzes historical returns, current economic trends, changes in customer demand and commercial acceptance of our products. Based on this information, management reserves a percentage of each dollar of product sales to provide for the estimated customer returns.

Similarly, management evaluates accounts receivables to determine if they will ultimately be collected. In performing this evaluation, significant judgments and estimates are involved, including an analysis of specific risks on a customer-by-customer basis for larger accounts and customers, and a receivables aging analysis that determines the percent that has historically been uncollected by aged category. Based on this information, management provides a reserve for the estimated amounts believed to be uncollectible.

Based on management's analysis of sales returns and uncollectible accounts, reserves totaling $218 million and $222 million have been established at September 30, 2005 and September 30, 2004, respectively. This compares to total gross receivables of $855 million and $793 billion at September 30, 2005 and September 30, 2004, respectively.

The comparability of the gross dollar value of such reserves has been affected by the inherent seasonality in the music business. That is, the recorded music business historically has generated approximately 35% of its sales in the last three months of the calendar year due to increased consumer demand associated with the holiday season. As such, both gross receivables and related allowances would be at a naturally lower level at September 30, the end of our fiscal year, and at a naturally higher level at December 31, the end of our first fiscal quarter. The ratios of our receivable allowances to gross accounts receivables were approximately 25% and 28% at the end of September 30, 2005 and September 30, 2004, respectively.

Gross Versus Net Revenue Classification

In the normal course of business, we act as an intermediary or agent with respect to certain payments received from third parties. For example, we distribute music product on behalf of third-party record labels.

The accounting issue encountered in these arrangements is whether we should report revenue based on the "gross" amount billed to the ultimate customer or on the "net" amount received from the customer after participation and other royalties paid to third parties. To the extent revenues are recorded gross (in the full amount billed), any participations and royalties paid to third parties are recorded as expenses so that the net amount (gross revenues, less expenses) flows through operating income. Accordingly, the impact on operating income is the same, whether we record the revenue on a gross basis or net basis (less related participations and royalties).

Determining whether revenue should be reported gross or net is based on an assessment of whether we are acting as the "principal" in a transaction or acting as an "agent" in the transaction. To the extent we are acting as a principal in a transaction, we report as revenue the payments received on a gross basis. To the extent we are acting as an agent in a transaction, we report as revenue the payments received less participations and royalties paid to third parties, i.e., on a net basis. The determination of whether we are serving as principal or agent in a transaction is judgmental in nature and based on an evaluation of the terms of an arrangement.

In determining whether we serve as principal or agent in these arrangements, we follow the guidance in EITF 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent" ("EITF 99-19"). Pursuant to such guidance, we serve as the principal in transactions where we have the substantial risks and rewards of ownership. The indicators that we have substantial risks and rewards of ownership are as follows:

- we are the supplier of the products or services to the customer;
- we have general inventory risk for a product before it is sold;
- we have latitude in establishing prices;
- we have the contractual relationship with the ultimate customer;
- we modify and service the product purchased to meet the ultimate customer specifications;
- we have discretion in supplier selection; and
- we have credit risk.

Conversely, pursuant to EITF 99-19, we serve as agent in arrangements where we do not have substantial risks and rewards of ownership. The indicators that we do not have substantial risks and rewards of ownership are as follows:

- the supplier (not Warner Music Group) is responsible for providing the product or service to the customer;
- the supplier (not Warner Music Group) has latitude in establishing prices;
- the amount we earn is fixed; and
- the supplier (not Warner Music Group) has credit risk.

Based on the above criteria and for the more significant transactions that we have evaluated, we record the distribution of product on behalf of third-party record labels on a gross basis, subject to the terms of the contract. However, recorded music compilations distributed by other record companies where we have a right to participate in the profits are recorded on a net basis.

Accounting for Royalty Advances

We regularly commit to and pay advance royalties to our artists and songwriters in respect of future sales. We account for these advance royalty payments under the related guidance in Statement of Financial Accounting Standard No. 50, "Financial Reporting in the Record and Music Industry" ("FAS 50"). Under FAS 50, we capitalize as assets certain advance royalty payments that management believes are recoverable from future royalties to be earned by the artist or songwriter.

Management's decision to capitalize an advance to an artist or songwriter as an asset requires significant judgment as to the recoverability of these advances. The recoverability of these assets is assessed upon initial commitment of the advance, based upon management's forecast of anticipated revenues from the sale of future and existing music and publishing-related products. In determining whether these amounts are recoverable, management evaluates the current and past popularity of the artist or songwriter, the initial or expected commercial acceptability of the product, the current and past popularity of the genre of music that the product is designed to appeal to, and other relevant factors. Based upon this information, management expenses the portion of such advances that it believes is not recoverable. In many cases, royalty advance payments to artists or publishers without history of successful commercial acceptability of the product and evidence of current or past popularity will be expensed immediately. All advances are assessed for recoverability continuously and at minimum on a quarterly basis.

We had $380 million and $446 million of advances on our balance sheet as of September 30, 2005 and 2004, respectively. We believe such advances are recoverable through future royalties to be earned by the related artists and songwriters.

Stock-Based Compensation

We account for stock-based compensation issued to employees in accordance with Statement of Financial Accounting Standard No. 148, "Accounting for Stock-Based Compensation Transition and Disclosure" ("FAS 148"), which amends Statement of Financial Accounting Standard FASB Statement No. 123, "Share Based Payment", "FAS 123"). This statement provides alternative methods of transition for a voluntary change to the fair value-based method of accounting for stock-based employee compensation. We adopted the expense recognition provision of FAS 123 as of March 1, 2004, the date of the Acquisition, and record stock-based compensation expense for grants on and after that date as provided by FAS 148, and will continue to provide pro forma information for all previous periods in the notes to financial statements to provide results as if FAS 123 had been adopted in those years. Under this provision, we estimate the fair value of our stock-based awards on the grant date and expense the fair value over the service period.

As disclosed in the notes to financial statements, we previously estimated the fair value of options issued at the date of grant using a Black-Scholes option-pricing model, which includes assumptions related to volatility, expected life, dividend yield and risk-free interest rate. In January of 2005 we determined that a binomial method was a more accurate and appropriate method for determining fair value. We have estimated the fair value of our grants made subsequent to January 2005 using the binomial method, which includes assumptions related to volatility, expected life, dividend yield and risk factors. We also award or sell restricted shares to our employees. For restricted shares awarded or sold below market value, the accounting charge is measured at the grant date and amortized ratably as non-cash compensation over the vesting term.

Accounting for Income Taxes

As part of the process of preparing its consolidated financial statements, we are required to estimate income taxes payable in each of the jurisdictions in which it operates. This process involves estimating the actual current tax expense together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within our consolidated balance sheets. Statement of Financial Accounting Standard No. 109, "Accounting for Income Taxes", ("FAS 109"), requires a valuation allowance be established when it is more likely than not that all or a portion of deferred tax assets will not be realized. In circumstances where there is sufficient negative evidence, establishment of a valuation allowance must be considered. We believe that cumulative losses in the most recent three-year period represent sufficient negative evidence to consider a valuation allowance under the provisions of FAS 109. As a result, we determined that certain of our deferred tax assets required the establishment of a valuation allowance.

The realization of the remaining deferred tax assets is primarily dependent on forecasted future taxable income. Any reduction in estimated forecasted future taxable income may require that we record additional valuation allowances against our deferred tax assets on which a valuation allowance has not previously been established. The valuation allowance that has been established will be maintained until there is sufficient positive evidence to conclude that it is more likely than not that such assets will be realized. An ongoing pattern of profitability will generally be considered as sufficient positive evidence. Our income tax expense recorded in the future may be reduced to the extent of offsetting decreases in our valuation allowance if such valuation allowances were not established through goodwill at the time of the Acquisition. The establishment and reversal of valuation allowances could have a significant negative or positive impact on our future earnings.

Tax assessments may arise several years after tax returns have been filed. Predicting the outcome of such tax assessments involves uncertainty; however, we believe that recorded tax liabilities adequately account for our analysis of probable outcomes.

New Accounting Principles

In addition to the critical accounting policies discussed above, we adopted several new accounting policies during the past two years. None of these new accounting principles had a material affect on our audited financial statements. See Notes 3 to our audited financial statements included elsewhere herein for a more complete summary.

RISK FACTORS

You should carefully consider the following risks and other information in this report before making an investment decision with respect to shares of our common stock. Any of the following risks could materially and adversely affect our business, financial condition or results of operations.

Risks Related to our Business

Increased costs associated with corporate governance compliance may significantly affect our results of operations.

Prior to our acquisition by the Investor Group in 2004, we were a business division of Time Warner. Accordingly, we have limited experience operating as an independent company implementing our own corporate governance practices. We expect the continued evaluation and implementation of corporate governance and securities disclosure and compliance practices in order to comply with these requirements will increase our legal compliance and financial reporting costs. In addition, they could make it more difficult for us to attract and retain qualified members of our board of directors, or qualified executive officers. Finally, director and officer liability insurance for public companies like us has become more difficult and more expensive to obtain, and we may be required to accept reduced coverage or incur higher costs to obtain coverage that is satisfactory to us and our officers or directors. We continue to evaluate and monitor regulatory developments and cannot estimate the timing or magnitude or additional costs we may incur as a result.

Our internal controls over financial reporting may not be adequate and our independent auditors may not be able to certify as to their adequacy, which could have a significant and adverse effect on our business and reputation.

We are evaluating our internal controls over financial reporting in order to allow management to report on, and our independent auditors to attest to, our internal controls over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act of 2002 and rules and regulations of the SEC there under, which we refer to as Section 404. Section 404 requires a reporting company such as ours to, among other things, annually review and disclose its internal controls over financial reporting, and evaluate and disclose changes in its internal controls over financial reporting quarterly. We will be required to comply with Section 404 as of September 30, 2006. We are currently performing the system and process evaluation and testing required (and any necessary

remediation) in an effort to comply with management certification and auditor attestation requirements of Section 404. In the course of our ongoing evaluation, we have identified areas of our internal controls requiring improvement, and plan to design enhanced processes and controls to address these and any other issues that might be identified through this review. As a result, we expect to incur additional expenses and diversion of management's time. We cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or the impact of the same on our operations and may not be able to ensure that the process is effective or that the internal controls are or will be effective in a timely manner. If we are not able to implement the requirements of Section 404 in a timely manner or with adequate compliance, our independent auditors may not be able to certify as to the effectiveness of our internal control over financial reporting and we may be subject to sanctions or investigation by regulatory authorities, such as the Securities and Exchange Commission. As a result, there could be an adverse reaction in the financial markets due to a loss of confidence in the reliability of our financial statements. In addition, we may be required to incur costs in improving our internal control system and the hiring of additional personnel. Any such action could adversely affect our results.

Our outside auditors have identified weaknesses in our internal controls that could affect our ability to ensure reliable financial reports.

In addition to our evaluation of internal controls under Section 404 of the Sarbanes-Oxley Act and any areas requiring improvement that we identify as part of that process, in connection with our most recent audit, our outside auditors identified a material weakness related to our royalty controls. A material weakness, as defined by the Public Company Accounting Oversight Board, is a significant deficiency that by itself, or in combination with other significant deficiencies, results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

Our outside auditors noted that our domestic operations currently use different royalty systems, which has created certain complexities in reconciling royalty payables. While we recognize that additional staff is needed to cope with current requirements in royalty processing until a new system can be developed, we may not be able to hire and train additional staff. While we have begun to take actions to address the issues surrounding our royalty systems, including hiring outside resources to assist our internal personnel with royalties accounting and entering into a joint venture with Universal Music Group, Exigen Group and Lightspeed Venture Partners to build a new uniform royalty system for all U.S. operations, additional measures will be necessary and these measures along with other measures we expect to take to improve our internal controls may not be sufficient to address the issues identified by our outside auditors or ensure that our internal controls are effective. If we are unable to provide reliable financial reports our business and prospects could suffer material adverse effects and our share price could be adversely affected.

The recorded music industry has been declining and may continue to decline, which may adversely affect our prospects and our results of operations.

Illegal downloading of music from the Internet, CD-R piracy, industrial piracy, economic recession, bankruptcies of record wholesalers and retailers and growing competition for consumer discretionary spending and retail shelf space may all be contributing to a declining recorded music industry. Additionally, the period of growth in recorded music sales driven by the introduction and penetration of the CD format has ended. No significant new legitimate audio format has yet emerged to take the place of the CD. The value of worldwide sales (recorded music, excluding sales of digital tracks), as reported by IFPI at fixed 2004 exchange rates, fell as the music industry witnessed a decline of 1.6% from 1999 to 2000, 1.3% from 2000 to 2001, 6.7% from 2001 to 2002, 7.6% from 2002 to 2003 and 1.3% from 2003 to 2004. We cannot assure you as to the timing or the extent of any improvement in the industry or that the evidence of improvement in 2004 based upon U.S. sales through the one-year period ending January 2, 2005 and global sales in the first half of 2004 will continue. For example, as of November 20, 2005, year-to-date U.S. recorded music sales (excluding sales of digital tracks) are down approximately 7.6% year-over-year. A declining recorded music industry is likely to lead to reduced levels of revenue and operating income generated by our Recorded Music business. Additionally, a declining recorded music industry is also likely to have a negative impact on our Music Publishing business, which generates a

significant portion of its revenues from mechanical royalties, primarily from the sale of music in CD and other recorded music formats.

There may be downward pressure on our pricing and our profit margins.

There are a variety of factors which could cause us to reduce our prices and erode our profit margins. They are, among others, increased price competition among record companies resulting from the Universal and Sony BMG recorded music duopoly, price competition from the sale of motion pictures in DVD-Video format and videogames, the ever greater price negotiating leverage of mass merchandisers and big box retailers, the increased costs of doing business with mass merchandisers and big box retailers as a result of complying with operating procedures that are unique to their needs and the adoption by record companies of initially lower-margin formats such as DualDisc and DVD-Audio. See "Risk Factors—We may be materially and adversely affected by the formation of Sony BMG Music Entertainment."

Our prospects and financial results may be adversely affected if we fail to identify, sign and retain artists and songwriters and by the existence or absence of superstar releases and by local economic conditions in the countries in which we operate.

We are dependent on identifying, signing and retaining artists with long-term potential, whose debut albums are well received on release, whose subsequent albums are anticipated by consumers and whose music will continue to generate sales as part of our catalog for years to come. The competition among record companies for such talent is intense. Competition among record companies to sell records is also intense and the marketing expenditures necessary to compete have increased as well. We are also dependent on signing and retaining songwriters who will write the hit songs of today and the classics of tomorrow under terms that are economically attractive to us. Our competitive position is dependent on our continuing ability to attract and develop talent whose work can achieve a high degree of public acceptance. Our financial results may be adversely affected if we are unable to identify, sign and retain such artists and songwriters under terms that are economically attractive to us. Our financial results may also be affected by the existence or absence of superstar artist releases during a particular period. Some music industry observers believe that the number of superstar acts with long-term appeal, both in terms of catalog sales and future releases, has declined in recent years. Additionally, our financial results are generally affected by the general economic and retail environment of the countries in which we operate, as well as the appeal of our recorded music catalog and our music publishing library.

We may have difficulty addressing the threats to our business associated with home copying and Internet downloading.

The combined effect of the decreasing cost of electronic and computer equipment and related technology such as CD burners and the conversion of music into digital formats have made it easier for consumers to create unauthorized copies of our recordings in the form of, for example, CDs and MP3 files. A substantial portion of our revenue comes from the sale of audio products that are potentially subject to unauthorized consumer copying and widespread dissemination on the Internet without an economic return to us. We are working to control this problem through litigation, by lobbying governments for new, stronger copyright protection laws and more stringent enforcement of current laws and by establishing legitimate new media business models. We cannot give any assurances that such measures will be effective. If we fail to obtain appropriate relief through the judicial process or the complete enforcement of judicial decisions issued in our favor (or if judicial decisions are not in our favor), if we are unsuccessful in our efforts to lobby governments to enact and enforce stronger legal penalties for copyright infringement or if we fail to develop effective means of protecting our intellectual property (whether copyrights or other rights such as patents, trademarks and trade secrets) or entertainment-related products or services, our results of operations, financial position and prospects may suffer.

Organized industrial piracy may lead to decreased sales.

The global organized commercial pirate trade is a significant threat to the music industry. Worldwide, industrial pirated music (which encompasses unauthorized physical copies manufactured for sale but does not

include Internet downloads or home CD burning) is estimated to have generated over $4.6 billion in revenues in 2004, according to IFPI. IFPI estimates that 1.5 billion pirated units were manufactured in 2004. According to IFPI estimates, approximately 34% of all music CDs sold worldwide in 2004 were pirated. Unauthorized copies and piracy contributed to the decrease in the volume of legitimate sales and put pressure on the price of legitimate sales. They have had, and may continue to have, an adverse effect on our business.

We may not be able to continue to realize the benefits from our restructuring plan and our restructuring plan may adversely affect our business.

In 2005 we substantially completed a restructuring of our business. The scope of our restructuring plan was broad and significant and may cause losses to our business that we cannot predict. Since the time of the Acquisition we have implemented annualized cost savings of approximately $250 million. We cannot assure you that we will continue to realize the benefits of the cost savings achieved.

The primary challenge we face in continuing to realize the cost savings in our restructuring plan is avoiding increased costs required to support our ongoing operations. Specifically, a variety of factors could cause us not to continue to achieve the benefits of the restructuring, or could result in harm to our business, including, among others, the following:

- higher than expected retention costs for employees that have been retained;
- increased operating costs or other unexpected costs associated with supporting the business and meeting financial objectives such as revenue growth;
- loss of revenues and market share due to, among other things, a diminished ability to attract and hire desirable talent;
- unexpected loss of artists or key employees; and
- loss of revenues and market share due to, among other things, a lack of sufficient resources to promote records and albums, and a lack of sufficient resources to attract new artists.

If we fail to continue to realize the benefits of the cost savings achieved through the restructuring plan, our results of operations and financial position may suffer. In addition, we cannot predict the extent to which our restructuring plan may adversely affect our business.

Our involvement in intellectual property litigation could adversely affect our business.

Our business is highly dependent upon intellectual property, a field that has encountered increasing litigation in recent years. If we are alleged to infringe the intellectual property rights of a third party, any litigation to defend the claim could be costly and would divert the time and resources of management, regardless of the merits of the claim. There can be no assurance that we would prevail in any such litigation. If we were to lose a litigation relating to intellectual property, we could be forced to pay monetary damages and to cease the sale of certain products or the use of certain technology. Any of the foregoing may adversely affect our business.

The recorded music industry is under investigation by Eliot Spitzer, the Attorney General for the State of New York, regarding its practices in promoting its records to radio stations.

On September 7, 2004, November 22, 2004 and March 31, 2005, Eliot Spitzer, the Attorney General of the State of New York, served us with requests for information in the form of subpoenas duces tecum in connection with an industry-wide investigation of the relationship between music companies and radio stations, including the use of independent promoters and accounting for any such payments. The investigation was pursuant to New York Executive Law §63(12) and New York General Business Law §349, both of which are consumer fraud

statutes. On November 22, 2005 we reached a settlement with the Attorney General in connection with this investigation. As part of such settlement, we agreed to make $5 million in charitable payments and to abide by a list of permissible and impermissible promotional activities. On July 25, 2005, Sony BMG reached a settlement with the Attorney General in connection with the same industry-wide investigation. Subsequent to the settlement by Sony BMG, TSR Records, an independent label, filed an antitrust suit against Sony BMG alleging that the label's radio promotion activities are anticompetitive. While it is too soon to predict the outcome of these recent developments on us, any litigation we may become involved in as a result of our settlement with the Attorney General, regardless of the merits of the claim, could be costly and would divert the time and resources of management.

Due to the nature of our business, our results of operations and cash flows may fluctuate significantly from period to period.

Our net sales, operating income and profitability, like those of other companies in the music business, are largely affected by the number and quality of albums that we release, our release schedule, and, more importantly, the consumer demand for these releases. We also make advance payments to recording artists and songwriters, which impact our operating cash flows. The timing of album releases and advance payments is largely based on business and other considerations and is made without regard to the timing of the release of our financial results. We report results of operations quarterly and our results of operations and cash flows in any reporting period may be materially affected by the timing of releases and advance payments, which may result in significant fluctuations from period to period.

Our operating results fluctuate on a seasonal and quarterly basis, and, in the event we do not generate sufficient net sales in our first fiscal quarter, we may not be able to meet our debt service and other obligations.

Our business is seasonal. For the fiscal year ended September 30, 2005, we derived approximately 83% of our revenues from our Recorded Music business. In the recorded music business, purchases are heavily weighted towards the last three months of the calendar year, which represent our first quarter under our September 30 fiscal year. Historically, we have realized approximately 35% of recorded music net sales worldwide during the last three months of the calendar year, making those three months (i.e., our new first fiscal quarter) material to our full-year performance. We realized 32% of recorded music calendar year net sales during the last three months of 2004. This sales seasonality affects our operating cash flow from quarter to quarter. We cannot assure you that our recorded music net sales for the last three months of any calendar year will continue to be sufficient to meet our obligations or that they will be higher than such net sales for our other quarters. In the event that we do not derive sufficient recorded music net sales in such last three months, we may not be able to meet our debt service requirements, working capital requirements, capital expenditure requirements, payment of regular dividends on our common stock and other obligations.

We may be unable to compete successfully in the highly competitive markets in which we operate and we may suffer reduced profits as a result.

The industry in which we operate is highly competitive, is based on consumer preferences and is rapidly changing. Additionally, the music industry requires substantial human and capital resources. We compete with other recorded music companies and music publishers to identify and sign new recording artists and songwriters who subsequently achieve long-term success and to renew agreements with established artists and songwriters. In addition, our competitors may from time to time reduce their prices in an effort to expand market share and introduce new services, or improve the quality of their products or services. We may lose business if we are unable to sign successful artists or songwriters or to match the prices or the quality of products and services, offered by our competitors. Our Music Publishing business competes not only with other music publishing companies, but also with songwriters who publish their own works. Our Recorded Music business is to a large

extent dependent on technological developments, including access to and selection and viability of new technologies, and is subject to potential pressure from competitors as a result of their technological developments. For example, our Recorded Music business may be adversely affected by technological developments that facilitate the piracy of music, such as Internet peer-to-peer file-sharing and CD-R activity; by its inability to enforce our intellectual property rights in digital environments; and by its failure to develop a successful business model applicable to a digital online environment, including such channels of distribution as satellite radio. It also faces competition from other forms of entertainment and leisure activities, such as cable and satellite television, pre-recorded films on videocassettes and DVD, the Internet and computer and videogames.

Our business operations in some countries subject us to trends, developments or other events in foreign countries which may affect us adversely.

We are a global company with strong local presences, which have become increasingly important as the popularity of music originating from a country's own language and culture has increased in recent years. Our mix of national and international recording artists and songwriters provides a significant degree of diversification for our music portfolio. However, our creative content does not necessarily enjoy universal appeal. As a result, our results can be affected not only by general industry trends, but also by trends, developments or other events in individual countries, including:

- limited legal protection and enforcement of intellectual property rights;
- restrictions on the repatriation of capital;
- differences and unexpected changes in regulatory environment, including environmental, health and safety, local planning, zoning and labor laws, rules and regulations;
- varying tax regimes which could adversely affect our results of operations or cash flows, including regulations relating to transfer pricing and withholding taxes on remittances and other payments by subsidiaries and joint ventures;
- exposure to different legal standards and enforcement mechanisms and the associated cost of compliance;
- difficulties in attracting and retaining qualified management and employees or rationalizing our workforce;
- tariffs, duties, export controls and other trade barriers;
- longer accounts receivable settlement cycles and difficulties in collecting accounts receivable;
- recessionary trends, inflation and instability of the financial markets;
- higher interest rates; and
- political instability.

We may not be able to insure or hedge against these risks, and we may not be able to ensure compliance with all of the applicable regulations without incurring additional costs. Furthermore, financing may not be available in countries with less than investment-grade sovereign credit ratings. As a result, it may be difficult to create or maintain profit-making operations in developing countries.

In addition, our results can be affected by trends, developments and other events in individual countries. There can be no assurance that in the future other country-specific trends, developments or other events will not have such a significant adverse effect on our business, results of operations or financial condition.

Our business may be adversely affected by competitive market conditions and we may not be able to execute our business strategy.

We intend to increase revenues and cash flow through a business strategy which requires us to, among other things, continue to maximize the value of our music assets, significantly reduce costs to maximize flexibility and adjust to new realities of the market, continue to act to contain digital piracy and capitalize on digital distribution and emerging technologies.

Each of these initiatives requires sustained management focus, organization and coordination over significant periods of time. Each of these initiatives also requires success in building relationships with third parties and in anticipating and keeping up with technological developments and consumer preferences. The results of the strategy and the success of our implementation of this strategy will not be known for some time in the future. If we are unable to implement the strategy successfully or properly react to changes in market conditions, our financial condition, results of operations and cash flows could be adversely affected.

Our ability to operate effectively could be impaired if we fail to attract and retain our executive officers.

Our success depends, in part, upon the continuing contributions of our executive officers. Although we have employment agreements with our executive officers, there is no guarantee that they will not leave. The loss of the services of any of our executive officers or the failure to attract other executive officers could have a material adverse effect on our business or our business prospects.

Legitimate channels for digital distribution of our creative content are a recent development, and their impact on our business is unclear and may be adverse.

We have positioned ourselves to take advantage of the Internet and wireless as a sales distribution channel and believe that the development of legitimate channels for digital music distribution holds promise for us in the future. However, legitimate channels for digital distribution are a recent development and we cannot predict their impact on our business. In digital formats, certain costs associated with physical products such as manufacturing, distribution, inventory and return costs do not apply. While there are some digital-specific variable costs and infrastructure investments necessary to produce, market and sell music in digital formats, we believe it is reasonable to expect that we will generally derive a higher contribution margin from digital versus physical sales. However, we cannot assure you that we will generally continue to achieve higher margins from digital sales. Any legitimate digital distribution channel that does develop may result in lower or less profitable sales for us than comparable physical sales. In addition, the transition to greater sales through digital channels introduces uncertainty regarding the potential impact of the "unbundling" of the album on our business. While recent studies have indicated that consumers spend more on music in general when they begin to purchase music in digital form than previously, it remains unclear how consumer behavior will change when faced with the prospect of purchasing only their favorite tracks from a given album rather than the entire album. In addition, if piracy continues unabated and legitimate digital distribution channels fail to gain consumer acceptance, our results of operations could be harmed.

A significant portion of our music publishing revenues is subject to rate regulation either by government entities or by local third-party collection societies throughout the world and rates on other income streams may be set by arbitration proceedings, which may limit our profitability.

Mechanical royalties and performance royalties are the two largest sources of income to our Music Publishing business and mechanical royalties are a significant expense to our Recorded Music business. In the U.S., mechanical rates are set pursuant to industry negotiations contemplated by the U.S. Copyright Act and performance rates are set by performing rights societies and subject to challenge by performing rights licensees. Outside the U.S., mechanical and performance rates are typically negotiated on an industry-wide basis. The mechanical and performance rates set pursuant to such processes may adversely affect us by limiting our ability to increase the profitability of our Music Publishing business. If the mechanical rates are set too high it may also

adversely affect us by limiting our ability to increase the profitability of our Recorded Music business. In addition, rates our Recorded Music business receives in the U.S. for, among other sources of income and potential income, the statutory license for eligible non-subscription services to perform sound recordings publicly by means of digital audio transmissions ("webcasting"), the statutory license to make ephemeral recordings of sound recordings for use of sound recordings and the statutory license for use of our content on satellite radio are set by an arbitration process under the U.S. Copyright Act unless rates are determined through voluntary negotiations. If the rates for these and other income sources are set too low through this process, it could have a material adverse impact on our Recorded Music business or our business prospects.

Unfavorable currency exchange rate fluctuations could adversely affect our results of operations.

The reporting currency for our financial statements is the U.S. dollar. We have substantial assets, liabilities, revenues and costs denominated in currencies other than U.S. dollars. To prepare our consolidated financial statements, we must translate those assets, liabilities, revenues and expenses into U.S. dollars at then-applicable exchange rates. Consequently, increases and decreases in the value of the U.S. dollar versus other currencies will affect the amount of these items in our consolidated financial statements, even if their value has not changed in their original currency. These translations could result in significant changes to our results of operations from period to period. For the fiscal year ended September 30, 2005, approximately 52% of our revenues related to operations in foreign territories. From time to time, we enter into foreign exchange contracts to hedge the risk of unfavorable foreign currency exchange rate movements. As of September 30, 2005, we have hedged our material foreign currency exposures related to royalty payments remitted between our foreign affiliates and our U.S. affiliates for the balance of the fiscal year.

We may not have full control and ability to direct the operations we conduct through joint ventures.

We currently have interests in a number of joint ventures and may in the future enter into further joint ventures as a means of conducting our business. In addition, we structure certain of our relationships with recording artists and songwriters as joint ventures. We may not be able to fully control the operations and the assets of our joint ventures, and we may not be able to make major decisions or may not be able to take timely actions with respect to our joint ventures unless our joint venture partners agree.

The enactment of legislation limiting the terms by which an individual can be bound under a "personal services" contract could impair our ability to retain the services of key artists.

California Labor Code Section 2855 ("Section 2855") limits the duration of time any individual can be bound under a contract for "personal services" to a maximum of seven years. In 1987, Subsection (b) was added, which provides a limited exception to Section 2855 for recording contracts, creating a damages remedy for record companies. Legislation was introduced in California to repeal Subsection (b) and then withdrawn. Legislation was introduced in New York to create a statute similar to Section 2855, which did not advance. There is no assurance that New York, California or any other state will not reintroduce or introduce similar legislation in the future. In fact, legislation similar to Section 2855 has recently been introduced in the New York Assembly. The repeal of Subsection (b) of Section 2855 and/or the passage of legislation similar to Section 2855 by other states could materially affect our results of operations and financial position.

We face a potential loss of catalog if it is determined that recording artists have a right to recapture rights in their recordings under the U.S. Copyright Act.

The U.S. Copyright Act provides authors (or their heirs) a right to terminate licenses or assignments of rights in their copyrighted works. This right does not apply to works that are "works made for hire". Since the effective date of U.S. copyrightability for sound recordings (February 15, 1972), virtually all of our agreements with recording artists provide that such recording artists render services under an employment-for-hire relationship. A termination right exists under the U.S. Copyright Act for musical compositions that are not "works made for hire". If any of our commercially available recordings were determined not to be "works made

for hire", then the recording artists (or their heirs) could have the right to terminate the rights they granted to us, generally during a five-year period starting at the end of 35 years from the date of a post-1977 license or assignment (or, in the case of a pre-1978 grant in a pre-1978 recording, generally during a five-year period starting either at the end of 56 years from the date of copyright or on January 1, 1978, whichever is later). A termination of rights could have an adverse effect on our Recorded Music business. From time to time, authors (or their heirs) can terminate our rights in musical compositions. However, we believe the effect of those terminations is already reflected in the financial results of our Music Publishing business.

If we acquire or invest in other businesses, we will face certain risks inherent in such transactions.

We may acquire, make investments in, or enter into strategic alliances or joint ventures with, companies engaged in businesses that are similar or complementary to ours. If we make such acquisitions or investments or enter into strategic alliances, we will face certain risks inherent in such transactions. For example, gaining regulatory approval for significant acquisitions or investments could be a lengthy process and there can be no assurance of a successful outcome. We could face difficulties in managing and integrating newly acquired operations. Additionally, such transactions would divert management resources and may result in the loss of artists or songwriters from our rosters. We cannot assure you that if we make any future acquisitions, investments, strategic alliances or joint ventures that they will be completed in a timely manner, that they will be structured or financed in a way that will enhance our credit-worthiness and allow for continued payment of regular dividends or that they will meet our strategic objectives or otherwise be successful. Failure to effectively manage any of these transactions could result in material increases in costs or reductions in expected revenues, or both.

We are controlled by entities that may have conflicts of interest with us.

The Investor Group controls a majority of our capital stock on a fully diluted basis. In addition, representatives of the Investor Group occupy substantially all of the seats on our board of directors and pursuant to a stockholders agreement, will have the right to appoint all of the independent directors to our board. As a result, the Investor Group has the ability to control our policies and operations, including the appointment of management, the entering into of mergers, acquisitions, sales of assets, divestitures and other extraordinary transactions, future issuances of our common stock or other securities, the payments of dividends, if any, on our common stock, the incurrence of debt by us and the amendment of our certificate of incorporation and bylaws. The Investor Group will have the ability to prevent any transaction that requires the approval of our board of directors or the stockholders regardless of whether or not other members of our board of directors or stockholders believe that any such transaction is in their own best interests. For example, the Investor Group could cause us to make acquisitions that increase our indebtedness or to sell revenue-generating assets. Additionally, the Investor Group are in the business of making investments in companies and may from time to time acquire and hold interests in businesses that compete directly or indirectly with us. The Investor Group may also pursue acquisition opportunities that may be complementary to our business, and, as a result, those acquisition opportunities may not be available to us. So long as the Investor Group continues to hold a majority of our outstanding common stock the Investor Group will be entitled to nominate a majority of our board of directors, and will have the ability to effectively control the vote in any election of directors. In addition, so long as the Investor Group continues to own a significant amount of our equity, even if such amount is less than 50%, they will continue to be able to strongly influence or effectively control our decisions.

Our reliance on one company for the manufacturing, packaging and physical distribution of our products in North America and Europe could have an adverse impact on our ability to meet our manufacturing, packaging and physical distribution requirements.

Cinram is currently our exclusive supplier of manufacturing, packaging and physical distribution services in North America and most of Europe. Accordingly, our continued ability to meet our manufacturing, packaging and physical distribution requirements in those territories depends largely on Cinram's continued successful operation in accordance with the service level requirements mandated by us in our service agreements. If, for any

reason, Cinram were to fail to meet contractually required service levels, we would have difficulty satisfying our commitments to our wholesale and retail customers, which could have an adverse impact on our revenues. Even though our agreements with Cinram give us a right to terminate based upon failure to meet mandated service levels, and there are several capable substitute suppliers, it might be difficult for us to switch to substitute suppliers for any such services, particularly in the short-term, and the delay and transition time associated with finding substitute suppliers could itself have an adverse impact on our revenues. In addition, our agreements with Cinram begin to expire in 2006. If we are unable to negotiate renewals of these agreements we would have to switch to substitute suppliers. Further, pricing negotiated with Cinram in future agreements may be more or less favorable than the existing agreements.

We may be materially and adversely affected by the formation of Sony BMG Music Entertainment.

In August 2004 Sony Music Entertainment ("Sony") and Bertelsmann Music Group ("BMG") merged their recorded music businesses to form Sony BMG Music Entertainment ("Sony BMG"). As a result, the recorded music market now consists of four major players (Universal, Sony BMG, EMI Recorded Music ("EMI") and us) rather than five (Universal, Sony, BMG, EMI and us). Prior to the formation of Sony BMG, there was one disproportionately large major, Universal, with approximately 25% market share and four other majors relatively equal in size with market shares ranging between 11% and 14%. Now there are two majors with 2004 global market shares over 25%, Universal and Sony BMG, and two significantly smaller majors, EMI and us, each with less than 15%. There is a threat that the change in the competitive landscape caused by the new Universal and Sony BMG duopoly could drive up the costs of artist signings and the costs of marketing and promoting records to our detriment.

Risks Related to our Leverage

Our substantial leverage on a consolidated basis could adversely affect our ability to raise additional capital to fund our operations, limit our ability to react to changes in the economy or our industry and prevent us from meeting our obligations under our indebtedness.

We are highly leveraged. As of September 30, 2005, our total consolidated indebtedness was $2.246 billion. We have an additional $250 million available for borrowing under the revolving portion of our senior secured credit facility (less $4 million of current letters of credit).

Our high degree of leverage could have important consequences for you, including:

- making it more difficult for us and our subsidiaries to make payments on indebtedness;
- increasing our vulnerability to general economic and industry conditions;
- requiring a substantial portion of cash flow from operations to be dedicated to the payment of principal and interest on indebtedness, therefore reducing our ability to use our cash flow to fund our operations, capital expenditures and future business opportunities;
- exposing us to the risk of increased interest rates as certain of the borrowings of our subsidiaries, including borrowings under our senior secured credit facility, will be at variable rates of interest;
- limiting our ability and the ability of our subsidiaries to obtain additional financing for working capital, capital expenditures, product development, debt service requirements, acquisitions and general corporate or other purposes; and
- limiting our ability to adjust to changing market conditions and placing us at a competitive disadvantage compared to our competitors who are less highly leveraged.

We and our subsidiaries may be able to incur substantial additional indebtedness in the future, subject to the restrictions contained in our senior secured credit facility and the indentures relating to our outstanding notes. If new indebtedness is added to our current debt levels, the related risks that we and our subsidiaries now face could intensify.

We may not be able to generate sufficient cash to service all of our indebtedness, and may be forced to take other actions to satisfy our obligations under our indebtedness, which may not be successful.

Our ability to make scheduled payments on or to refinance our debt obligations depends on our financial condition and operating performance, which is subject to prevailing economic and competitive conditions and to certain financial, business and other factors beyond our control. We cannot assure you that we will maintain a level of cash flows from operating activities sufficient to permit us to pay the principal, premium, if any, and interest on our indebtedness, including the notes.

If our cash flows and capital resources are insufficient to fund our debt service obligations, we may be forced to reduce or delay investments in recording artists, and songwriters capital expenditures, or to sell assets, seek additional capital or restructure or refinance our indebtedness. These alternative measures may not be successful and may not permit us to meet our scheduled debt service obligations. In the absence of such operating results and resources, we could face substantial liquidity problems and might be required to dispose of material assets or operations to meet our debt service and other obligations. Our senior secured credit facility and the indenture governing our outstanding notes restrict our ability to dispose of assets and use the proceeds from dispositions. We may not be able to consummate those dispositions or to obtain the proceeds which we could realize from them and these proceeds may not be adequate to meet any debt service obligations then due.

Holdings also will be relying on Acquisition Corp. and its subsidiaries to make payments on the Holdings Notes. If Acquisition Corp. does not dividend funds to Holdings in an amount sufficient to make such payments, Holdings may default under the indenture governing the Holdings notes, which would result in all such notes becoming due and payable. Because Acquisition Corp.'s debt agreements have covenants that limit its ability to make payments to Holdings, Holdings may not have access to funds in an amount sufficient to service its indebtedness.

Our debt agreements contain restrictions that limit our flexibility in operating our business.

Our senior secured credit agreement and the indentures governing our outstanding notes contain various covenants that limit our ability to engage in specified types of transactions. These covenants limit the ability of our restricted subsidiaries to, among other things:

- incur additional indebtedness or issue certain preferred shares;
- pay dividends on or make distributions in respect of our capital stock or make other restricted payments;
- make certain investments;
- sell certain assets;
- create liens on certain indebtedness without securing the notes;
- consolidate, merge, sell or otherwise dispose of all or substantially all of our assets;
- enter into certain transactions with our affiliates; and
- designate our subsidiaries as unrestricted subsidiaries.

In addition, under our senior secured credit agreement, our subsidiaries are required to satisfy and maintain specified financial ratios and other financial condition tests. Their ability to meet those financial ratios and tests can be affected by events beyond our control, and they may not be able to meet those ratios and tests. A breach of any of these covenants could result in a default under our senior secured credit agreement. Upon the occurrence of an event of default under our senior secured credit agreement, the lenders could elect to declare all amounts outstanding under our senior secured credit agreement to be immediately due and payable and terminate all commitments to extend further credit. If we were unable to repay those amounts, the lenders under our senior secured credit agreement could proceed against the collateral granted to them to secure that indebtedness. We have pledged a significant portion of our assets as collateral under our senior secured credit agreement. If the lenders under our senior secured credit agreement accelerate the repayment of borrowings, we may not have sufficient assets to repay our senior secured credit agreement, as well as any unsecured indebtedness.

Risks Related to our Common Stock

We are a "controlled company" within the meaning of the New York Stock Exchange rules and, as a result, will qualify for, and intend to rely on, exemptions from certain corporate governance requirements.

The Investor Group controls a majority of our outstanding common stock. As a result, we are a "controlled company" within the meaning of the New York Stock Exchange corporate governance standards. Under the New York Stock Exchange rules, a company of which more than 50% of the voting power is held by an individual, a group, or another company is a "controlled company" and may elect not to comply with certain New York Stock Exchange corporate governance requirements, as applicable, including (1) the requirement that a majority of the board of directors consist of independent directors, (2) the requirement that we have a nominating/corporate governance committee that is composed entirely of independent directors with a written charter addressing the committee's purpose and responsibilities and (3) the requirement that we have a compensation committee that is composed entirely of independent directors with a written charter addressing the committee's purpose and responsibilities. We are and intend to continue to utilize these exemptions while we are a controlled company. As a result, we will not have a majority of independent directors nor will our nominating and corporate governance committee, which also serves as our executive committee, and compensation committee consist entirely of independent directors. Accordingly, you will not have the same protections afforded to stockholders of companies that are subject to all of the New York Stock Exchange corporate governance requirements.

Future sales of our shares could depress the market price of our common stock.

The market price of our common stock could decline as a result of sales of a large number of shares of common stock in the market or the perception that such sales could occur. These sales, or the possibility that these sales may occur, also might make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate. As of September 30, 2005 we had approximately 148.5 million shares of common stock outstanding. Of those shares, the 32.6 million shares sold in our Initial Common Stock Offering in May 2005 are freely tradable. Of the remaining shares, approximately 8.3 million shares represent restricted stock. Of these shares, approximately 1.1 million shares were vested as of September 30, 2005. The approximately 107.5 million remaining shares plus the vested restricted stock will be eligible for resale from time to time, subject to contractual and Securities Act restrictions. The Investor Group, which collectively beneficially own approximately 107.5 million shares, have the ability to cause us to register the resale of their shares and certain other holders of our common stock, including members of our management, will be able to participate in such registration. In addition, notwithstanding the foregoing, we have registered all 8.3 million shares of restricted common stock and approximately 8.4 million shares underlying options issued and that may be issued in the future pursuant to our benefit plans and arrangements on registration statements on Form S-8 and such shares may be sold as provided therein.

The market price of our common stock may be volatile, which could cause the value of your investment to decline.

Securities markets worldwide experience significant price and volume fluctuations. This market volatility, as well as general economic, market or potential conditions, could reduce the market price of our common stock in spite of our operating performance. In addition, our operating results could be below the expectations of securities analysts and investors, and in response, the market price of our common stock could decrease significantly. As a result, the market price of our common stock could decline below price at which you purchase it. You may be unable to resell your shares of our common stock at or above such price. Among other factors that could affect our stock price are:

- actual or anticipated variations in operating results;
- changes in financial estimates by research analysts;
- actual or anticipated changes in economic, political or market conditions, such as recessions or international currency fluctuations;

- actual or anticipated changes in the regulatory environment affecting the music industry;
- changes in the retailing environment;
- changes in the market valuations of other music industry peers; and
- announcements by us or our competitors of significant acquisitions, strategic partnerships, divestitures, joint ventures or other strategic initiatives.

See "Risk Factors—Due to the nature of our business, our results of operations and cash flows may fluctuate significantly from period to period." In the past, following periods of volatility in the market price of a company's securities, stockholders have often instituted class action securities litigation against those companies. Such litigation, if instituted, could result in substantial costs and a diversion of management attention and resources, which could significantly harm our profitability and reputation.

Provisions in our Charter and amended and restated bylaws and Delaware law may discourage a takeover attempt.

Provisions contained in our Charter and amended and restated bylaws ("Bylaws") and Delaware law could make it more difficult for a third party to acquire us, even if doing so might be beneficial to our stockholders. Provisions of our Charter and Bylaws impose various procedural and other requirements, which could make it more difficult for shareholders to effect certain corporate actions. For example, our Charter authorizes our board of directors to determine the rights, preferences, privileges and restrictions of unissued series of preferred stock, without any vote or action by our shareholders. Thus, our board of directors can authorize and issue shares of preferred stock with voting or conversion rights that could adversely affect the voting or other rights of holders of our common stock. These rights may have the effect of delaying or deterring a change of control of our company. These provisions could limit the price that certain investors might be willing to pay in the future for shares of our common stock.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As discussed in Note 22 to our audited consolidated financial statements for the twelve months ended September 30, 2005, the Company is exposed to market risk arising from changes in market rates and prices, including movements in foreign currency exchange rates and interest rates. As of September 30, 2005, other than as described below, there have been no material changes to the Company's exposure to market risk since September 30, 2004.

We are exposed to foreign currency exchange rate risk with respect to our £100 million principal amount of sterling-denominated notes that were issued in April 2004. These sterling notes mature on April 15, 2014. As of September 30, 2005, these sterling notes had a fair value of approximately $185 million, compared to a carrying value of $176 million. Based on the principal amount of sterling-denominated notes outstanding as of September 30, 2005 and assuming that all other market variables are held constant (including the level of interest rates), a 10% weakening or strengthening of the U.S. dollar compared to the British pound sterling would not have an impact on the fair value of these sterling notes, since these notes are completely hedged as of September 30, 2005.

We are exposed to interest rate risk with respect to our floating rate debt. Based on the amount of our floating-rate debt and our interest rate swap agreements outstanding as of September 30, 2005, each 25 basis point increase or decrease in interest rates would increase or decrease our annual interest expense and cash outlay by approximately $1.3 million. This potential increase or decrease is based on the simplified assumption that the level of floating-rate debt remains constant with an immediate across the board increase or decrease as of September 30, 2005 with no subsequent change in rates for the remainder of the period. This increase or decrease in rates would partially be mitigated by an increase or decrease in interest income earned on our cash balances, almost all of which are invested in short-term variable interest rate earning assets.

We monitor our positions with, and the credit quality of, the financial institutions that are party to any of our financial transactions. Credit risk relating to the interest rate swaps is considered low because the swaps are entered into with strong, credit-worthy counterparties, and the credit risk is confined to the net settlement of the interest over the remaining life of the swaps.

The Company did not enter into any significant foreign exchange forward contracts in October and November 2005.

During the twelve months ended September 30, 2005, the Company entered into additional interest rate swap agreements with a notional face amount of $597 million. Under these interest rate swap agreements, we agreed to receive floating-rate payments (based on three-month LIBOR rates) in exchange for fixed-rate payments. Based on the addition of the new interest-rate swap agreements, each 25 basis point increase or decrease in interest rates would increase or decrease our annual interest expense and cash outlay by approximately $1.3 million. This potential increase or decrease is based on the simplified assumption that the level of floating-rate debt remains constant with an immediate across the board increase or decrease as of September 30, 2005 with no subsequent changes in rates for the remainder of the period.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

WARNER MUSIC GROUP CORP.

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Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of Warner Music Group Corp.

We have audited the accompanying consolidated balance sheets of Warner Music Group Corp. (the "Company") as of September 30, 2005 and 2004, and the related consolidated statements of operations, shareholders' equity, and cash flows for the twelve months ended September 30, 2005 and for the seven months ended September 30, 2004. Our audits also included the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Broad (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company at September 30, 2005 and 2004, and the consolidated results of its operations and its cash flows for the twelve months ended September 30, 2005 and the seven months ended September 30, 2004, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The condensed consolidated financial statements are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

New York, New York
November 15, 2005
/s/ Ernst & Young LLP

Report of Independent Registered Public Accounting Firm

The Shareholders of Warner Music Group Corp.

We have audited the combined statements of operations, group equity, and cash flows of Warner Music Group Corp. ("Old WMG") for the three months ended February 29, 2004 (Predecessor Basis) and for the twelve months ended November 30, 2003 (Predecessor Basis). Our audits also included the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of Old WMG's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company's internal control over financial reporting. Our audits included consideration of the internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the combined results of its operations and its cash flows for the three months ended February 29, 2004 (Predecessor Basis), and for the twelve months ended November 30, 2003 (Predecessor Basis), in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The condensed consolidating financial statements are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in our audits of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as whole.

March 10, 2005
New York, New York
/s/ Ernst & Young LLP

Warner Music Group Corp.

Consolidated Balance Sheets

	September 30, 2005	September 30, 2004
	(in millions)	
Assets		
Current assets:		
Cash and equivalents	$ 288	$ 555
Accounts receivable, less allowances of $218 and $222 million	637	571
Inventories	52	65
Royalty advances expected to be recouped within one year	190	223
Deferred tax assets	36	38
Other current assets	39	86
Total current assets	1,242	1,538
Royalty advances expected to be recouped after one year	190	223
Investments	21	8
Property, plant and equipment, net	157	189
Goodwill	869	978
Intangible assets subject to amortization, net	1,815	1,937
Intangible assets not subject to amortization	100	100
Other assets	104	117
Total assets	$ 4,498	$ 5,090
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	$ 247	$ 226
Accrued royalties	1,057	1,003
Taxes and other withholdings	23	10
Current portion of long-term debt	17	12
Note payable to shareholders	—	342
Other current liabilities	404	587
Total current liabilities	1,748	2,180
Long-term debt	2,229	1,828
Dividends payable	5	—
Deferred tax liabilities, net	201	265
Other noncurrent liabilities	226	333
Minority interest in preferred stock of subsidiary	—	204
Total liabilities	4,409	4,810
Commitments and Contingencies (See Note 21)		
Shareholders' equity:		
Common stock ($0.001 par value; 500,000,000 shares authorized; 148,455,313 and 107,544,923 shares issued and outstanding)	—	—
Additional paid-in capital	548	512
Accumulated deficit	(480)	(238)
Accumulated other comprehensive income, net	21	6
Total shareholders' equity	89	280
Total liabilities and shareholders' equity	$ 4,498	$ 5,090

See accompanying notes.

Warner Music Group Corp.

Consolidated and Combined Statements of Operations

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
	(audited)	(audited)	(audited)	(unaudited)	(audited)
	(in millions, except per share data)				
Revenues[a]	$ 3,502	$ 1,769	$ 779	$ 2,487	$ 3,376
Costs and expenses:					
Cost of revenues[a][b]	(1,850)	(944)	(415)	(1,449)	(1,940)
Selling, general and administrative expenses[a][b]	(1,301)	(677)	(319)	(995)	(1,286)
Impairment of goodwill and other intangible assets	—	—	—	—	(1,019)
Amortization of intangible assets	(187)	(104)	(56)	(201)	(242)
Loss on termination of management agreement	(73)	—	—	—	—
Loss on sale of physical distribution assets	—	—	—	(12)	(12)
Restructuring costs, net	(7)	(26)	—	(27)	(35)
Total costs and expenses	(3,418)	(1,751)	(790)	(2,684)	(4,534)
Operating income (loss)	84	18	(11)	(197)	(1,158)
Interest expense, net[a]	(182)	(80)	(2)	(5)	(5)
Net investment-related gains (losses)	1	—	—	(17)	(26)
Equity in the losses of equity-method investees, net	(1)	(2)	(2)	(32)	(41)
Deal-related transaction and other costs	—	—	—	(7)	(70)
Loss on repayment of Holdings Notes	(35)	—	—	—	—
Loss on repayment of bridge loan	—	(6)	—	—	—
Unrealized gain (loss) on warrants	17	(120)	—	—	—
Other income (expense), net[a]	7	(4)	—	(10)	(17)
Minority interest expense	(5)	(14)	—	—	—
Loss before income taxes	(114)	(208)	(15)	(268)	(1,317)
Income tax (expense) benefit	(55)	(30)	(17)	67	(36)
Net loss	$ (169)	$ (238)	$ (32)	$ (201)	$ (1,353)
Net loss per common share:					
Basic and Diluted	$ (1.40)	$ (2.21)			
Average common shares:					
Basic and Diluted	120.9	107.5			
(a) Includes depreciation expense of:	$ (51)	$ (36)	$ (16)	$ (71)	$ (86)
(b) Includes the following income (expenses) resulting from transactions with related companies (Note 20)					
Revenues	$ 9	$ —	$ 4	$ 35	$ 56
Cost of revenues	3	—	(2)	(195)	(239)
Selling, general and administrative expenses	7	(10)	(12)	(114)	(144)
Interest income (expense), net	—	—	1	8	10
Other expense, net	—	—	—	(10)	(17)
Minority interest expense	(5)	(14)	—	—	—

See accompanying notes.

Warner Music Group Corp.

Consolidated and Combined Statements of Cash Flows

	Successor		Predecessor		
	Year Ended September 30, 2005 (audit	Seven Months Ended September 30, 2004 (audited)	Three Months Ended February 29, 2004 (audit	Ten Months Ended September 30, 2003 (unaudited)	Year Ended November 30, 2003 (audited)
			(in millions)		
Cash flows from operating activities					
Net loss	$ (169)	$ (238)	$ (32)	$ (201)	$ (1,353)
Adjustments to reconcile net loss to net cash provided by operating activities:					
Impairment of goodwill and other intangible assets	—	—	—	—	1,019
Depreciation and amortization	235	142	72	272	328
Deferred taxes	—	8	(4)	(117)	(19)
Loss on sale of physical distribution assets	—	—	—	17	17
Loss on debt repayment	35	6	—	—	—
Non-cash interest expense	69	15	2	10	11
Net investment-related losses (gains)	(1)	—	—	17	26
Equity in the losses of equity-method investees, including distributions	1	3	2	35	44
Non-cash, stock-based compensation expense	25	—	—	—	—
Unrealized (gain) loss on warrants	(17)	120	—	—	—
Minority interest expense	5	14	—	—	—
Changes in operating assets and liabilities:					
Accounts receivable	(58)	(33)	387	275	(121)
Inventories	(3)	(10)	6	24	17
Royalty advances	—	77	(4)	38	111
Accounts payable and accrued liabilities	10	(23)	(109)	(116)	169
Other balance sheet changes	70	3	1	8	39
Net cash provided by operating activities	205	86	321	257	278
Cash flows from investing activities					
Acquisition of Old WMG[a]	—	(2,638)	—	—	—
Other investments and acquisitions	(28)	(10)	(1)	(43)	(52)
Investment proceeds	54	—	19	—	38
Capital expenditures	(30)	(15)	(3)	(30)	(51)
Net cash (used in) provided by investing activities	(54)	(2,663)	14	(73)	(65)
Cash flows from financing activities					
Borrowings	946	2,348	—	114	114
Financing costs of borrowings	(20)	(95)	—	—	—
Debt repayments	(588)	(631)	(124)	(101)	(101)
Capital contributions	—	—	262	132	132
Proceeds from the issuance of common stock	554	850	—	—	—
Costs to issue common stock	(32)	—	—	—	—
Proceeds from issuance of subsidiary preferred stock	—	400	—	—	—
Repurchase of subsidiary preferred stock	(200)	(202)	—	—	—
Dividends paid on subsidiary preferred stock	(9)	—	—	—	—
Proceeds from the issuance of restricted shares	1	3	—	—	—
Cash paid to repurchase warrant	(138)	—	—	—	—
Returns of capital and dividends paid	(917)	—	—	—	—
Loans to third parties	(10)	—	—	—	—
Decrease (increase) in amounts due from Time Warner-affiliated companies	—	—	194	(293)	(195)
Dividends paid to minority interest on subsidiary preferred stock or to Time Warner for predecessor periods	—	(8)	(342)	—	(68)
Principal payments on capital lease	—	—	—	(3)	(3)
Other	(3)	—	—	—	—
Net cash provided by (used in) financing activities	(416)	2,661	(10)	(151)	(121)
Effect of foreign currency exchange rate changes on cash	(1)	—	2	6	11
Net (decrease) increase in cash and equivalents	(267)	84	327	35	103
Cash and equivalents at beginning of period	555	471	144	41	41
Cash and equivalents at end of period	$ 288	$ 555	$ 471	$ 80	$ 144

(a) Net cash used in operating activities for the twelve months ended September 30, 2005 and for the seven months ended September 30, 2004 includes approximately $80 million and $105 million of acquisition-related restructuring payments, respectively.

(b) Excludes $35 million of non-cash consideration issued as part of the purchase price paid to Time Warner in the form of warrants.

See accompanying notes.

Warner Music Group Corp.

Consolidated and Combined Statements of Shareholders' and Group Equity

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	Common Stock							
	Common Shares	Par	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Group Equity	Due from Time Warner-Affiliated Companies, net	Total Shareholders' and Group Equity
	(in millions, except number of common shares)							
Predecessor:								
Balance at November 30, 2002	—	—	$ —	$ —	$ —	$ 3,566	$ (565)	$ 3,001
Comprehensive loss:								
Net loss[a]	—	—	—	—	—	(1,353)	—	(1,353)
Foreign currency translation adjustment	—	—	—	—	—	68	—	68
Deferred gains on foreign exchange contracts	—	—	—	—	—	4	—	4
Total comprehensive loss	—	—	—	—	—	(1,281)	—	(1,281)
Reduction in tax benefits on stock options exercised	—	—	—	—	—	(2)	—	(2)
Increase in amounts due from Time Warner-affiliated companies, net	—	—	—	—	—	—	(195)	(195)
Capital contributions	—	—	—	—	—	132	—	132
Dividends	—	—	—	—	—	(68)	—	(68)
Balance at November 30, 2003	—	—	—	—	—	2,347	(760)	1,587
Comprehensive loss:								
Net loss	—	—	—	—	—	(32)	—	(32)
Foreign currency translation adjustment	—	—	—	—	—	21	—	21
Total comprehensive loss	—	—	—	—	—	(11)	—	(11)
Decrease in amounts due from Time Warner-affiliated companies, net	—	—	—	—	—	—	325	325
Capital contributions	—	—	—	—	—	262	—	262
Dividends	—	—	—	—	—	(969)	497	(472)
Balance at February 29, 2004	—	$ —	$ —	$ —	$ —	$ 1,629	$ 62	$ 1,691

(a) Net loss for 2003 includes an approximate $1.019 billion impairment charge to reduce the carrying value of goodwill, trademarks and other intangible assets in the fourth quarter of 2003. In addition, net loss for 2002 includes a $4.8 billion impairment charge to reduce the carrying value of goodwill upon the initial adoption of FAS 142 and a $1.5 billion impairment charge to reduce the carrying value of goodwill and other intangible assets in the fourth quarter of 2002 (see Note 10).

See accompanying notes.

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Warner Music Group Corp.

Consolidated and Combined Statements of Shareholders' and Group Equity

	Common Stock							
	Common Shares	Par	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Group Equity	Due from Time Warner-Affiliated Companies, net	Total Shareholders' and Group Equity
	(in millions, except number of common shares)							
Successor								
Balance at February 29, 2004— Predecessor	—	$ —	$ —	$ —	$ —	$ 1,629	$ 62	$ 1,691
Adjustments to record the Acquisition:								
Transfer of excluded net liabilities to Time Warner	—	—	—	—	—	12	(12)	—
Elimination of historical equity balances	—	—	—	—	—	(1,641)	(50)	(1,691)
Capital contribution to fund a portion of the purchase price of Old WMG	107,544,922	—	850	—	—	—	—	850
Balance at March 1, 2004, adjusted to give effect to the Acquisition	107,544,922	—	850	—	—	—	—	850
Comprehensive loss:								
Net loss	—	—	—	(238)	—	—	—	(238)
Foreign currency translation adjustment	—	—	—	—	10	—	—	10
Deferred losses on derivative financial instruments	—	—	—	—	(4)	—	—	(4)
Total comprehensive loss	—	—	—	(238)	6	—	—	(232)
Return of capital	—	—	(342)	—	—	—	—	(342)
Issuance of stock options and restricted shares of common stock	6,570,254	—	3	—	—	—	—	3
Other	—	—	1	—	—	—	—	1
Balance at September 30, 2004	114,115,176	—	512	(238)	6	—	—	280
Comprehensive loss:								
Net loss	—	—	—	(169)	—	—	—	(169)
Foreign currency translation adjustment	—	—	—	—	3	—	—	3
Deferred gains on derivative financial instruments	—	—	—	—	12	—	—	12
Total comprehensive loss	—	—	—	—	15	—	—	15
Return of capital	—	—	(508)	(73)	—	—	—	(581)
Issuance of common stock, net of issuance costs	32,600,000	0.001	522	—	—	—	—	522
Issuance of stock options and restricted shares of common stock	1,740,137	0.001	25	—	—	—	—	25
Other	—	—	(3)	—	—	—	—	(3)
Balance at September 30, 2005	148,455,313	0.001	$ 548	$ (480)	$ 21	$ —	$ —	$ 89

See accompanying notes.

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements

1. Description of Business

Warner Music Group Corp. (the "Company" or "Parent") was formed by a private equity consortium of Investors (the "Investor Group") on November 21, 2003. The Company is the direct parent of WMG Holdings Corp. ("Holdings"), which is the direct parent of WMG Acquisition Corp. ("New WMG" or "Acquisition Corp."). New WMG is one of the world's major music companies and the successor to the interests of the recorded music and music publishing businesses of Time Warner Inc. ("Time Warner"). Such predecessor interests formerly owned by Time Warner are hereinafter referred to as "Old WMG" or the "Predecessor." Effective March 1, 2004, WMG Acquisition Corp. acquired Old WMG from Time Warner for approximately $2.6 billion (the "Acquisition").

On May 10, 2005, the Company sold 32,600,000 shares of its common stock in an initial public offering (the "Initial Common Stock Offering"). In connection with the Initial Common Stock Offering, the Company (i) converted all its formerly outstanding shares of Class L Common Stock into shares of Class A Common Stock, (ii) renamed all of its formerly outstanding shares of Class A Common Stock as "common stock", which had the effect of eliminating from the Company's authorized capital stock the Class L Common Stock and Class A Common Stock and (iii) authorized an approximately 1,139 to 1 split of the Company's common stock.

The Company classifies its business interests into two fundamental areas: recorded music and music publishing. A brief description of those operations is presented below.

Recorded Music Operations

The Company's recorded music operations consist of the discovery and development of artists and the related marketing and distribution of recorded music produced by such artists. In addition to the more traditional methods of discovering and developing artists, the Company has implemented new initiatives to identify and nurture artists earlier in the development process and reduce development costs by leveraging its independent distribution network. The Company refers to these new business models as incubator initiatives. Asylum and East West are current incubator labels. In addition, the Company has also entered into strategic ventures with other record labels.

The Company's recorded music operations also include a catalog division called Rhino Entertainment ("Rhino"), which was formerly called Warner Strategic Marketing. Rhino specializes in marketing our music catalog through compilations and reissuances of previously released music and video titles, as well as in the licensing of tracks to/from third parties for various uses, including film and television soundtracks.

The Company's principal recorded music distribution operations include Warner-Elektra-Atlantic Corporation ("WEA Corp."), which primarily distributes the Company's music products to retailers and wholesale distributors in the United States; a 90% interest in Alternative Distribution Alliance ("ADA"), a distribution company which primarily distributes the products of independent record labels to retailers and wholesale distributors; various distribution centers and ventures operated internationally; and an 80% interest in Word Entertainment, whose distribution operations specialize in the distribution of music products in the Christian retail marketplace.

The Company plays an integral role in virtually all aspects of the music value chain from discovering and developing talent, to producing albums and promoting artists and their product. After an artist has entered into a contract with one of the Company's record labels, a master recording of the artist's music is created. The recording is then replicated for sale to consumers primarily in the CD format, and now, in digital formats. In the U.S., WEA Corp. and ADA market, sell and deliver product, either directly or through sub-distributors and

wholesalers, to thousands of record stores, mass merchants and other retailers throughout the country. Recorded music products are also sold in physical form to Internet physical retailers.

In the United States, the Company's recorded music operations are conducted principally through its major record labels—Warner Bros. Records and The Atlantic Records Group. In markets outside the U.S., recorded music activities are conducted through our Warner Music International ("WMI") division and its various subsidiaries, affiliates and non-affiliated licensees.

Music Publishing Operations

The Company's music publishing business is focused on the exploitation songs as intellectual property. 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.

Warner/Chappell is the Company's 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. The music publishing library includes many standard titles that span multiple music genres. Warner/Chappell also administers the music and soundtracks of several third-party television and film producers and studios, including Lucasfilm, Ltd. and Hallmark Entertainment.

The Company also previously owned Warner Bros. Publications ("WBP"), which printed and distributed a broad selection of sheet music, books and educational materials, orchestrations, folios, personality books, and arrangements from the catalogs of Warner/Chappell and other music publishers. On May 31, 2005, we sold our printed sheet music business to Alfred Publishing. See Note 6.

Music Publishing revenues are derived from four main sources:

- *Mechanical:* the licensor receives royalties with respect to compositions embodied in recordings sold in any format or configuration, including singles, albums, CDs, digital downloads and mobile phone ringtones.
- *Performance:* the licensor receives royalties when the composition is performed publicly (*e.g.*, broadcast radio and television, movie theater, concert, nightclub or Internet and wireless streaming).
- *Synchronization:* the licensor receives royalties or fees for the right to use the composition in combination with visual images (*e.g.*, in films, television commercials and programs and videogames).
- *Other:* the licensor receives royalties from other uses such as stage productions and printed sheet music.

2. Basis of Presentation

New Basis of Presentation

The accompanying consolidated and combined financial statements present separately the financial position, results of operations, cash flows and changes in equity for both the Company and its predecessor, Old WMG. As described in further detail in Note 5, Old WMG was acquired by a subsidiary of the Company effective as of March 1, 2004. In connection with the Acquisition, a new accounting basis was established for the Company as of the acquisition date based upon an allocation of the purchase price to the underlying net assets acquired.

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements—(Continued)

Financial information for the pre- and post-acquisition periods have been separated by a vertical line on the face of the consolidated and combined financial statements to highlight the fact that the financial information for such periods have been prepared under two different historical-cost bases of accounting.

Old Basis of Presentation

As previously described, the operations of Old WMG were under the control of Time Warner through the end of February 2004. In January 2001, historic Time Warner was acquired by America Online Inc. ("AOL") in a transaction hereinafter referred to as the "AOL Time Warner Merger". The AOL Time Warner Merger was accounted for under the purchase method of accounting. Under the purchase method of accounting, the basis of the historical net assets included in the accompanying combined financial statements was adjusted, effective as of January 1, 2001, to reflect an allocable portion of the purchase price relating to the AOL Time Warner Merger. See Note 5 for additional information.

For all periods prior to the closing of the Acquisition, the accompanying combined financial statements reflect all assets, liabilities, revenues, expenses and cash flows directly attributable to Old WMG. In addition, the accompanying combined financial statements include allocations of certain costs of Time Warner and Old WMG deemed reasonable by the Company's management, in order to present the results of operations, financial position, changes in group equity and cash flows of Old WMG on a stand-alone basis. The principal allocation methodologies are described below. The financial information included herein does not necessarily reflect the results of operations, financial position, changes in group equity and cash flows of Old WMG in the future or what would have been reflected had Old WMG been a separate, stand-alone entity during the periods presented. The income tax benefits and provisions, related tax payments and deferred tax balances have been prepared as if Old WMG operated as a stand-alone taxpayer for the periods presented.

For all periods prior to the closing of the Acquisition, certain general and administrative costs incurred by Time Warner have been allocated to the combined financial statements of Old WMG, including pension and other benefit-related costs, insurance-related costs and other general and administrative costs. These cost allocations were determined based on a combination of factors, as appropriate, including Old WMG's pro rata share of the revenues under the management of Old WMG and other more directly attributable methods, such as claim experience for insurance costs and employee-related attributes for pension costs. The costs allocated to the Company are not necessarily indicative of the costs that would have been incurred if Old WMG had obtained such services independently, nor are they indicative of costs that will be charged or incurred in the future. However, management believes that such allocations are reasonable.

Fiscal Year

In 2004, in connection with the Acquisition, the Company changed its fiscal year-end to September 30 from November 30. As such, financial information for 2004 is presented for a shortened, ten-month transition period ended September 30, 2004. This financial information for 2004 also has been separated into two pre-acquisition and post-acquisition periods as a result of the change in accounting basis that occurred relating to the Acquisition. In order to enhance comparability, financial information for the ten-month period ended September 30, 2004 has been supplemented by the presentation of unaudited financial information for the ten-month period ended September 30, 2003. Based on how the Company's closing schedule occurred in 2003, the information for the ten-month period ended September 30, 2003 consists of 43 weeks, as compared to 44 weeks contained in the ten-month period ended September 30, 2004.

Basis of Consolidation and Combination

Prior to the closing of the Acquisition, the recorded music and music publishing operations of the Company were legally held by multiple subsidiaries and affiliates of Old WMG and Time Warner. As such, the

accompanying financial statements present the *combined* accounts of such businesses for all periods prior to the Acquisition. After the closing of the Acquisition, New WMG acquired the stock or net assets of those predecessor businesses. Accordingly, the accompanying financial statements present the *consolidated* accounts of such businesses for all periods after the closing of the Acquisition. The consolidated accounts include 100% of the assets, liabilities, revenues, expenses, income, losses and cash flows of the Company and all entities in which the Company has a controlling voting interest and/or variable interest entities required to be consolidated in accordance with accounting principles generally accepted in the United States ("U.S. GAAP"). All significant inter-company balances and transactions have been eliminated in consolidation and combination.

Recapitalization

As discussed above, on May 10, 2005, the Company sold 32,600,000 shares of its common stock in the Initial Common Stock Offering. In connection with the Initial Common Stock Offering, the Company (i) converted all its formerly outstanding shares of Class L Common Stock into shares of Class A Common Stock, (ii) renamed all of its formerly outstanding shares of Class A Common Stock as "common stock", which had the effect of eliminating from the Company's authorized capital stock the Class L Common Stock and Class A Common Stock and (iii) authorized an approximately 1,139 to 1 split of the Company's common stock, (collectively, the "Recapitalization"). Accordingly, historical financial statements have been restated to reflect the Recapitalization for all periods occurring after the Acquisition that was effective as of March 1, 2004. Such restatement primarily related to common stock and equivalent shares information, net income (loss) per common share computations and stock-based compensation disclosures.

3. Summary of Significant Accounting Policies

Use of Estimates

The preparation of consolidated and combined financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates due to, among other factors, the risks inherent in the recorded music and music publishing businesses, including continuing industry-wide piracy. Estimates are used when accounting for certain items such as allowances for doubtful accounts and sales returns, depreciation and amortization, asset impairments (including royalty advances and intangible assets), contingencies, reserves (including certain royalty payables), the value of stock-based compensation and the value of stock warrants issued to Time Warner. In addition, significant estimates were used in accounting for the Acquisition under the purchase method of accounting, and prior to the Acquisition, in allocating certain costs to Old WMG in order to present Old WMG's operating results on a stand-alone basis (see Note 2).

Cash and Equivalents

The Company considers all highly liquid investments with maturities of three months or less when purchased to be cash equivalents.

Foreign Currency Translation

The financial position and operating results of substantially all foreign operations are consolidated or combined using the local currency as the functional currency. Local currency assets and liabilities are translated at the rates of exchange on the balance sheet date, and local currency revenues and expenses are translated at average rates of exchange during the period. Resulting translation gains or losses are included in the accompanying consolidated and combined statement of shareholders' and group equity as a component of accumulated other comprehensive income (loss).

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements—(Continued)

Derivative and Financial Instruments

Effective January 1, 2001, the Company adopted Financial Accounting Standards Board ("FASB") Statement No. 133, as amended by FASB Statement No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities" ("FAS 133"). FAS 133 requires that all derivative instruments be recognized on the balance sheet at fair value. In addition, FAS 133 provides that, for derivative instruments that qualify for hedge accounting, changes in the fair value are either (a) offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or (b) recognized in equity until the hedged item is recognized in earnings, depending on whether the derivative is being used to hedge changes in fair value or cash flows. The ineffective portion of a derivative's change in fair value is immediately recognized in earnings.

As further described in Note 19, the Company issued, and subsequently repurchased, stock warrants to Time Warner as part of the purchase price of the Acquisition. The stock warrants were derivative financial instruments which the Company accounted for in accordance with the provisions of FAS 133. Accordingly, the warrants were reflected as a liability in the accompanying consolidated balance sheet of the Company at September 30, 2004, at fair value. In turn, changes in the fair value of the warrants were reflected in the accompanying consolidated statement of operations of the Company for the year ended September 30, 2005 and the seven months ended September 30, 2004.

The carrying value of the Company's financial instruments approximates fair value, except for certain differences relating to long-term, fixed-rate debt and other financial instruments that are not significant. The fair value of financial instruments is generally determined by reference to market values resulting from trading on a national securities exchange or an over-the-counter market. In cases where quoted market prices are not available, fair value is based on estimates using present value or other valuation techniques. See Note 14 for the fair value of the Company's debt.

Revenues

Recorded Music

In accordance with industry practice and as is customary in many territories, certain products (such as CDs and cassettes) are sold to customers with the right to return unsold items. Revenues from such sales are recognized when the products are shipped based on gross sales less a provision for future estimated returns. Revenues from the sale of recorded music products through digital distribution channels are recognized when the products are sold by the providers.

Music Publishing

Revenues are earned from the receipt of royalties relating to the licensing of rights in musical compositions, and for the sale of published sheet music and songbooks.

The receipt of royalties principally relates to amounts earned from the public performance of copyrighted material, the mechanical reproduction of copyrighted material on recorded media including digital formats, and the use of copyrighted material in synchronization with visual images. Consistent with industry practice, music- publishing royalties generally are recognized as revenue when received.

Gross Versus Net Revenue Classification

In the normal course of business, the Company acts as an intermediary or agent with respect to certain payments received from third parties. For example, the Company distributes music product on behalf of third-party record labels. Pursuant to Emerging Issues Task Force ("EITF") No. 99-19, "Reporting Revenue Gross as a Principal versus Net as an Agent," such transactions are recorded on a "gross" or "net" basis

depending on whether the Company is acting as the "principal" in the transaction or acting as an "agent" in the transaction. The Company serves as the principal in transactions in which it has substantial risks and rewards of ownership and, accordingly, revenues are recorded on a gross basis. For those transactions in which the Company does not have substantial risks and rewards of ownership, the Company is considered an agent in the transactions and, accordingly, revenues are recorded on a net basis.

To the extent revenues are recorded on a gross basis, any participations and royalties paid to third parties are recorded as expenses so that the net amount (gross revenues less expenses) flows through operating income. To the extent revenues are recorded on a net basis, revenues are reported based on the amounts received, less participations and royalties paid to third parties. Either way, the impact on operating income is the same whether the Company records the revenues on a gross or net basis.

Based on an evaluation of the individual terms of each contract and whether the Company is acting as principal or agent, the Company generally records revenues from the distribution of recorded music product on behalf of third-party record labels on a gross basis. However, revenues are recorded on a net basis for recorded music compilations distributed by other record companies where the Company has a right to participate in the profits.

Royalty Advances and Royalty Costs

The Company regularly commits to and pays advance royalties to its artists and songwriters in respect of future sales. The Company accounts for these advance royalty payments under the related guidance in FASB No. 50, "Financial Reporting in the Record and Music Industry" ("FAS 50"). Under FAS 50, certain advance royalty payments that are believed to be recoverable from future royalties to be earned by the artist or songwriter are capitalized as assets. The decision to capitalize an advance to an artist or songwriter as an asset requires significant judgment as to the recoverability of these advances. The recoverability of these assets is assessed upon initial commitment of the advance, based upon the Company's forecast of anticipated revenues from the sale of future and existing music and publishing-related products. In determining whether these amounts are recoverable, the Company evaluates the current and past popularity of the artist or songwriter, the initial or expected commercial acceptability of the product, the current and past popularity of the genre of music that the product is designed to appeal to, and other relevant factors. Based upon this information, the portion of such advances that are believed not to be recoverable is expensed. All advances are assessed for recoverability continuously and at minimum on a quarterly basis.

Royalties earned by artists, songwriters, co-publishers, other copyright holders and trade unions are recognized as an expense in the period in which the sale of the product takes place, less an adjustment for future estimated returns.

Inventories

Inventories consist of CDs, cassettes and related music products, as well as published sheet music and songbooks. Inventories are stated at the lower of cost or estimated realizable value. Cost is determined using first-in, first-out ("FIFO") and average cost methods, which approximate cost under the FIFO method. Returned goods included in inventory are valued at estimated realizable value, but not in excess of cost.

Advertising

In accordance with American Institute of Certified Public Accountants ("AICPA") Statement of Position ("SOP") No. 93-7, "Reporting on Advertising Costs," advertising costs, including costs to produce music videos

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

used for promotional purposes, are expensed as incurred. Advertising expense amounted to approximately $195 million for the year ended September 30, 2005, $94 million for the seven months ended September 30, 2004, $53 million for the three months ended February 29, 2004, and $202 million for the year ended November 30, 2003. Deferred advertising costs, which principally relate to advertisements that have not been exhibited or services that have not been received, were approximately $3 million and $4 million at September 30, 2005 and 2004, respectively.

Concentration of Credit Risk

In the recorded music business, the Company has 15 key customers that generate significant sales volume. At September 30, 2005 each of these customers composed from 1% to 7% of the Company's consolidated gross accounts receivable, and approximately 52% in the aggregate. Based on a history of cash collection, the Company does not believe there is any significant collection risk from such customers. In the music publishing business, the Company collects a significant portion of its royalties from copyright collection societies around the world. Collection societies and associations generally are not-for-profit organizations that represent composers, songwriters and music publishers. These organizations seek to protect the rights of their members by licensing, collecting license fees and distributing royalties for the use of their works. Accordingly, the Company does not believe there is any significant collection risk from such societies.

Shipping and Handling

The costs associated with shipping goods to customers are recorded as cost of revenues. Shipping and handling charges billed to customers are included in revenues.

Investments

In January 2003, FASB Interpretation No. 46, "Consolidation of Variable Interest Entities—an Interpretation of ARB No. 51" ("FIN 46") was issued. FIN 46 requires that the Company first evaluate its investments to determine if any investments in companies in which the Company has significant influence, but less than a controlling voting interest, qualify as a variable interest entity ("VIE"). In determining if an entity is a VIE, FIN 46 requires one to evaluate whether the equity of the entity is sufficient to absorb its expected losses. The evaluation requires the consideration of qualitative factors and various assumptions, including expected future cash flows and funding needs. Even if the entity's equity is determined to be sufficient to absorb expected losses, the rules provide that in certain circumstances there needs to be a qualitative assessment as to whether "substantially all" the benefits of the entity are for the benefit of one of the variable interest holders. In such circumstances, the entity would be deemed a VIE. FIN 46 further provides that the primary beneficiary of a VIE is required to consolidate the VIE's operations.

The Company adopted the provisions of FIN 46 effective as of November 30, 2003. In particular, the Company consolidated four recorded music ventures, which were previously accounted for under the equity method of accounting. The operations of these ventures principally consist of the discovery and development of artists and related music products, which are distributed by the Company. The application of FIN 46 did not have a material impact on the Company's financial statements.

For investments in companies in which the Company has significant influence, but less than a controlling voting interest, that do not qualify as VIE's under the provisions of FIN 46, the Company accounts for the investments using the equity method. This is generally presumed to exist when the Company owns between 20% and 50% of the investee. Should the Company had a greater than 50% ownership interest in an investee and the minority shareholders held certain rights that allowed them to participate in the day-to-day operations of the business, the Company would also use the equity method of accounting.

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

Under the equity method, only the Company's investment in and amounts due to and from the equity investee are included in the consolidated balance sheet; only the Company's share of the investee's earnings (losses) is included in the consolidated operating results; and only the dividends, cash distributions, loans or other cash received from the investee, additional cash investments, loan repayments or other cash paid to the investee are included in the consolidated cash flows.

Investments in companies in which the Company does not have a controlling interest or is unable to exert significant influence are accounted for at market value if the investments are publicly traded and there are no resale restrictions greater than one year ("available-for-sale investments"). If there are resale restrictions greater than one year, or if the investment is not publicly traded, then the investment is accounted for at cost.

Property, Plant and Equipment

Property, plant and equipment are recorded at historical cost. Depreciation is calculated using the straight-line method based upon the estimated useful lives of depreciable assets as follows: five to ten years for furniture and fixtures, periods of up to five years for computer equipment and periods of up to seven years for machinery and equipment. Buildings are depreciated over periods of up to fifty years. Leasehold improvements are depreciated over periods up to the life of the lease.

Accounting for Goodwill and Other Intangible Assets

In July 2001, FASB Statement No. 141, "Business Combinations" ("FAS 141") and FASB Statement No. 142, "Goodwill and Other Intangible Assets" ("FAS 142") were issued. These standards changed the accounting for business combinations by, among other things, prohibiting the prospective use of pooling-of-interests accounting. In addition, FAS 142 required that goodwill, including the goodwill included in the carrying value of investments accounted for using the equity method of accounting, and certain other intangible assets deemed to have an indefinite useful life, should not be amortized. These new rules also require that goodwill and certain intangible assets be assessed for impairment using fair value measurement techniques. The Company adopted the provisions of FAS 142 effective as of December 1, 2001. See Note 10 for further discussion on the adoption of FAS 142.

Internal-Use Software Development Costs

In accordance with AICPA SOP No. 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use", the Company capitalizes certain external and internal computer software costs incurred during the application development stage. The application development stage generally includes software design and configuration, coding, testing and installation activities. Training and maintenance costs are expensed as incurred, while upgrades and enhancements are capitalized if it is probable that such expenditures will result in additional functionality. Capitalized software costs are depreciated over the estimated useful life of the underlying project on a straight-line basis, generally not exceeding five years.

Valuation of Long-Lived Assets

The Company periodically reviews the carrying value of its long-lived assets, including property, plant and equipment, whenever events or changes in circumstances indicate that the carrying value may not be recoverable. To the extent the estimated future cash inflows attributable to the asset, less estimated future cash outflows, are less than the carrying amount, an impairment loss is recognized in an amount equal to the difference between the carrying value of such asset and its fair value. Assets to be disposed of and for which there is a committed plan to dispose of the assets, whether through sale or abandonment, are reported at the lower of carrying value or fair value less costs to sell.

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

Stock-Based Compensation

Post-Acquisition

Effective March 1, 2004, in connection with the Acquisition, the Company adopted the fair value recognition provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("FAS 123") to account for all stock-based compensation plans adopted subsequent to the Acquisition. Under the fair value recognition provisions of FAS 123, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the service period.

Pre-Acquisition

Prior to the Acquisition, certain employees of Old WMG participated in various Time Warner stock option plans. In accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and related interpretations, compensation cost for stock options or other equity-based awards granted to employees was recognized in income based on the excess, if any, of the quoted market price of the stock at the grant date of the award over the amount an employee must pay to acquire the stock. Generally, the exercise price for stock options granted to employees equaled or exceeded the fair market value of Time Warner common stock at the date of grant, thereby resulting in no recognition of compensation expense by Old WMG. For any awards that generated compensation expense as defined under APB 25, Old WMG calculated the amount of compensation expense and recognized the expense over the vesting period of the award.

Had compensation cost for Time Warner's stock option plans been determined based on the fair value method set forth in FAS 123, Old WMG's net loss for all periods presented prior to the closing of the Acquisition would have been as follows:

	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
	(audited)	(unaudited)	(audited)
Net loss:			
As reported	$ (32)	$ (201)	$ (1,353)
Pro forma	$ (42)	$ (243)	$ (1,403)

See Note 18 for further information on employee stock-based compensation.

Income Taxes

Income taxes are provided using the asset and liability method presented by FASB Statement No. 109, "Accounting for Income Taxes" ("FAS 109"). Under this method, income taxes (i.e., deferred tax assets, deferred tax liabilities, taxes currently payable/refunds receivable and tax expense) are recorded based on amounts refundable or payable in the current year and include the results of any differences between U.S. GAAP and tax reporting. Deferred income taxes reflect the tax effect of net operating loss, capital loss and general business credit carryforwards and the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial statements and income tax purposes, as determined under enacted tax laws and rates. Valuation allowances are established when management determines that it is more likely than not that some portion or all of the deferred tax asset will not be realized. The financial effect of changes in tax laws or rates is accounted for in the period of enactment.

Prior to the closing of the Acquisition, the taxable results of Old WMG were included in the consolidated U.S. federal, and various states, local and foreign income tax returns of Time Warner or its subsidiaries. Also, in

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

certain state, local and foreign jurisdictions, Old WMG filed on a stand-alone basis. The income tax provision reflected in the combined statement of operations of Old WMG is presented as if Old WMG operated on a stand-alone basis, consistent with the liability method prescribed by FAS 109. The majority of the temporary differences for pre-Acquisition periods related to non-deductible reserves and adjustments to the carrying value of assets and liabilities established in the accounting for the AOL Time Warner Merger, as well as net operating loss carry forwards in 2002 only.

Comprehensive Income (Loss)

Comprehensive income (loss), which is reported in the accompanying consolidated and combined statements of shareholders' and group 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 deferred gains and losses on financial instruments designated as hedges under FAS 133, which include interest-rate swap and foreign exchange contracts.

For all periods prior to the closing of the Acquisition, accumulated other comprehensive income (loss) has been presented as a component of group equity and has not been set forth separately due to the complex nature of preparing a *combined* set of financial statements for operations that were legally held by multiple subsidiaries of Old WMG and Time Warner. Such historical accumulated other comprehensive income (loss) balances were eliminated as part of the change in accounting basis that occurred effective on March 1, 2004, in connection with the closing of the Acquisition. The following summary set forth the components of other comprehensive income (loss), net of related taxes, that have been accumulated in shareholders' equity since March 1, 2004:

	Foreign Currency Translation Gain (Losses)	Derivative Financial Instruments Gain (Losses)	Accumulated Other Comprehensive Gain (Losses)
		(in millions)	
Balance at March 1, 2004	$ —	$ —	$ —
Activity through September 30, 2004	10	(4)	6
Balance at September 30, 2004	$ 10	$ (4)	$ 6
Activity through September 30, 2005	3	12	15
Balance at September 30, 2005	$ 13	$ 18	$ 21

Other Recently Issued Accounting Standards

Over the past two years, there have been new accounting standards issued, including FASB 123(R), "Share-based Payment (revised)" ("FAS 123R"), which was issued in December 2004. The Company plans to adopt the provisions of FAS 123(R) during the first quarter of fiscal 2006. The adoption of this accounting standard is not expected to have a material impact on the Company's financial statements.

4. Net Loss Per Common Share

The Company computes net loss per common share in accordance with FASB Statement No. 128, "Earnings per Share" ("FAS 128"). Under the provisions of FAS 128, basic net loss per common share is computed by dividing the net loss applicable to common shares after preferred dividend requirements, if any, by the weighted average of common shares outstanding during the period. Diluted net income (loss) per common share adjusts basic net income (loss) per common share for the effects of stock options, warrants and other potentially dilutive financial instruments, only in the periods in which such effect is dilutive.

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

The following table sets forth the computation of basic and diluted net loss per common share (in millions, except per share amounts):

	Year ended September 30, 2005	Seven Months Ended September 30, 2004
Basic and diluted pro forma net loss per common share:		
Numerator:		
Net loss	$ (169)	$ (238)
Denominator:		
Weighted average common shares outstanding for basic and diluted calculation	120.9	107.5
Net loss per common share—basic and diluted:		
Net loss per common share—basic and diluted	$ (1.40)	$ (2.21)

The calculation of diluted net loss per share includes an adjustment to the weighted-average common shares outstanding for the potential dilution that would occur if the Company's stock options or warrants were exercised or the Company's restricted stock had vested. In the periods reported, the effect of the assumed exercise of stock options and warrants and the assumed vesting of restricted shares would have been antidilutive and accordingly, the following share amounts were excluded from the calculation of diluted net loss per share:

	Year ended September 30, 2005	Seven Months Ended September 30, 2004
Stock options	2,298,844	511,810
Restricted stock	6,146,792	4,997,356

See Note 18 for a summary of restricted stock and stock options outstanding during the period and Note 19 for a summary of the terms of the warrants that were issued to Time Warner in connection with the Acquisition.

5. The Acquisition

As previously described in Note 1, effective as of March 1, 2004, a subsidiary of the Company acquired Old WMG from Time Warner for approximately $2.6 billion. The initial consideration exchanged consisted of $2.560 billion of cash and $35 million of non-cash consideration in the form of warrants that gave Time Warner the right, under certain conditions, to purchase up to 19.9% of the capital stock of the Company (see Note 19). In addition, the Company incurred approximately $78 million of transaction costs in connection with the Acquisition.

Pursuant to the terms of the purchase agreement between the Company and Time Warner, the purchase consideration is subject to certain adjustments, generally based on changes in the financial position of Old WMG between the date the purchase agreement was signed and the date the transaction closed. The parties currently are in discussions over the terms of final settlement. Such changes are not expected to be material; however, the purchase price reflected in the accompanying financial statements has been reduced by approximately $12 million to reflect a reimbursement by Time Warner to the Company of a portion of the purchase consideration already agreed to by the parties.

The $2.638 billion cash portion of the purchase price, including transaction costs, was financed by a $1.250 billion initial capital investment by the Investor Group and aggregate borrowings of $1.388 billion. The

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

$1.250 billion initial capital investment by the Investor Group was comprised of (i) an $85 million contribution in exchange for the issuance of 85,000 shares of Class A Common Stock of the Company, (ii) a $765 million contribution in exchange for the issuance of 9,445 shares of Class L Common Stock of the Company and (iii) a $400 million direct contribution to Holdings in exchange for 40,000 shares of cumulative preferred stock of Holdings. The Company also incurred $262 million of additional indebtedness to pay certain financing-related fees, as well as to fund future working capital requirements that included a portion of the anticipated costs to restructure the business. See Note 14 for a description of the Company's financing arrangements and Note 19 for a description of the returns of capital paid to the Investor Group subsequent to the Acquisition.

The Acquisition was accounted for by the purchase method of accounting for business combinations. Under the purchase method of accounting, the acquisition cost of $2.638 billion, including $78 million of transaction costs and the $12 million reduction in the purchase price described above, was preliminarily allocated to the net assets acquired in proportion to estimates of their respective fair values. The excess of the purchase price over the estimated fair value of the net assets acquired was recorded as goodwill.

The accompanying consolidated financial statements include the following allocation of the purchase price to the net assets acquired: recorded music catalog, $1.216 billion; music publishing copyrights, $808 million; trademarks, $110 million; goodwill, $846 million; other current and noncurrent assets, $1.852 billion; net deferred tax liabilities, $163 million; acquisition-related restructuring liabilities, $275 million; and other current and noncurrent liabilities, $1.756 billion.

Pro Forma Financial Information

The following unaudited pro forma financial information presents the operating results of the Company as if each of (i) the Acquisition and original financing, (ii) the April 2004 Acquisition Corp. Refinancing (as described under Note 14) and (iii) the transactions with Cinram International Inc. with respect to manufacturing, packaging and physical distribution services (as described under Note 6), had occurred at the beginning of each period presented (in millions):

	Pro Forma		
	Ten Months Ended September 30, 2004	Twelve Months Ended September 30, 2004	Year Ended November 30, 2003
Revenue	$ 2,548	$ 3,436	$ 3,361
Impairment of goodwill and other intangible assets	—	(1,019)	(1,019)
Depreciation and amortization	(201)	(245)	(257)
Operating income (loss)	16	(929)	(1,017)
Net loss	(286)	(1,026)	(914)

2003 Deal-Related and Other Transaction Costs

In connection with the Acquisition and the prior pursuit by Time Warner and Old WMG of other strategic ventures or dispositions involving Old WMG's businesses in 2003 that did not occur, Old WMG incurred approximately $70 million of costs, as follows (in millions):

	Year Ended November 30, 2003
Transaction costs, primarily legal, accounting and investment banking fees	$ 30
Loss on executive contractual obligations	25
Loss on pension plan curtailment	15
	$ 70

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

As part of the Acquisition, the Investor Group and Time Warner agreed that Time Warner would retain its obligations to all employees of Old WMG covered under Time Warner's U.S. pension plans; however, employees of Old WMG would no longer be able to earn additional benefits for future services. Accordingly, Old WMG recognized a $15 million loss in 2003 in connection with the pension curtailment that ultimately occurred upon the closing of the Acquisition. In addition, Old WMG recorded a $25 million loss in 2003 relating to certain executive contractual obligations that were triggered upon the closing of the Acquisition.

6. Other Acquisitions and Dispositions

Bad Boy Records LLC Joint Venture

On April 8, 2005, the Company entered into an agreement with an affiliate of Sean "Diddy" Combs to form Bad Boy Records LLC ("Bad Boy"), a joint venture, owned 50% by the Company and 50% by the affiliate. The Company purchased its 50% membership interest in Bad Boy Records LLC for approximately $30 million in cash. The joint venture includes catalog and roster artists such as Notorious B.I.G., Mario Winans, Mase, Carl Thomas, B5, Boyz N Da Hood and Diddy. Mr. Combs is the CEO of the joint venture and supervises its staff and day-to-day operations. The Company provides funding, marketing, promotion and certain backoffice services for the joint venture. The transaction was accounted for under the purchase method of accounting during the third quarter of fiscal 2005 as the Company bears a majority of the financial risks and rewards associated with the venture. The results of operations of Bad Boy are included in the Company's results of operations from its acquisition date. The accompanying consolidated financial statements include the following allocation of the approximately $30 million purchase price to the Company's share of underlying net assets based on their respective fair values: recorded music catalog, $9 million; artists' contracts, $14 million; goodwill, $20 million; and other current liabilities, $14 million.

Sale of Music Manufacturing

In October 2003, Time Warner completed its sale of the DVD and CD manufacturing, printing, packaging, physical distribution and merchandising businesses formerly managed by Old WMG for $1.05 billion in cash to Cinram International Inc. ("Cinram"). The sale included the following businesses: WEA Manufacturing Inc., Warner Music Manufacturing Europe GmbH, Ivy Hill Corporation, Giant Merchandising and the physical distribution operations of WEA Corp.

In addition, Time Warner and Old WMG entered into exclusive, long-term agreements for Cinram to provide manufacturing, printing, packaging and physical distribution of Time Warner's and the Company's DVDs and CDs in North America and Europe at fair market value-based rates. Cinram is currently the Company's exclusive supplier of such services in North America and most of Europe.

As previously noted, the physical distribution operations of WEA Corp., which are included in the accompanying financial statements, were included in the sale. Old WMG recognized a $12 million pretax loss in 2003 in connection with the sale, which has been reflected as a component of operating loss in the accompanying statement of operations. For the year ended November 30, 2003, Old WMG included in its accompanying statement of operations approximately $15 million of revenues; approximately $11 million of operating losses; approximately $4 million of operating losses before depreciation and amortization expense; and an approximate $7 million net loss related to the physical distribution operations of WEA Corp.

Acquisition of Certain Minority Interests in Maverick Recording Company

As of September 30, 2004, the Company had a 50% interest in Maverick Recording Company ("Maverick"). In November 2004, the Company acquired an additional 30% interest in Maverick from its existing partner for approximately $17 million and certain amounts previously owed by such partner to the Company. The transaction was accounted for under the purchase method of accounting during the first quarter of

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

fiscal 2005. The purchase price was allocated to the underlying net assets of Maverick in proportion to their estimated fair value, principally artist contracts and recorded music catalog. As part of the transaction, the Company and the remaining partner in Maverick entered into an agreement pursuant to which either party can elect to have the Company purchase the remaining 20% interest in Maverick that it does not own by December 2007.

Sale of Warner Bros. Publications

On May 31, 2005, the Company sold Warner Bros. Publications, which conducted the Company's printed sheet music operations, to Alfred Publishing. As part of the transaction, the Company agreed to license the right to use its music publishing copyrights in the exploitation of printed sheet music and songbooks for a twenty-year period of time. No gain or loss was recognized on the transaction, as the historical book basis of the net assets sold was adjusted to fair value in connection with the accounting for the Acquisition. Due to the Company's continuing involvement with Warner Bros. Publications, it was not reported as discontinued operations.

The sale is not expected to have a material effect on the future operating results and financial condition of the Company. For the year ended September 30, 2005, the ten months ended September 30, 2004, and the year ended November 30, 2003, the operations being sold generated revenues of approximately $35 million, $36 million, and $56 million, respectively; operating income (loss) of approximately $1 million, $(7) million, and $1 million, respectively; operating income (loss) before depreciation and amortization expense of $1 million, $(7) million, and $2 million, respectively; and net losses of approximately $1 million, $8 million, and $2 million, respectively.

7. Investments

The Company's investments consist of:

	September 30, 2005	September 30, 2004
	(In millions)	
Equity-method investments	$ 11	$ 8
Cost-method investments	10	—
	$ 21	$ 8

In connection with the Acquisition, primarily all of Old WMG's investments were transferred to Time Warner. Significant equity-method investments held by the Company at September 30, 2004 related to the Company's continuing interest in Deston Songs and a new investment made in 2004 in Royalty Services, L.P. (25% owned) to develop a shared royalty system platform with Universal Music Group, Exigen Group and Lightspeed Venture Partners.

In 2005, the Company disposed of its equity-method investment in Deston Songs, and made additional capital contributions to its investment in Royalty Services, L.P., as required by the agreement. Additionally, during 2005 the Company made an investment of $9 million to acquire a 15% interest in Front Line Management, a cost-method investment, and other equity investments of $4 million. Such investments are not material to the Company's overall financial position or operating results.

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

Net Investment-Related Gains (Losses)

For the year ended September 30, 2005 the Company recognized $1 million of net investment-related gains, primarily related to the disposition of an equity-method investment. There were no significant investment-related gains or losses recognized in either the seven-month period ended September 30, 2004 nor the three-month period ended February 29, 2004.

For the year ended November 30, 2003, Old WMG recognized $26 million of net investment-related losses, principally to reduce the carrying value of certain investments, including Old WMG's interest in Telstar. Of such amount, approximately $17 million of net investment-related losses were recognized by Old WMG in the ten-month period ended September 30, 2003.

8. Inventories

Inventories consist of the following:

	September 30, 2005	September 30, 2004
	(in millions)	
Compact discs, cassettes and other music-related products	$ 84	$ 79
Published sheet music and song books	2	23
	86	102
Less reserve for obsolescence	(34)	(37)
	$ 52	$ 65

The decline in published sheet music and song books relates to the sale of the Company's printed music operations as described in Note 6.

9. Property, Plant and Equipment

Property, plant and equipment consist of the following:

	September 30, 2005	September 30, 2004
	(in millions)	
Land	$ 23	$ 19
Buildings and improvements	107	109
Furniture and fixtures	17	16
Computer hardware and software	91	78
Machinery and equipment	3	3
	241	225
Less accumulated depreciation	(84)	(36)
	$ 157	$ 189

10. Goodwill and Intangible Assets

Impairment Charges

During the fourth quarter of the fiscal year ended November 30, 2003, in connection with Time Warner's agreement to sell Old WMG as described more fully in Note 5, Old WMG recorded a $1.019 billion impairment

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charge. The charge was necessary to reduce the carrying value of Old WMG's intangible assets to fair value, based on the consideration agreed to be exchanged in the transaction. The impairment charge is classified as a component of operating loss in the accompanying statement of operations. The charge consisted of a reduction in the carrying value of goodwill by $5 million, brands and trademarks by $766 million, recorded music catalog by $208 million and other intangible assets by $40 million. The impairment charge was non-cash in nature and did not affect Old WMG's liquidity.

Goodwill

The following analysis details the changes in goodwill for each reportable segment during the year ended September 30, 2005 and the ten months ended September 30, 2004:

	Recorded Music	Music Publishing	Total
		(in millions)	
Balance at November 30, 2003	$ —	$ —	$ —
Acquisition of Old WMG	395	583	978
Balance at September 30, 2004	$ 395	$ 583	$ 978
Acquisitions	23	—	23
Purchase accounting adjustments	(124)	(8)	(132)
Balance at September 30, 2005	$ 294	$ 575	$ 869

The acquisition of goodwill primarily relates to the acquisition of a 50% interest in Bad Boy as described in Note 6. The allocation of the Bad Boy purchase price included approximately $20 million of goodwill acquired.

Purchase accounting adjustments relate to changes in the initial estimates of the restructuring costs that arose from the Acquisition and changes to the fair value of assets and liabilities recorded in connection with the Acquisition. These changes were determined in connection with the Company's finalization of the purchase price allocation related to the Acquisition and include the settlement of certain receivables from Time Warner for an amount that is $12 million less than the original amount recorded. The remaining adjustments relate mainly to revisions of the costs to terminate artist contracts and other long-term agreements, and changes to pre-Acquisition deferred tax liability and taxes payable balances.

The Company performs its annual goodwill impairment test in accordance with FAS 142 during the fourth quarter of each fiscal year. 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. The Company conducted its annual goodwill impairment test in September of 2005. The results of the test were that no impairment occurred in 2005.

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Other Intangible Assets

Other intangible assets consist of the following:

	September 30, 2004	Acquisitions	Other (a)	September 30, 2005
				(in millions)
Intangible assets subject to amortization:				
Record music catalog	$ 1,216	$ 33	$ (7)	$ 1,242
Music publishing copyrights	811	16	(10)	817
Artist contacts	—	31	—	31
Trademarks	10	—	—	10
Other intangible assets	4	—	—	4
	2,041	80	(17)	2,104
Accumulated amortization	(104)			(289)
Total net intangible assets subject to amortization	1,937			1,815
Intangible assets not subject to amortization:				
Trademarks and brands	100			100
Total net other intangible assets	$ 2,037			$ 1,915

(a) Other represents foreign currency translation adjustments.

The increase in the Company's gross intangible assets represents the allocation of the purchase price of the Company's acquisition of an additional interest in Maverick to the net assets acquired, principally music copyrights of approximately $17 million and artist contracts of approximately $16 million, and the acquisition of a 50% interest in Bad Boy as described in Note 6, including the acquisition of recorded music catalog of approximately $9 million and artist contracts of approximately $14 million. The increase also relates to the acquisition of approximately $16 million of publishing copyrights during the year ended September 30, 2005.

Amortization

Based on the amount of intangible assets subject to amortization at the end of September 2005, the expected amortization for each of the next five fiscal years is as follows:

	Years Ended September 30,
	(in millions)
2006	$ 188
2007	188
2008	188
2009	187
2010	181
Thereafter	883
	$ 1,815

The life all acquired intangible assets is evaluated based on the expected future cash flows associated with the asset. The expected amortization expense above reflects estimated useful lives assigned to the Company's identifiable, finite-lived intangible assets established in the accounting for the Acquisition effective as of

March 1, 2004 as follows: ten years for recorded music catalog, fifteen years for music publishing copyrights and fifteen years for trademarks. Artist contracts acquired by the Company have variable estimated useful lives which do not exceed ten years.

Amortization expense included in Old WMG's statement of operations for each of the three months ended February 29, 2004 and the year ended November 30, 2003 was based on different estimated useful lives assigned to Old WMG's identifiable, finite-lived intangible assets. For each of the three months ended February 29, 2004 and the year ended November 30, 2003, estimated useful lives of fifteen years were assigned to both of Old WMG's recorded music catalog and music publishing copyrights. The change in estimated useful lives from 2003 to 2004 was implemented in connection with the valuation of the Company's intangible assets in connection with the Acquisition. See Note 5 for a discussion of the pro forma effects of the Acquisition on the historical operating results of Old WMG, including the effects from the aforementioned changes in estimated useful lives.

11. Restructuring Costs

2005 Restructuring Activities

In August of 2005, Jason Flom, the co-chairman of The Atlantic Records Group left the Company. In an effort to streamline the businesses, the Company merged the operations of Lava Records into the operations of The Atlantic Records Group in September 2005. As a result, certain employee positions at Lava were restructured. In addition to restructuring such employee positions, the Company evaluated its workforce at other affiliates and restructured certain other positions in order to maximize cost-effectiveness. These employee terminations resulted in restructuring charges of $4 million in the year ended September 30, 2005. Additionally, certain artists' contracts were terminated as part of the cost-saving initiative. Such artist contract terminations resulted in $3 million restructuring charges in the year ended September 30, 2005.

Acquisition-Related Restructuring Costs

In connection with the Acquisition that was effective as of March 1, 2004, the Company reviewed its operations and implemented several plans to restructure its operations. As part of these restructuring plans, the Company recorded a restructuring liability of approximately $307 million during 2004. This restructuring liability included costs to exit and consolidate certain activities of the Company, as well as costs to terminate employees and certain artist, songwriters and co-publisher contracts. Such liabilities were recognized as part of the cost of the Acquisition.

Of the total $307 million restructuring costs recorded by the Company, approximately $164 million related to work-force reductions, including employee termination benefits and relocation costs; approximately $75 million related to costs to terminate certain artist, songwriters and co-publisher contracts; and the balance of approximately $68 million related to other anticipated costs to exit certain leased facilities and operations, such as international distribution operations. The number of employees identified to be involuntarily terminated approximated 1,600.

Based on the restructuring plans already implemented, the Company revised its original estimates of restructuring costs during the year ended September 30, 2005. This resulted in an overall reduction in the restructuring costs of approximately $32 million. The Company's restructuring liabilities and goodwill as of September 30, 2005 have been reduced by such amounts. As of September 30, 2005, the Company had approximately $49 million of liabilities for Acquisition-related restructuring costs recorded in its balance sheet. These liabilities represent estimates of future cash obligations for all restructuring activities that had been

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implemented. The outstanding balance of these liabilities primarily relate to extended payment terms for long-term lease obligations for vacated facilities or long-term artist commitments. These remaining lease obligations are expected to be settled by 2019. We expect to pay a majority of the remaining costs in fiscal 2006.

	Employee Terminations	Other Exit Costs	Total
		(In millions)	
Liability as of November 30, 2003	$ —	$ —	$ —
Additions in 2004	164	143	307
Cash paid in 2004	(92)	(13)	(105)
Non-cash reductions in 2004(a)	(1)	(22)	(23)
Liability as of September 30, 2004	$ 71	$ 108	$ 179
Cash paid in 2005	(53)	(27)	(80)
Non-cash reductions in 2005(a)	—	(18)	(18)
Reversals of PPA liabilities in 2005	(4)	(28)	(32)
Liability as of September 30, 2005	$ 14	$ 35	$ 49

(a) Principally relates to changes in foreign currency exchange rates, the non-cash write-off of the carrying value of advances relating to terminating certain artist, songwriter and co-publisher contracts.

Cost-Savings Incentive Plan

In addition, in connection with the Acquisition, the Company approved a cost-savings incentive compensation plan during 2004 in order to incentivize management to implement the aforementioned restructuring plans and reduce operating costs. Under the plan, key employees of the Company were entitled to earn up to $20 million in the aggregate based on the attainment and maintenance of certain cost-savings targets. Based on the level of cost savings actually generated at the end of September 30, 2004, which exceeded the cost savings targets under the plan, the Company determined that it was probable that eligible employees would vest in the full benefits under the plan. Accordingly, the Company expensed the full $20 million liability under the plan, along with other restructuring-related costs of $6 million, during the seven months ended September 30, 2004. Out of the aggregate $26 million liability, $16 million has been paid during the year ended September 30, 2005. We expect to pay the remaining $10 million in fiscal 2006.

Other Non-Acquisition Related Restructuring Costs

In addition to the costs of restructurings associated with acquisition and merger activities, Old WMG has also recognized restructuring costs that are unrelated to business combinations and are expensed as incurred.

2003 Restructuring Activities

During 2003, in a continuing effort to reduce costs, Old WMG implemented a series of significant restructuring activities. In particular, Old WMG restructured its domestic distribution operations, outsourced its Canadian distribution operations, and continued to reduce its worldwide headcount to adjust to changing economic conditions in various markets. In connection with these initiatives, Old WMG recognized restructuring charges of approximately $35 million in 2003. Of this amount, approximately $22 million related to work-force reductions, including employee termination benefits and relocation costs, and approximately $13 million related to other anticipated costs to exit certain facilities. The number of employees that were involuntarily terminated approximated 365. All restructuring activities were completed by the end of 2003.

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As of November 30, 2003, there was approximately $10 million of non-Acquisition related restructuring costs that had yet to be paid, principally relating to severance obligations and long-term lease obligations for vacated facilities. As previously noted, in connection with the Acquisition, Time Warner agreed to assume all unpaid severance obligations from Old WMG. Accordingly, all such liabilities were transferred to Time Warner effective as of March 1, 2004. In addition, in connection with the Acquisition, the Company reevaluated its global facility requirements and further consolidated its real estate holdings. As part of this re-evaluation, the Company remeasured the fair value of its long-term lease obligations for vacated facilities, eliminated the pre-existing $2 million book value of the lease obligations for vacated facilities and recorded the net impact as an addition to goodwill. See prior discussion of Acquisition-related restructuring costs.

The restructuring costs related to each of the Company's business segments, as well as corporate-level employees. Selected information related to the 2003 restructuring plans by business segment is as follows (in millions):

Employee Terminations

	Recorded Music	Music Publishing	Corporate	Total
Additions in 2003	$ 18	$ 3	$ 1	$ 22
Cash paid in 2003	(13)	(1)	—	(14)
Liability as of November 30, 2003	5	2	1	8
2004 activity; primarily adjustments relating to the Acquisition	(5)	(2)	(1)	(8)
Liability as of September 30, 2004	$ —	$ —	$ —	$ —

Other Exit Costs

	Recorded Music	Music Publishing	Corporate	Total
Additions in 2003	$ 13	$ —	$ —	$ 13
Cash paid in 2003	(10)	—	—	(10)
Non-cash reductions in 2003	(1)	—	—	(1)
Liability as of November 30, 2003	2	—	—	2
2004 activity; primarily adjustments relating to the Acquisition	(2)	—	—	(2)
Liability as of September 30, 2004	$ —	$ —	$ —	$ —

12. Other Current and Noncurrent Liabilities

Other current liabilities consist of the following (in millions):

	September 30, 2005	September 30, 2004
Accrued expenses	$ 166	$ 159
Accrued compensation and benefits	107	93
Deferred income	46	46
Acquisition and merger-related restructuring liabilities	30	90
Other contractual obligations	19	—
Fair value of warrants	—	155
Accrued interest	33	131
Cost-savings incentive plan payable	10	10
Dividends payable	1	—
Other	2	3
	$ 404	$ 587

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Other noncurrent liabilities consist of the following (in millions):

	September 30, 2005	September 30, 2004
Deferred income	$ 15	$ 25
Accrued compensation and benefits	21	29
Minority interest	19	19
Cost-savings incentive plan payable	—	10
Acquisition and merger-related restructuring liabilities	19	89
Unfavorable and other contractual obligations	132	135
Licensing advance payable	8	8
Other	22	28
	$ 226	$ 333

Licensing Advance Payable

Other noncurrent liabilities include an $8 million obligation at each of September 30, 2005 and 2004 to repay an advance received in a prior period under a licensing agreement. Under the terms of the original agreement, such amount was subject to repayment if the advance was not recouped from royalties generated under the agreement by November 30, 2003. In June 2003, the parties entered into an amended agreement whereby, in connection with an extension of the term of the original agreement, the Company agreed to repay the advance over a six-year period ended November 30, 2009. Of the total repayment amount, $2 million was repaid in 2003. The remaining $8 million is repayable as follows: 2006, $0.5 million; 2007, $0.5 million; 2008, $3 million; and 2009, $4 million.

13. Note Payable to Shareholders

In September 2004, the Company declared a $342 million dividend to its shareholders in the form of a note payable. The note payable was interest-bearing at a rate of 10% per annum. The note payable was paid in October 2004 using proceeds received from a return of capital previously invested in Acquisition Corp. Interest paid to the Company's shareholders under the note payable amounted to approximately $1 million.

14. Debt

In connection with the Acquisition, the Company incurred $1.650 billion of indebtedness consisting of (i) $1.150 billion of borrowings under the term loan portion of a senior secured credit facility and (ii) $500 million of borrowings under a senior subordinated bridge loan facility (the "Bridge Loan"). A portion of these borrowings was refinanced by WMG Acquisition Corp., a subsidiary of the Company, in April 2004 (the "Acquisition Corp. Refinancing"). In addition, in December 2004, Holdings incurred approximately $700 million of debt to redeem its outstanding shares of cumulative preferred stock and pay a return of capital to the Investor Group (the "Holdings Refinancing"). A portion of this debt was redeemed in June 2005 (the "Holdings Redemption"). The following summarizes the Acquisition Corp. Refinancing, the Company's debt capitalization as of September 30, 2005 and 2004, the principal terms of the Company's financing arrangements, the Holdings Refinancing.

The Acquisition Corp. Refinancing

In April 2004, the Company incurred $697 million of new indebtedness, consisting of the issuance by Acquisition Corp. of (i) $465 million principal amount of 7.375% Senior Subordinated Notes due 2014,

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(ii) 100 million Sterling principal amount of 8.125% Senior Subordinated notes due 2014 (U.S. dollar equivalent of $182 million as of April 2004) and (iii) $50 million of additional borrowings under the term loan portion of the Company's senior secured credit facility.

Together with available cash on hand, such proceeds were used (i) to repay all $500 million of borrowings under the Bridge Loan, (ii) to redeem a portion of the cumulative preferred stock of Holdings in the amount of $202 million and (iii) to pay certain financing-related transaction costs.

In connection with this re-financing, the Company incurred a $6 million pretax loss during the seven months ended September 30, 2004 to write off the carrying value of its unamortized debt issuance costs paid in connection with its borrowings under the Bridge Loan.

Debt Capitalization

As of September 30, 2005 and 2004, the Company's long-term debt consisted of (in millions):

	September 30, 2005	September 30, 2004
Senior secured credit facility:		
Revolving credit facility	$ —	$ —
Term loan	1,430	1,194
	1,430	1,194
7.375% U.S. dollar-denominated Notes due 2014—Acquisition Corp	465	465
8.125% Sterling-denominated Notes due 2014—Acquisition Corp	177	181
9.5% Senior Discount Notes due 2014—Holdings	174	—
Total debt	2,246	1,840
Less current portion	(17)	(12)
Total long term debt	$ 2,229	$ 1,828

Senior Secured Credit Facility

Holdings and Acquisition Corp. are party to a senior secured credit facility that was entered into in connection with the Acquisition. The senior secured credit facility consists of a $1.2 billion term loan portion and a $250 million revolving credit portion. The term loan portion of the facility matures in seven years in February 2011. Acquisition Corp. is required to prepay outstanding term loans, subject to certain exceptions and conditions, with excess cash flow or in the event of certain asset sales, casualty and condemnation events and incurrence of debt. Acquisition Corp. is required to make minimum repayments under the term loan portion of the facility in quarterly principal amounts of $4.2 million for the first six years and nine months, with a remaining balloon payment in February 2011.

The revolving credit portion of the senior secured facility matures in six years in February 2010. There are no mandatory reductions in borrowing availability for the revolving credit portion of the facility through its term.

Borrowings under both the term loan and revolving credit portion of the senior secured credit facility bear interest at a rate equal to an applicable margin plus, at the Company's option, either (a) a base rate determined by reference to the higher of (1) the prime rate of Bank of America, N.A. and (2) the federal funds rate plus 1/2 of 1% or (b) a LIBOR rate determined by reference to the costs of funds for deposits in the currency of such borrowing for the interest period relevant to such borrowing adjusted for certain additional costs. The initial

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applicable margin for borrowings under the revolving credit facility and the term loan facility is 1.75% with respect to base rate borrowings and 2.75% with respect to LIBOR borrowings. The applicable margins for borrowings under the senior secured credit facility may be reduced, subject to Acquisition Corp. attaining certain leverage ratios.

In addition to paying interest on outstanding principal under the senior secured credit facility, Acquisition Corp. is required to pay a commitment fee to the lenders under the revolving credit facility in respect of the unutilized commitments. The initial commitment fee rate is .50%. As of September 30, 2005, the commitment fee rate was 0.375%. The commitment fee rate may be reduced subject to Acquisition Corp. attaining certain leverage ratios. Acquisition Corp. is also required to pay customary letter of credit fees, as necessary.

The senior secured credit facility contains a number of covenants that, among other things, restrict, subject to certain exceptions, Acquisition Corp.'s ability and the ability of its subsidiaries to sell assets, incur additional indebtedness or issue preferred stock, repay other indebtedness, pay dividends and distributions or repurchase capital stock, create liens on assets, make investments, loans or advances, make certain acquisitions, engage in mergers or consolidations, engage in certain transactions with affiliates, amend certain material agreements, change the business conducted by itself, its parent company and its subsidiaries, and enter into agreements that restrict dividends from subsidiaries. In addition, the secured credit facility requires Acquisition Corp. to maintain the following financial covenants: a maximum total leverage ratio, a minimum interest coverage ratio and a maximum capital expenditures limitation.

The Company obtained an amendment to its senior secured credit facility in May of 2005 to provide for, among other things, an additional term loan of $250 million which the Company has obtained concurrent with the Initial Common Stock Offering, a reduction in the margin applicable on the term loan, and more flexibility under certain restrictive covenants.

Senior Subordinated Notes due 2014

The Company has outstanding two tranches of Senior Subordinated notes of Acquisition Corp. due 2014: $465 million principal amount of U.S. dollar-denominated notes (the "U.S. Notes") and 100 million principal amount of Sterling-denominated notes (the "Sterling Notes" and collectively, the "Subordinated Notes"). The Subordinated Notes mature on April 15, 2014. Interest is payable on the Subordinated Notes on a semi-annual basis at a fixed rate of 7.375% per annum for the U.S. Notes and 8.125% per annum for the Sterling Notes.

The Subordinated Notes are redeemable in whole or in part, at the option of Acquisition Corp., at any time at a redemption price defined under the indenture governing the Subordinated Notes (the "Indenture") that generally includes a premium. In addition, upon a change of control of Acquisition Corp. and upon certain asset sales as specified under the Indenture, Acquisition Corp. may be required to make an offer to redeem the Subordinated Notes from the holders at a redemption price defined under the Indenture that includes a premium.

The Subordinated Notes are unsecured and subordinated to all of Acquisition Corp.'s existing and future senior indebtedness, including Acquisition Corp.'s obligations under its senior secured credit facility. Each of Acquisition Corp.'s wholly owned domestic subsidiaries that have guaranteed the obligations under Acquisition Corp.'s senior secured credit facility also have guaranteed the Subordinated Notes on a joint, several and unconditional basis.

The Indenture limits Acquisition Corp.'s ability and the ability of its restricted subsidiaries to incur additional indebtedness or issue certain preferred shares; to pay dividends on or make other distributions in respect of its capital stock or make other restricted payments; to make certain investments; to sell certain assets;

to create liens on certain debt without securing the notes; to consolidate, merge, sell or otherwise dispose off all or substantially all of its assets; to enter into certain transactions with affiliates; and to designate its subsidiaries as unrestricted subsidiaries.

Subject to certain exceptions, the Indenture permits Acquisition Corp. and its restricted subsidiaries to incur additional indebtedness, including secured indebtedness.

The Holdings Refinancing

In December 2004, Holdings issued $847 million principal amount of debt consisting of (i) $250 million principal amount of Floating Rate Senior Notes due 2011 (the "Holdings Floating Rate Notes"), (ii) $397 million principal amount at maturity of 9.5% Senior Discount Notes due 2014, which had an initial issuance discount of $147 million (the "Holdings Discount Notes") and (iii) $200 million principal amount of Floating Rate Senior PIK Notes due 2014 (the "Holdings PIK Notes," and collectively, the "Holdings Notes"). The gross proceeds of $696 million received from the issuance of the Holdings Notes were used to (i) redeem the remaining shares of cumulative preferred stock of Holdings at a redemption price of $209 million, including $9 million of accrued and unpaid dividends, (ii) pay a return of capital to Parent Corp. and its shareholders in the aggregate amount of $472 million and (iii) pay debt-related issuance costs of approximately $15 million.

The Holdings Redemption

In June 2005, using proceeds from the Company's Initial Common Stock Offering and approximately $57 million of cash on hand, Holdings redeemed all of the Holdings Floating Rate Notes, all of the Holdings PIK Notes, and 35% of the aggregate outstanding principal at maturity of the Holdings Discount Notes.

The Holdings Floating Rate Notes were redeemed in full on June 15, 2005. From the issuance date through the redemption date, the notes bore interest at a quarterly floating rate based on three-month LIBOR rates plus a margin equal to 4.375%. Interest was payable quarterly in cash beginning on March 15, 2005.

The Holdings Discount Notes were issued at a discount and have an initial accreted value of $630.02 per $1,000 principal amount at maturity. Prior to December 15, 2009, no cash interest payments are required. However, interest accrues on the Holdings Discount Notes in the form of an increase in the accreted value of such notes such that the accreted value of the Holdings Discount Notes will equal the principal amount at maturity on December 15, 2009. Thereafter, cash interest on the Holdings Discount Notes is payable semi-annually at a fixed rate of 9.5% per annum. The Holdings Discount Notes mature on December 15, 2014. The Company redeemed 35% of the Holdings Discount Notes on June 15, 2005.

The Holdings PIK Notes were redeemed in full on June 15, 2005. From the date of issuance through the date of redemption, the notes bore interest at a semi-annual, floating rate based on six-month LIBOR rates plus a margin equal to 7%. Interest was accrued in the form of additional PIK Notes at the election of the Company. Such amounts were also repaid in connection with the redemption.

In connection with the redemption of the Holdings Floating Rate Notes and 35% of the Holdings Discount Notes, the Company was required to pay redemption premiums of $10 million and $9 million, respectively, which the Company paid on June 15, 2005 and recorded as a loss on the repayment of the notes in the consolidated statement of operations for the year ended September 30, 2005.

The Company was also required to pay all accrued interest as of the redemption date related to the Holdings Notes that were redeemed. This amount consisted of $5 million related to the Holdings Floating Rate Notes, $9 million related to the Holdings PIK notes, and $4 million in accreted value of the 35% of Holdings Discount

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Notes redeemed. Of such amount, $8 million had been expensed in previous quarters and $10 million was recorded as interest expense in the consolidated statement of operations for the year ended September 30, 2005.

In connection with the redemption of certain of the Holdings Notes, the Company also wrote off the remaining balance of debt-issuance costs of $12 million related to the notes redeemed and the remaining unamortized original issue discount of $4 million related to the Holdings PIK Notes. Such amounts were recorded as a loss on the repayment of the notes in the consolidated statement of operations for the year ended September 30, 2005.

Parent has fully and unconditionally guaranteed the remaining Holdings Discount Notes. The Holdings Notes are unsecured and subordinated to all of Holdings' existing and future secured debt, including Holdings' guarantee of borrowings by Acquisition Corp. under the Company's senior secured credit facility. In addition, the Holdings Notes are structurally subordinated to the Subordinated Notes of Acquisition Corp.

The Indentures limit Holdings' ability and the ability of its restricted subsidiaries to incur additional indebtedness or issue certain preferred shares; to pay dividends on or make other distributions in respect of its capital stock or make other restricted payments; to make certain investments; to sell certain assets; to create liens on certain debt without securing the notes; to consolidate, merge, sell or otherwise dispose of all or substantially all of its assets; to enter into certain transactions with affiliates; and to designate its subsidiaries as unrestricted subsidiaries.

Restricted Net Assets

The Company is a holding company with no independent operations or assets other than through its interests in its subsidiaries, such as Holdings and Acquisition Corp. Accordingly, the ability of the Company to obtain funds from its subsidiaries is restricted by the senior secured credit facility of Acquisition Corp., the indenture for the Subordinated Notes issued by Acquisition Corp., and the indentures for the Holdings Notes.

Pre-Acquisition Debt

During 2003, the Company incurred approximately $114 million of indebtedness in connection with a recapitalization of certain wholly owned international subsidiaries. The principal amount of 100 million Euros was owed to Societe General and was repaid in 2004 in connection with the Acquisition.

Interest Expense and Maturities

Total interest expense, including amounts payable to Time Warner and its affiliates for all periods prior to the closing of the Acquisition, was $182 million for the year ended September 30, 2005, $88 million for the seven months ended September 30, 2004, $3 million for the three months ended February 29, 2004, and $47 million for the year ended November 30, 2003. The weighted-average interest rate of the Company's total debt at September 30, 2005 and 2004 was 6.55% and 5.75%, respectively.

Based on the amount of debt outstanding as of September 30, 2005, annual repayments of long-term debt for each of the five years subsequent to September 30, 2005 are approximately $17 million per year.

Fair Value of Debt

Based on the level of interest rates prevailing at September 30, 2005, the fair value of the Company's fixed-rate debt exceeded its carrying value by approximately $10.6 million. Unrealized gains or losses on debt do not result in the realization or expenditure of cash and generally are not recognized for financial reporting purposes unless the debt is retired prior to its maturity.

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15. Income Taxes

For the year ended September 30, 2005 and the seven months ended September 30, 2004, the Company is a stand-alone tax filer. However, for all periods prior to the closing of the Acquisition, which includes the three months ended February 29, 2004 and the year ended November 30, 2003, the taxable results of Old WMG were included in the consolidated U.S. federal and various U.S. state and local, and foreign income tax returns of Time Warner or its subsidiaries. Also, in certain U.S. state and local, and foreign jurisdictions, Old WMG filed on a stand-alone basis. The tax provisions and related balance sheet disclosures for the periods prior to the closing of the Acquisition have been prepared assuming Old WMG was a stand-alone taxpayer for the periods presented.

Domestic and foreign pretax income (loss) are as follows (in millions):

	Successor		Predecessor	
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Year Ended November 30, 2003
Domestic	$ (194)	$ (246)	$ (40)	$ (1,304)
Foreign	80	38	25	(13)
Total	$ (114)	$ (208)	$ (15)	$ (1,317)

Current and deferred income taxes (tax benefits) provided are as follows (in millions):

	Successor		Predecessor	
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Year Ended November 30, 2003
Federal:				
Current	$ —	$ —	$ —	$ —
Deferred	—	—	(2)	(36)
Foreign:				
Current(a)	53	21	21	52
Deferred	—	8	(2)	111
U.S. State:				
Current	2	1	—	3
Deferred	—	—	—	(94)
Total	$ 55	$ 30	$ 17	$ 36

(a) Includes cash withholding taxes of $14 million, $9 million, $5 million and $19 million for the year ended September 30, 2005, seven months ended September 30, 2004, the three months ended February 29, 2004, and the year ended November 30, 2003, respectively.

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The differences between the U.S. federal statutory income tax rate of 35% and income taxes provided are as follows (in millions):

	Successor		Predecessor	
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Year Ended November 30, 2003
Taxes on income at the U.S. federal statutory rate	$ (40)	$ (73)	$ (5)	$ (461)
U.S. state and local taxes[a]	2	1	—	(59)
Non-deductible impairments of goodwill	—	—	—	2
Foreign income taxed at different rates, including withholding taxes	14	9	6	38
Unrecoverable foreign taxes due to reorganization	—	—	—	46
Current year loss without benefit	86	46	16	44
Non-deductible loss / (Non-taxable gain) on warrant	(6)	42	—	—
Non-deductible loss on minority interest	2	5	—	—
Tax loss carry forward write-off	—	—	—	423
Other	(3)	—	—	3
Total income tax expense	$ 55	$ 30	$ 17	$ 36

(a) U.S. state and local taxes for the year ended November 30, 2003 were net of U.S. federal tax benefit.

During the year ended September 30, 2005, the Company incurred losses in the U.S. and certain foreign territories. The tax benefit associated with these losses was offset by a valuation allowance as the Company has determined that it is more likely than not that these losses will not be utilized. Significant components of the Company's net deferred tax assets/(liabilities) are summarized below (in millions):

	September 30, 2005	September 30, 2004
Deferred tax assets:		
Allowances and reserves	$ 52	$ 4
Employee benefits and compensation	15	34
Other accruals	105	87
Depreciation and amortization	42	14
Tax attribute carryforwards	134	157
Other	11	2
Total deferred tax assets	359	298
Valuation allowance	(323)	(293)
Net deferred tax assets	36	5
Deferred tax liabilities:		
Assets acquired in business combinations	(201)	(232)
Total deferred tax liabilities	(201)	(232)
Net deferred tax assets (liabilities)	$ (165)	$ (227)

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At September 30, 2005, goodwill was reduced by $56 million as a result of the reversal of valuation allowances established at the acquisition date for purchase price liabilities and a determination that it is more likely than not that some portion or all of the deferred tax assets will be realized in certain foreign jurisdictions. Of the total valuation allowance of $323 million at September 30, 2005, $74 million is related to purchased deferred tax assets and when released, will be reversed through goodwill.

At September 30, 2005, the Company has U.S. federal tax net operating loss carryforwards of approximately $110 million, which will begin to expire in fiscal year 2024 and tax net operating losses in certain U.S. state and foreign jurisdictions expiring in various periods. In addition, the Company has foreign tax credit carryforwards for U.S. tax purposes of $19 million, of which $8 million and $11 million will expire in 2009 and 2015, respectively.

U.S. income and foreign withholding taxes have not been recorded on permanently reinvested earnings of certain foreign subsidiaries of approximately $400 million at September 30, 2005. As such, no federal income taxes thereon have been provided for these undistributed earnings. Should these earnings be distributed, foreign tax credits would reduce the additional federal income tax that would be payable. Availability of credits is subject to limitations; accordingly, it is not practicable to estimate the amount of the ultimate deferred tax liability, if any, on accumulated earnings.

16. Pensions and Other Postretirement Benefits

Prior the Acquisition, Old WMG employees in the U.S. and U.K. generally participated in defined benefit pension plans sponsored by Time Warner. As part of the Acquisition, Time Warner agreed to retain its obligations related to such employees of Old WMG; however, those employees are no longer eligible to earn additional benefits for future services. As a result, Old WMG recognized a $15 million loss in 2003 in connection with the probable pension curtailment that ultimately occurred upon the closing of the Acquisition.

Most international employees, such as those in Germany and Japan, participate in locally sponsored defined benefit plans, which are not considered to be material in the aggregate and have a combined projected benefit obligation of approximately $23 million and $40 million as of September 30, 2005 and 2004, respectively. Pension benefits under the Plans are based on formulas that reflect the employees' years of service and compensation levels during their employment period. The Company had an aggregate pension liability relating to these plans of approximately $23 million and $23 million recorded in its balance sheet as of September 30, 2005 and 2004, respectively.

For the year ended September 30, 2005, the seven months ended September 30, 2004, the three months ended February 29, 2004 and the year ended November 30, 2003, pension expense amounted to $6 million, $4 million, $3 million and $21 million, respectively.

Certain employees also participate in pre-tax defined contribution plans. The Company's contributions to the defined contribution plans are based upon a percentage of the employees' elected contributions. The Company's defined contribution plan expense amounted to approximately $2 million for the year ended September 30, 2005, $2 million for the seven months ended September 30, 2004, $2 million for the three months ended February 29, 2004 and $4 million for the year ended November 30, 2003.

17. Minority Interest in Preferred Stock of Subsidiary

As previously described in Note 5, a portion of the $2.6 billion purchase price for the Acquisition was funded by a $400 million direct contribution by the Investor Group to Holdings in exchange for 40,000 shares of

cumulative preferred stock of Holdings ("Holdings' Preferred Stock"). Each share of Holdings' Preferred Stock had a liquidation preference of $10,000 per share plus cumulative accrued and unpaid dividends at a rate of 10% per annum, compounded quarterly.

As previously described in Note 14, the Company redeemed half of the outstanding shares of Holdings' Preferred Stock as part of the April 2004 Acquisition Corp. Refinancing at a redemption price of $202 million, including $2 million of accrued and unpaid dividends. The remaining shares of Holdings' Preferred Stock were redeemed in December 2004 as part of the Holdings Refinancing at a redemption price of $209 million, including $9 million of accrued and unpaid dividends.

As of September 30, 2004, the outstanding shares of Holdings' Preferred Stock had a liquidation preference of $204 million. Such amount has been classified as minority interest in the accompanying consolidated balance sheet of the Company. As noted above, all such amounts were repaid prior to September 30, 2005. Cumulative dividends on the Holdings' Preferred Stock, whether paid or unpaid, were $5 million for the year ended September 30, 2005 and $14 million for the seven months ended September 30, 2004 and are classified as minority interest expense in the accompanying consolidated statement of operations of the Company.

18. Stock-Based Compensation Plans

Post-Acquisition

In connection with the Acquisition, the Company, implemented an equity-based, management compensation plan to align compensation for certain key executives with the performance of the Company. Under this plan, certain key executives were granted a combination of service-based and performance-based stock options or restricted stock. In addition, certain key executives were granted the right to purchase shares of restricted stock in the Company. Similarly, the stock options and shares of restricted stock granted allow such executives to acquire shares of common stock of the Company. A description of each type of equity-based award is described below.

Service-Based Awards

During the year ended September 30, 2005 and the seven months ended September 30, 2004, the Company granted various service-based equity awards to certain key executives of the Company. In the year ended September 30, 2005, these awards consisted of 2,643,233 stock options to purchase shares of common stock of the Company and 583,379 restricted shares of common stock of the Company. The stock options were granted under one of the Company's long-term incentive plans. In the seven months ended September 30, 2004, these awards consisted of 497,893 stock options to purchase shares of common stock of the Company and 796,701 restricted shares of common stock of the Company. The stock option awards become exercisable over a four-year vesting period tied to the executives' continuing employment and expire ten years from the date of grant. Similarly, the restricted shares vest over a four-year period, also contingent upon the employees' continued employment.

Performance-Based Awards

During the year ended September 30, 2005 and the seven months ended September 30, 2004, the Company granted various performance-based equity awards to certain key executives of the Company. In the year ended September 30, 2005, these awards consisted of 2,540,490 stock options to purchase the Company's common stock and 1,156,758 restricted shares to purchase shares of the common stock of the Company. These stock options were granted under one of the Company's long-term incentive plans. In the seven months ended September 30, 2004, these awards consisted of approximately 995,786 stock options to purchase shares of

common stock of the Company and approximately 1,593,402 restricted shares of common stock of the Company. The awards vest over a four-year period tied to the executives' continuing employment and the achievement of certain performance conditions by the Company. In particular, half of the awards have a performance condition based on a 2x liquidity event and the other half of the awards have a performance condition based on a 3x liquidity event (each respectively a "Liquidity Event").

As defined in the underlying plan agreements, a 2x or 3x Liquidity Event generally means the occurrence of an event that implies an aggregate value for the equity held by the Investor Group of 2x or 3x, respectively, of its initial value, as adjusted for prior dividends or other returns of capital received by the Investor Group. Such Liquidity Events include, but are not limited to, an initial public offering of the Company's common stock and a change-in-control transaction under which the Investor Group receives cash and/or marketable securities in exchange for its equity. In connection with the Company's Initial Common Stock Offering in May 2005, the 2x Liquidity Event occurred.

Performance-based stock option awards expire ten years from the date of grant. In addition, to the extent that the performance condition of an award is not satisfied prior thereto, the performance-based award vests on the seventh anniversary of the date of grant as long as the executive is still employed by the Company. Under the Company's LTIP program and its 2005 Omnibus Stock Plan, the Company has an additional 2,089,420 stock options or other stock based awards authorized that have not been awarded.

Purchases of Restricted Stock

During the year ended September 30, 2005 and the seven months ended September 30, 2004, the Company allowed certain key executives to purchase restricted shares of its common stock. To the extent such shares were purchased at a price equal to fair market value at the date of purchase, there was no compensatory element of the transaction. However, to the extent such shares were purchased at a price below fair market value at the date of purchase, the discount has been treated as deferred compensation in the Company's financial statements and is being expensed over the executives' expected service period.

During the year ended September 30, 2005, executives of the Company purchased 1,496,148 restricted shares of the Company's common stock at a cost of $1.04 per share, compared to the weighted-average fair value of the stock of $9.38 per share. The aggregate discount of $12 million will be expensed over the service periods of the awards.

During the seven months ended September 30, 2004, an executive of the Company purchased approximately 3,283,944 restricted shares of common stock of the Company at a fair value of $0.88 per share. Certain other executives of the Company purchased approximately 896,208 restricted shares of common stock of the Company at a cost of $0.88 per share, compared to the weighted-average fair value of the stock of $4.24 per share. The aggregate discount of approximately $3 million will be expensed over the service periods of the awards.

Of the total restricted stock awards granted and restricted stock purchased, 1,095,042 shares were vested as of September 30, 2005.

Assumptions

For purposes of applying FAS 123, the fair value of each stock option grant was estimated on the date of grant using the Black-Scholes option-pricing model, if granted prior to January 2005 and the Binomial model subsequent to January 2005, both of which are based upon several assumptions estimated by the company. The following weighted-average assumptions were used for all grants to the Company's employees in the seven

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

months ended September 30, 2004 and the twelve months ended September 30, 2005, respectively: dividend yield of 0% and 0%; expected volatility of 50% and 47.8%; risk-free interest rate of 3.07% and 3.80%; and expected term to exercise of 5 years and 6.01 years.

Fair Value of Equity-Based Awards

A summary of the fair value of equity-based awards granted during the year ended September 30, 2005 and the seven months ended September 30, 2004 is set forth below:

	Year ended September 30, 2005			Seven months ended September 30, 2004		
	Number of Shares Granted	Weighted-Average Exercise Price	Weighted-Average Fair Value	Number of Shares Granted	Weighted-Average Exercise Price	Weighted-Average Fair Value
Service-Based Stock Options:						
At-market grants	1,372,988	$ 17.14	$ 6.92	398,315	$ 0.88	$ 0.41
Below-market grants	1,270,245	5.10	7.35	99,578	0.88	4.87
Performance-Based Stock Options:						
At-market grants—2x liquidity event	—	—	—	398,315	0.88	0.41
Below-market grants—2x liquidity event	1,270,245	5.10	7.35	99,578	0.88	4.87
At-market grants—3x liquidity event	—	—	—	398,315	0.88	0.41
Below-market grants—3x liquidity event	1,270,245	5.10	7.35	99,578	0.88	4.87
Total Stock Options	5,183,723	$ 8.29	$ 7.24	1,493,679	$ 0.88	$ 1.30
Restricted Stock Grants:						
Service-based awards	583,379	N/A	$ 10.28	796,701	N/A	$ 0.88
Performance-based 2x liquidity event awards	578,379	N/A	10.22	796,700	N/A	0.88
Performance-based 3x liquidity event awards	578,379	N/A	10.22	796,701	N/A	0.88
Total Restricted Stock Grants[a]	1,740,137	N/A	$ 10.24	2,390,102	N/A	$ 0.88

(a) Excludes 1,496,148 and 4,180,152 restricted shares of common stock of the Company, which were purchased in 2005 and 2004, respectively, by executives of the Company at prices at or below fair market value. The weighted-average purchase price and weighted-average fair value of such shares purchased in 2005 and 2004 were $1.04 and $0.88 per share, respectively and $9.38 and $1.60 per share, respectively.

Compensation Expense

For the year ended September 30, 2005, the Company recognized non-cash compensation expense of $25 million relating to its stock-based compensation plans.

For the seven months ended September 30, 2004, the Company recognized non-cash compensation expense of less than $1 million relating to its stock-based compensation plans.

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

Summary of Stock Option Activity

A summary of stock option activity is as follows:

	Options Outstanding	Weighted-Average Exercise Price
Balance at November 30, 2003	—	$ —
Granted	1,493,679	0.88
Exercised	—	—
Cancelled	—	—
Balance at September 30, 2004	1,493,679	$ 0.88
Granted	5,183,723	8.29
Exercised	—	—
Cancelled	(298,736)	0.88
Balance at September 30, 2005	6,378,666	$ 6.90

None of the stock options were exercisable as of September 30, 2004. The following table summarized information about stock options outstanding as of September 30, 2005:

Range of Exercise Prices	Number of Options Outstanding as of September 30, 2005	Weighted-Average Remaining Contractual Life (in years)	Weighted-Average Exercise Price	Number of Options Exercisable as of September 30, 2005	Weighted-Average Exercise Price
Under $5.00	3,696,374	8.90	2.90	398,315	2.90
$ 5.00 - $9.99	970,716	9.22	6.39	—	—
$10.00 - $14.99	338,588	9.51	10.46	—	—
$15.00 and above	1,372,988	9.69	17.14	—	—
	6,378,666	9.15	6.90	398,315	2.90

Payments Relating to Executive Compensation

The Company determined that certain shares of restricted stock issued in 2004 and early 2005 may have been sold at prices below fair market value on the applicable date of sale and certain options to purchase shares of the Company's stock granted may have had exercise prices below fair market value on the applicable date of grant. As a result, certain U.S. employee holders of the restricted stock who made elections under Section 83(b) of the Internal Revenue Code will be subject to additional ordinary income tax to the extent of the fair market value of the restricted stock received over the purchase price they paid for such stock. In other cases, certain employees who did not make such an election will be subject to higher taxes on their restricted shares at the time of vesting than would have been the case had they purchased the shares for fair market value. In addition, under the provisions of the American Jobs Creation Act of 2004, signed into law in October 22, 2004, U.S. employee option holders whose options vest with exercise prices below fair market value on the date of grant are subject to significant penalties under new Section 409A of the Internal Revenue Code. IRS Notice 2005-1 provides transitional guidance on the application of Section 409A which, among other things, permits options with exercise prices below the fair market value of the underlying stock on the date of grant to be amended or replaced with new options having an exercise price at least equal to the fair market value on the grant date. Non-U.S. employee holders of restricted stock or options may be subject to similar or other related issues. In order for the Company to address these issues the board, based on a re-assessment of fair market values on the applicable dates, approved the actions discussed below.

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Notes to Consolidated and Combined Audited Financial Statements—(Continued)

Restricted Stock

The Company is authorized to pay each employee who purchased restricted stock at prices that were below fair market value on the date of purchase a cash bonus. The cash bonus payable to those employees who made a Section 83(b) election is an amount equal to the tax liability incurred by the employee as of the date of purchase based on any difference between the re-determined purchase date fair market value and the amount originally paid by the employee, plus an amount necessary to pay the taxes on the bonus. The bonuses that are payable to each of those employees who did not make a Section 83(b) election or the applicable foreign equivalent is an amount reflecting an estimate of the additional tax which would be payable by the employee at the time the restricted stock is scheduled to vest due to that taxable amount being subject to ordinary income rather than capital gains tax rates, and assuming that the re-determined value of the stock remains constant over the vesting period, adjusted down to reflect a present value discount based on the earliest possible vesting dates. The Company will pay these employees an amount necessary to pay the taxes on the bonus. This resulted in total cash payments of approximately $10 million, which the Company has expensed in the year ended September 30, 2005.

Options

The Company has revised the exercise prices of certain options to purchase its common stock to prices equal to the applicable re-determined fair market values of the common stock on the dates of the respective grants. To compensate the grantees for the loss of value represented by this adjustment to the option exercise prices, the Company will pay each affected employee a cash bonus in an amount equal to the excess of the adjusted aggregate exercise price of the employee's options over the original aggregate exercise price of the employee's options, adjusted down to reflect a present value discount based on the earliest possible exercise dates. The Company has treated the revision of the exercise prices of certain option grants as a modification of such grants under the related guidance and as such, recorded additional expense of $6 million in the year ended September 30, 2005. The cash bonuses that were paid during 2005, or will be paid shortly thereafter, will total approximately $9 million.

Further, in connection with the cash dividends the Company declared and paid to holders of its common stock consisting of the Investor Group and certain members of management who held shares of common stock prior to the Initial Common Stock Offering, the Company has made an adjustment to all options outstanding at the time of declaration of the dividend. The adjustment consists of a cash make-whole payment consisting of an amount equal to the pro rata amount that would have been received per share had all outstanding options been exercised at the time of the declaration of the dividend adjusted down to reflect a present value discount based on the earliest possible exercise dates. The Company has recorded approximately $3 million of expense related to such payments in the year ended September 30, 2005.

Of the amounts related to restricted stock and options, all but $3 million has been paid as of September 30, 2005.

Pre-Acquisition

Prior to the closing of the Acquisition, employees of Old WMG were granted options to purchase Time Warner common stock under various Time Warner stock option plans. Such options were granted to employees of Old WMG with exercise prices equal to, or in excess of, fair market value at the date of grant. Accordingly, in accordance with APB 25 and related interpretations, compensation cost generally was not recognized by Time Warner, nor charged to Old WMG, related to such stock option plans. Generally, the options became exercisable over a four-year vesting period and expired ten years from the date of grant. See Note 3 for a summary of the impact on reported net income (loss) had Old WMG recognized compensation cost for employee stock options.

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Time Warner Black-Scholes Assumptions

For purposes of applying FAS 123, the fair value of each option grant was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for grants to Old WMG's employees in the three months ended February 29, 2004 and the years ended November 30, 2003: dividend yields of 0% in each period; expected volatility of 35.2% and 52.8%, respectively; risk-free interest rates of 3.1% and 2.6%, respectively; and expected terms to exercise of 1.4 years and 3.1 years, respectively.

Fair Value of Time Warner Equity-Based Awards

The weighted-average fair value of an option granted to the Company's employees was $3.20 and $4.33 for the three months ended February 29, 2004 and the year ended November 30, 2003, respectively.

Summary of Time Warner Stock Option Activity

A summary of Time Warner stock option activity with respect to employees of the Company is as follows:

	Time Warner Options Outstanding	Weighted-Average Exercise Price
Balance at November 30, 2002	29,716	33.72
Granted during 2003	6,341	11.72
Exercised during 2003	(196)	12.21
Cancelled/transferred during 2003(a)	(2,379)	23.79
Balance at November 30, 2003	33,482	30.39

(a) Includes all options cancelled and forfeited during the year, as well as options related to employees who have been transferred out of and into the Company to and from other Time Warner divisions.

Of the approximate 33 million Time Warner stock options held by employees of Old WMG as of the closing date of the Acquisition, approximately 27 million stock options remained outstanding and the balance was cancelled pursuant to the underlying terms of the awards. These stock options remain the obligation of Time Warner and not the Company, and will expire pursuant to the underlying terms of the awards, generally not exceeding three years from the closing date of the Acquisition. In exchange for the cancellation of certain unvested stock option awards as of the Acquisition date, employees of Old WMG received an aggregate $21 million payment funded by Time Warner. This payment was considered in the determination of the fair value of Old WMG's net assets as of November 30, 2003 and, accordingly, has been classified as a component of the impairment charge recognized during the year ended November 30, 2003.

Time Warner Restricted Stock Plans

Time Warner also had various restricted stock plans for employees and non-employee directors of the board. Under these plans, shares of common stock are granted which do not vest until the end of a restriction period, generally between three to five years. During 2003, Time Warner issued approximately 821,000 shares of restricted stock to employees of Old WMG at a weighted-average fair value of $13 per share.

Of the 922,000 unvested shares of Time Warner restricted stock held by employees of Old WMG as of the closing date of the Acquisition, 217,000 shares became vested either pursuant to their original terms or on an accelerated basis, 568,000 shares are still subject to vesting conditions and remain the obligation of Time Warner and the balance was cancelled by Time Warner. Old WMG recognized the cost associated with the vesting of such shares and the anticipated change in employee status of certain executives in 2003 as a component of deal-related transaction and other costs in its statement of operations.

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19. Shareholders' Equity

The Company's capital stock formerly consisted of two classes of common stock that were issued in connection with the Acquisition. In addition, as part of the purchase price for the Acquisition, the Company issued warrants that gave Time Warner the right, under certain conditions, to purchase up to 19.9% of the capital stock of the Company. A summary of the terms of these securities is presented below.

Common Stock

In connection with the Acquisition, the Company received (i) a $765 million capital contribution in exchange for the issuance of 9,445 shares of Class L Common Stock and (ii) an $85 million capital contribution in exchange for the issuance of 85,000 shares of Class A Common Stock.

Shares of Class L Common Stock had identical terms as the shares of Class A Common Stock, except with respect to voting rights, liquidation preferences and conversion features, as follows:

- Shares of Class L Common Stock were non-voting, whereas each share of Class A Common Stock is entitled to one vote;
- Each share of Class L Common Stock had a liquidation preference of $81,000 plus an amount equal to accrued and unpaid dividends at a rate of 10% per annum, compounded quarterly. Shares of Class A Common Stock have no liquidation preferences; and
- Each share of Class L Common Stock was convertible into one share of Class A Common Stock plus an additional number of shares of Class A Common Stock determined by dividing the Class L liquidation preference at the date of conversion by the adjusted market value of each share of Class A Common Stock as set forth in the certificate of designation governing such shares.

As more fully described in Note 2, in connection with the Initial Common Stock Offering, the Recapitalization occurred. In connection with the Recapitalization, all shares of Class L Common Stock were converted into shares of Class A Common Stock and, along with all other outstanding shares of Class A Common Stock, were renamed as common stock.

Warrants

A portion of the consideration paid to Time Warner in connection with the Acquisition was in the form of two stock warrants that were issued to Time Warner.

One of the warrants gave Time Warner the right, under certain conditions related to the occurrence of a major music transaction, to purchase approximately 19.9% of the Class A and Class L Common Stock of Parent and 19.9% of the preferred shares issued by Holdings, after taking into account the exercise of the warrant (the "MMT Warrants"). Time Warner could exercise its rights under the warrants only (i) upon the sale to certain music companies of all or substantially all of the recorded music business or music publishing business conducted by the Company or the acquisition by certain music companies of 35% of the outstanding shares of Parent or Holdings; (ii) the acquisition of all or substantially all of the recorded music business or music publishing business of certain music companies; or (iii) a merger with or the formation of a joint venture or other combination of all or substantially all of the recorded music business or music publishing business with that of certain music companies.

The other warrant gave Time Warner the right to purchase approximately 15% of the Class A and Class L Common Stock of Parent and 15% of the preferred shares issued by Holdings, after taking into account the

exercise of the warrant (the "Three-Year Warrants"). Time Warner could exercise its rights under the Three-Year Warrants at any time prior to March 1, 2007, provided that there had not been a public equity offering that results in the common and preferred securities of Parent or Holdings to be outstanding; there had not been a sale of a majority of the then-outstanding common and preferred securities of Parent or Holdings to a third party; or the exercise of the MMT Warrants. Any of those events would cause the term of the Three-Year Warrants to expire.

On May 16, 2005, in connection with the Company's Initial Common Stock Offering, the Company repurchased the Three-Year warrants from Time Warner for an aggregate purchase price of $138 million. The repurchase of the Three-Year warrants had the effect of terminating Time Warner's MMT warrants as of the date of repurchase. As a result, as of September 30, 2005, the warrants were no longer outstanding.

Returns of Capital and Dividends Paid

In September 2004, the Company declared a $342 million dividend to its Class L common stockholders in the form of a note payable. The note payable was paid in October 2004 using proceeds received from a return of capital previously invested in WMG Acquisition Corp.

In connection with the Holdings Refinancing, the Company paid a $472 million return of capital to its Class L common shareholders, of which $422 million was paid in December 2004, $42.5 million was paid in March 2005 and $7.5 million was paid in May 2005.

In connection with the Initial Common Stock Offering, the Company declared a dividend of $8.5 million related to the remaining liquidation preference of its Class L common stock, which was paid on May 16, 2005. The Company also declared a dividend of $100.5 million to its common stockholders immediately prior to the Initial Common Stock Offering, substantially all of which was paid on May 16, 2005. Of the total dividend amount, approximately $7 million related to holders of unvested shares of restricted stock. Of such amount, approximately $1 million was paid on May 16, 2005 and the remaining $6 million will be paid when, and if, such restricted shares vest.

On October 3, 2005, the Company declared a dividend on its outstanding common stock to its shareholders of record as of October 24, 2005. The dividend was paid November 23, 2005, at a rate of $0.13 per share, representing a dividend of approximately $19.3 million in the aggregate. The portion of the dividend with respect to unvested restricted stock of approximately $1 million will be paid at such time as such shares become vested.

20. Related Party Transactions

The nature of the Company's related party transactions has changed as the Company has migrated from a wholly owned operation of Time Warner for all periods prior to the closing of the Acquisition to a stand-alone independent company, effective as of March 1, 2004. Accordingly, the following discussion of related party transactions highlights the significant related party relationships and transactions that existed both before and after the closing of the Acquisition.

Post-Acquisition

Transition Services Agreements

In connection with the Acquisition, the Company entered into a seller administrative services agreement with Time Warner (the "Seller Administrative Services Agreement"). Under the Seller Administrative Services Agreement, Time Warner agreed to provide the Company with certain administrative services, including (i) accounting services, (ii) tax services, (iii) human resources and benefits services, (iv) information technology

services, (v) legal services, (vi) treasury services, (vii) payroll services, (viii) travel services, (ix) real estate management services and (x) messenger services. The obligations for Time Warner to provide those services generally expired on December 31, 2004. The amounts to be paid under the Seller Administrative Services Agreement generally were based on the costs incurred by Time Warner in providing those administrative services, including Time Warner's employee costs and out-of-pocket expenses. For each of the twelve months ended September 30, 2005, and the seven months ended September 30, 2004, the Company incurred $4 million of costs under these administrative arrangements.

Management/Monitoring Agreement

In connection with the Acquisition, the Company entered into a management agreement with the Investor Group for ongoing consulting and management advisory services. Pursuant to this agreement, the Company paid an aggregate of $75 million to the Investor Group under the management agreement in connection with the Acquisition and related original financing. These fees were apportioned between direct costs of the Acquisition (and capitalized as part of the allocation of purchase price) and capitalized debt issuance costs. In consideration for ongoing consulting and management advisory services, the management agreement required the Company to pay (or to cause Holdings or Acquisition Corp. to pay) the Investor Group an aggregate annual fee of $10 million per year ("Periodic Fees"), which was payable quarterly in advance. For both the year ended September 30, 2005 and the seven months ended September 30, 2004, the Company recorded expense of $6 million related to this fee, and such amount has been included as a component of selling, general and administrative expenses in the accompanying statement of operations.

In addition, in the case of future services provided in connection with any future acquisition, disposition, or financing transactions involving Acquisition Corp., the Company or Holdings, the management agreement required the Company to pay (or to cause Holdings or Acquisition Corp. to pay) the Investor Group an aggregate fee of one percent of the gross transaction value of each such transaction ("Subsequent Fees"). The agreement also required Acquisition Corp., Warner Music Group and Holdings to pay the reasonable expenses of the Investor Group in connection with, and indemnify them for liabilities arising from, the management agreement, the Acquisition and any related transactions, their equity investment in Acquisition Corp., Warner Music Group or Holdings, their operations, and the services they provide to Acquisition Corp., Warner Music Group and Holdings.

The management agreement provided that it would continue in full force and effect until December 30, 2014, provided, however, that the Investor Group may cause the agreement to terminate at any time upon agreement of the Investor Group. In the event of the termination of the management agreement, the Company, Holdings and Acquisition Corp. shall pay each of the Investor Group (x) any unpaid portion of the Periodic Fees, any Subsequent Fees and any expenses due with respect to periods prior to the date of termination plus (y) the net present value (using a discount rate equal to the then yield on U.S. Treasury Securities of like maturity) of the Periodic Fees that would have been payable with respect to the period from the date of termination until December 30, 2014.

On May 10, 2005, the Investor Group terminated the Management Agreement, and on May 16, 2005, the Company paid the Investor Group a $73 million termination fee for the termination of the Management Agreement, which was reflected in the Company's statement of operations for the year ended September 30, 2005.

Other Arrangements with the Investor Group and its Affiliates

In the normal course of conducting its business, the Company entered into various other transactions with the Investor Group and its affiliates. As an example, employees of the Investor Group filled management roles on

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an interim basis while the Company was transitioning to a permanent management team, including the role of Chief Financial Officer of the Company from June 2004 until December 2004. Such employees did not receive any compensation from the Company for such services; however, a representative cost for such services in the aggregate amount of $280,000 was charged to the statement of operations for the seven months ended September 30, 2004 with a corresponding increase in additional paid-in capital.

Pre-Acquisition

As previously described, the operations of Old WMG were under the control of Time Warner through the end of February 2004. During this period, in the normal course of conducting its business, Old WMG had various transactions with Time Warner and its affiliates, including the CD and DVD manufacturing and printing operations of Time Warner formerly under the management of Old WMG. The following is a summary of the principal transactions between Old WMG on the one hand, and Time Warner and its affiliates on the other hand.

Manufacturing and Printing Services with Time Warner Affiliates

Old WMG had an exclusive arrangement with affiliates of Time Warner to receive manufacturing and printing services in connection with the production of CDs, cassettes and other music-related audio and video products. Amounts included in cost of sales in connection with these services were approximately $216 million for the year ended November 30, 2003. Such costs did not reflect terms negotiated on an arm's-length basis between the units. In connection with the sale of Time Warner's manufacturing and printing operations in October 2003, such services were provided on an arm's-length basis by Cinram, effective with the closing date of the sale (see Note 6).

Distribution Services with Time Warner and Old WMG Affiliates

Old WMG provided distribution services to certain Time Warner affiliates, including Warner Home Video and Time-Life Inc. In addition, Old WMG provided distribution services to other related parties, including companies in which Old WMG had ownership interests therein that allowed for the exercise of significant influence over the operations and financial policies of the investees. Amounts included in revenues in connection with these services were approximately $51 million for the year ended November 30, 2003. Such revenues may not have reflected terms negotiated on an arm's-length basis between the entities. In connection with the sale of Time Warner's manufacturing and printing operations in October 2003, the services for Warner Home Video were provided by Cinram, effective with the closing date of the sale (see Note 6).

Licensing Arrangements with Time Warner and Old WMG Affiliates

Old WMG periodically licensed its masters and rights in owned or administered musical compositions to affiliates of Time Warner for inclusion in certain movie soundtracks, film and television series, music compilations and other forms of entertainment. Amounts included in revenues in connection with these and other licensing arrangements were approximately $2 million for the three months ended February 29, 2004 and $6 million for the year ended November 30, 2003. Such revenues reflect terms resulting from a negotiation between the units that, in management's view, result in a reasonable basis.

Old WMG also entered into sub-publishing or administrative agreements with certain Time Warner affiliates, whereby it exploited or administered rights in musical compositions held by such affiliates. Royalty expenses included in cost of revenues in connection with these arrangements were approximately $2 million for

the three months ended February 29, 2004 and $19 million for the year ended November 30, 2003. Such amounts reflect terms resulting from a negotiation between the units that, in management's view, result in a reasonable basis.

Real Estate and Marketing Arrangements with Time Warner Affiliates

Old WMG utilized and paid for certain office space leased by Time Warner and its affiliates. In addition, Old WMG periodically advertised its products in media produced by Time Warner and its affiliates. Amounts included in costs and expenses in connection with these arrangements were approximately $2 million for the three months ended February 29, 2004 and $26 million for the year ended November 30, 2003. Such amounts reflect terms resulting from a negotiation between the units that, in management's view, result in a reasonable basis.

Financing Arrangements with Time Warner Affiliates

As described in Note 3, Old WMG had agreements with Time Warner, whereby all cash received or paid by Old WMG was included in, or funded by, clearing accounts or international cash pools within Time Warner's centralized cash management system. Some of these arrangements were interest bearing and others were not. Net interest income of approximately $1 million for three months ended February 29, 2004 and $10.8 million for the year ended November 30, 2003 were recognized from Time Warner and its affiliates or other related parties.

In addition, Old WMG participated in Time Warner's foreign currency risk-management program and was allocated its proportional share of foreign exchange contract gains and losses. Net foreign exchange contract losses were immaterial for the three months ended February 29, 2004 and $17 million for the year ended November 30, 2003 and were recognized and are classified in other income (expense), net, in the accompanying statement of operations.

See Note 24 for a description of the Company's participation in Time Warner's accounts receivable securitization program.

Other Costs with Time Warner Affiliates

Employees of Old WMG participated in several Time Warner medical, stock option, pension, deferred compensation and other benefit plans for which Old WMG was charged an allocable share of plan expenses, including administrative costs. The Company also was covered under various Time Warner insurance policies and was charged an allocable share of such costs. Amounts included in expenses in connection with these and other sundry costs, such as communications networking costs, were approximately $8 million for the three months ended February 29, 2004 and $62 million for the year ended November 30, 2003.

Affiliated Management Services

Through February 2004, Old WMG had general management responsibility over substantially all of Time Warner's music operations, including Time Warner's CD and DVD manufacturing and printing operations. Accordingly, certain general and administrative costs incurred in the management of those operations were allocated to Old WMG, including legal, accounting, financial and information technology services. As described previously in Note 2, the allocation of these costs was determined based on Old WMG's pro rata share of the revenues generated by those collective operations. The costs allocated to Old WMG are not necessarily indicative of the costs that would have been incurred if Old WMG had obtained such services independently, nor are they

indicative of costs that will be charged or incurred in the future. However, management believes such allocations are reasonable. Amounts included in expenses in connection with these affiliated management service costs were approximately $2 million for the three months ended February 29, 2004 and $79 million for the year ended November 30, 2003. Such amounts exclude approximately $47 million of costs for the year ended November 30, 2003 that have been separately allocated to Time Warner's former CD and DVD manufacturing and printing operations for comparable management services.

21. Commitments and Contingencies

Leases

The Company occupies various facilities and uses certain equipment under many operating leases. Net rent expense was approximately $37 million in the year ended September 30, 2005, $24 million in the seven months ended September 30, 2004, $13 million in the three months ended February 29, 2004, and $53 million in the year ended November 30, 2003.

At September 30, 2005, future minimum payments under non-cancelable operating leases (net of sublease income) are as follows:

	September 30, 2005
	(in millions)
2006	$ 34
2007	38
2008	34
2009	32
2010	27
Thereafter	198
Total	$ 363

Guaranteed Minimum Talent Advances

The Company routinely enters into long-term commitments with artists, songwriters and co-publishers for the future delivery of music product. Aggregate firm commitments to such talent approximated $369 million and $345 million as of September 30, 2005 and 2004, respectively. Such commitments are payable principally over a ten-year period, generally upon delivery of albums from the artists or future musical compositions by songwriters and co-publishers.

Other

Other off-balance sheet, firm commitments, which include letters of credit and minimum funding commitments to investees, amounted to approximately $50 million and $65 million at September 30, 2005 and 2004, respectively.

Litigation

The Company was subject to a number of state and federal class action lawsuits, as well as an action brought by a number of state Attorneys General alleging unlawful horizontal and vertical agreements to fix the

prices of compact discs by the major record companies. The parties to the federal action commenced by the Attorneys General have entered into a settlement agreement related to all but two of the related lawsuits. On July 9, 2003, the Court entered a final judgment approving the settlement. In one of the two lawsuits remaining after the settlement, *Ottinger v. EMI Music, Inc., et al.*, the Court entered an order granting final approval of the settlement on January 21, 2004. In the other action, *In re Compact Disc Antitrust Litig.*, which was brought by individual retailers of compact discs alleging unlawful horizontal agreements to fix the prices of compact discs by the major record companies, on July 29, 2004, the Court denied the parties' motion to grant final approval to the settlement. On August 30, 2004, plaintiffs filed a Second Amended Consolidated Complaint adding additional individual retailers as named plaintiffs in the litigation, which the Company answered, denying all claims, on September 15, 2004. On October 29, 2004, the parties reached an agreement on the terms of a settlement. On February 2, 2005, the Court entered a Stipulation of Dismissal with Prejudice of the entire action. In connection with the aforementioned settlements, Old WMG paid approximately $30 million in cash and product costs in the aggregate during 2001 and 2002. Such amounts did not affect the statement of operations as the settlements were charged against a pre-existing liability relating to these matters.

On September 7, 2004, November 22, 2004 and March 31, 2005, Eliot Spitzer, the Attorney General of the State of New York, served Warner Music Group with requests for information in the form of subpoenas duces tecum in connection with an industry-wide investigation of the relationship between music companies and radio stations, including the use of independent promoters and accounting for any such payments. The investigation was pursuant to New York Executive Law §63(12) and New York General Business Law §349, both of which are consumer fraud statutes. On November 22, 2005 the Company reached a settlement with the Attorney General in connection with this investigation. As part of such settlement, the Company agreed to make $5 million in charitable payments and to abide by a list of permissible and impermissible promotional activities.

In addition to the matters discussed above, the Company is involved with employment claims and other legal proceedings that are incidental to its normal business activities. It is reasonably possible that an adverse outcome on any of these matters could result in a material effect on the Company's consolidated financial statements. Due to the preliminary status of many of these matters, the Company is unable to predict the outcome or determine a range of loss at this time. However, in the opinion of management, it is not likely that the ultimate outcome of these matters will have a material effect on the Company's consolidated financial statements.

22. Derivative Financial Instruments

The Company has exposure to changes in foreign currency exchange rates relating to the cash flows generated by its international operations and exposure to changes in interest rates relating to floating-rate borrowings under its senior secured credit facility. Consequently, the Company uses derivative financial instruments to manage such risks. The following is a summary of the Company's risk management strategies and the effect of those strategies on the Company's financial statements.

Interest Rate Risk Management

The Company uses interest rate swap agreements to manage the floating to fixed-rate proportion of its debt portfolio. In particular, under its senior secured credit facility, the Company is required to maintain a fixed-to-floating debt ratio of at least 50% of its actual funded debt through at least April 2007. The Company enters into interest rate swap agreements in order to hedge the variability of expected future cash interest payments. Under interest rate swap agreements, the Company agrees to receive floating-rate payments (based on

three-month LIBOR rates) in exchange for fixed-rate payments for a fixed term of three years through May 2007. As of September 30, 2005, the Company had total notional amounts hedged under these agreements of $897 million.

The interest rate swap agreements have been designated as a cash flow hedge of the associated variability in future interest payments. As such, the agreements have been recorded at fair value in the accompanying balance sheet and the related gains or losses on the agreements are deferred in shareholder's equity (as a component of comprehensive income). These deferred gains and losses are recognized as an adjustment to interest expense in the period in which the related interest payments being hedged are made 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 amount of the interest payments being hedged, any changes in fair value relating to the ineffective portion of these contracts are immediately recognized in income.

For the year ended September 30, 2005 and the seven months ended September 30, 2004, the Company recognized approximately $4 million and $2 million, respectively, of expense on its interest rate swap agreements, which have been classified as a component of interest expense in the accompanying statement of operations. The Company did not recognize any material gains or losses during the period relating to the ineffective portion of the agreements. At September 30, 2005 the Company had deferred approximately $7 million of gains on its interest rate swap agreements in shareholders' equity, of which approximately $5 million is expected to be recognized to income over the next year.

The Company monitors its positions with, and the credit quality of, the financial institutions that are party to any of its financial transactions. Credit risk related to interest rate swaps is considered low because swaps are entered into with strong creditworthy counterparties and are limited to the net interest payments due/payable for the remaining life of the swap.

Foreign Currency Risk Management

Historically, the Company has used (and continues to use) foreign 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. In addition, the Company currently hedges foreign currency risk associated with financing transactions such as third party and inter-company debt and other balance sheet items.

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 and Australian dollar. Additionally, prior to the closing of the Acquisition, Old WMG and Time Warner used foreign exchange contracts to manage this risk, primarily the exposure to changes in the value of the British pound sterling, Japanese yen and euros. In connection with the anticipated closing of the Acquisition, all positions were unwound as of the end of December 2003. In connection with the discontinuance of such cash flow hedges, Old WMG recognized approximately $5 million of losses during the fourth quarter of 2003.

For royalty related hedges, the Company records foreign exchange contracts at fair value on its balance sheet and the related gains or losses on these contracts are deferred in shareholder's equity (as a component of comprehensive income). 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 income. For hedges of financing transactions and other balance sheet

items, hedge gains and losses are taken directly to the statement of operations since there is an equal and offsetting statement of operations entry related to the underlying exposure. Excluding the aforementioned losses on the discontinuance of cash flow hedges, Old WMG recognized a $694,000 gain in 2003 due to the ineffective portion of certain foreign exchange contracts. Gains and losses on foreign exchange contracts generally are included as a component of other income (expense), net, in the Company's statement of operations.

As of September 30, 2005, the Company had outstanding hedge contracts for the sale of $472 million and the purchase of $248 million of foreign currencies at fixed rates. Further, as of September 30, 2005, the Company had approximately $1.5 million of deferred net gains in comprehensive income related to foreign exchange hedging. The Company had no significant deferred net gains or losses on foreign exchange contracts at September 30, 2004. For the year ended November 30, 2003, Old WMG recognized $12 million in losses on foreign exchange contracts, which were largely offset by corresponding decreases and increases, respectively, in the dollar value of foreign currency royalty payments that have been received in cash from the sale of U.S.-copyrighted products abroad.

Warrants

The Company recorded unrealized gains related to the warrants issued to Historic TW as part of the purchase price of the Acquisition of $17 million for the year ended September 30, 2005. On May 16, 2005, the Company repurchased the Three-Year warrants from Historic TW at a cost of approximately $138 million, which approximated fair value at that date (see Note 19).

23. 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 areas: recorded music and music publishing. 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, non-cash amortization of intangible assets and non-cash impairment charges to reduce the carrying value of goodwill and 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 or combination and, therefore, do not themselves impact consolidated or combined results.

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements—(Continued)

During 2004, in connection with the Acquisition, the Company changed its methodology for allocating certain corporate costs and assets to its business segments. Accordingly, the Company has restated its operating performance and asset measures for all prior periods to reflect its new cost-allocation methodology on a consistent basis.

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, [illegible]	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
Revenues					
Recorded music	$ 2,924	$ 1,429	$ 630	$ 2,039	$ 2,839
Music publishing	607	348	157	467	563
Intersegment elimination	(29)	(8)	(8)	(19)	(26)
Total revenues	$ 3,502	$ 1,769	$ 779	$ 2,487	$ 3,376

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, [illegible]	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
OIBDA[a]					
Recorded music	$ 380	$ 120	$ 38	$ 8	$ 116
Music publishing	141	87	38	88	107
Corporate expenses[b]	(199)	(49)	(15)	(21)	(34)
Total OIBDA	$ 322	$ 158	$ 61	$ 75	$ 189

(a) The comparability of OIBDA by business segment for all periods presented has been affected by certain significant transactions. See *Transactions Affecting the Comparability of Operating Results* presented hereinafter.

(b) Corporate expenses for 2003 were reduced by an allocation of costs to Time Warner's former CD and DVD manufacturing operations that were managed by Old WMG. Such operations were sold by Time Warner in October 2003, and accordingly, no such cost allocations were made for the 2004 periods. See Note 20 for further reference.

	Successor		Predecessor		
	Year Ended September 30, [illegible]	Seven Months Ended September 30, 2004	Three Months Ended February [illegible]	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
Depreciation of Property, Plant and Equipment					
Recorded music	$ 32	$ 23	$ 11	$ 51	$ 62
Music publishing	5	3	1	6	7
Corporate	14	10	4	14	17
Total depreciation	$ 51	$ 36	$ 16	$ 71	$ 86

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements—(Continued)

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
Amortization of Intangible Assets					
Recorded music	$ 133	$ 73	$ 36	$ 138	$ 165
Music publishing	54	31	20	63	77
Corporate	—	—	—	—	—
Total amortization	$ 187	$ 104	$ 56	$ 201	$ 242

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
Impairment of Goodwill and Other Intangibles					
Recorded music	$ —	$ —	$ —	$ —	$ 1,019
Music publishing	—	—	—	—	—
Corporate	—	—	—	—	—
Total impairment	$ —	$ —	$ —	$ —	$ 1,019

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
Operating Income (Loss)[a]					
Recorded music	$ 215	$ 24	$ (9)	$ (181)	$ (1,130)
Music publishing	82	53	17	19	23
Corporate	(213)	(59)	(19)	(35)	(51)
Total operating income (loss)	$ 84	$ 18	$ (11)	$ (197)	$ (1,158)

(a) The comparability of operating income (loss) by business segment for all periods presented has been affected by certain significant transactions. See *Transactions Affecting the Comparability of Operating Results* presented hereinafter.

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements—(Continued)

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29, 2004	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
Reconciliation of OIBDA to Operating Income (Loss)					
OIBDA	$ 322	$ 158	$ 61	$ 75	$ 189
Depreciation expense	(51)	(36)	(16)	(71)	(86)
Amortization expense	(187)	(104)	(56)	(201)	(242)
Impairment of goodwill and other intangible assets	—	—	—	—	(1,019)
Operating income (loss)	$ 84	$ 18	$ (11)	$ (197)	$ (1,158)

Transactions Affecting the Comparability of Operating Results

The comparability of OIBDA and operating income (loss) by business segment for all periods presented has been affected by certain transactions, consisting of a management agreement termination fee in the year ended September 30, 2005, restructuring activities in all periods, the sale of Old WMG's physical distribution assets in 2003, and significant impairment charges in 2003 relating to Old WMG's intangible assets. The effect of such transactions that was included in OIBDA and operating income (loss) by business segment is summarized below:

	Fiscal Year Ended September 30, 2005			
	Recorded Music	Music Publishing	Corporate	Total
		(in millions)		
Loss on termination of management agreement	$ —	$ —	$ (73)	$ (73)
Restructuring costs	(7)	—	—	(7)
Decrease in OIBDA and operating income	$ (7)	$ —	$ (73)	$ (80)

	Seven Months Ended September 30, 2004			
	Recorded Music	Music Publishing	Corporate	Total
		(in millions)		
Restructuring costs-related decrease in OIBDA and operating income	$ (17)	$ (1)	$ (8)	$ (26)

	Ten Months Ended September 30, 2003			
	Recorded Music	Music Publishing	Corporate	Total
		(Unaudited) (in millions)		
Restructuring costs	$ (24)	$ (3)	$ —	$ (27)
Loss on sale of physical distribution assets	(12)	—	—	(12)
Decrease in OIBDA and operating income	$ (36)	$ (3)	$ —	$ (39)

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements—(Continued)

	Year Ended November 30, 2003			
	Recorded Music	Music Publishing	Corporate	Total
	(in millions)			
Restructuring costs	$ (31)	$ (3)	$ (1)	$ (35)
Loss on sale of physical distribution assets	(12)	—	—	(12)
Decrease in OIBDA	(43)	(3)	(1)	(47)
Impairment of goodwill and other intangible assets	(1,019)	—	—	(1,019)
Decrease in operating income	$ (1,062)	$ (3)	$ (1)	$ (1,066)

Total assets and capital expenditures by business segment are presented below:

	September 30, 2005	September 30, 2004
	(in millions)	
Assets		
Recorded music	$ 2,517	$ 2,649
Music publishing	1,645	1,754
Corporate[a]	336	687
Total assets	$ 4,498	$ 5,090

(a) Primarily includes deferred tax assets and fixed assets.

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29,	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
Capital Expenditures:					
Recorded music	$ 22	$ 11	$ 2	$ 14	$ 29
Music publishing	2	1	—	3	3
Corporate	6	3	1	13	19
Total capital expenditures	$ 30	$ 15	$ 3	$ 30	$ 51

Revenues and total assets relating to operations in different geographical areas are set forth below:

	Successor		Predecessor		
	Year Ended September 30, 2005	Seven Months Ended September 30, 2004	Three Months Ended February 29	Ten Months Ended September 30, 2003	Year Ended November 30, 2003
			(in millions)		
Revenues[a]					
United States	$ 1,675	$ 848	$ 334	$ 1,211	$ 1,505
United Kingdom	387	221	111	287	407
Germany	215	124	43	158	210
Japan	170	105	41	144	202
France	241	112	55	154	217

Italy	121	56	37	185	108
Other international	693	303	158	448	727
Total revenues	$ 3,502	$ 1,769	$ 779	$ 2,487	$ 3,376

(a) Revenues are attributed to countries based on the location of customer.

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements—(Continued)

	September 30, 2005	September 30, 2004
	(in millions)	
Assets		
United States	$ 2,597	$ 3,164
United Kingdom	396	512
Germany	210	269
Japan	192	252
France	225	280
Italy	190	98
Other international	688	515
Total assets	$ 4,498	$ 5,090

24. Additional Financial Information

Time Warner Accounts Receivable Securitization Facility

Prior to the Acquisition, Old WMG, through its WEA Corp. subsidiary, participated in one of Time Warner's accounts receivable securitization facilities. Such facility provided for the accelerated receipt of approximately $450 million of cash, in the aggregate, on available accounts receivable. In connection with this securitization facility, Old WMG sold, on a revolving and nonrecourse basis, certain of its accounts receivable ("Pooled Receivables") to a qualifying Special Purpose Entity ("SPE") which, in turn, sold a percentage ownership interest in the Pooled Receivables to third-party commercial paper conduits sponsored by a financial institution. The receivables were sold to the SPE at net realizable value, after any loss due to uncollectibility was recorded by Old WMG. These securitization transactions were accounted for as a sale in accordance with FASB Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities," because Old WMG relinquished control of the receivables.

When the receivables were sold to the SPE, Old WMG recorded a retained beneficial interest in the SPE and an intercompany receivable from Time Warner representing the cash portion of the proceeds received by Time Warner on the sale for which there was no obligation to repay. The retained beneficial interest, which was adjusted to reflect the portion of receivables that was not expected to be collectible, accrued interest at a rate that varied with prevailing market interest rates. For this reason, and because the accounts receivables underlying the retained ownership interests that were sold to the qualifying SPE were generally short-term in nature, the fair value of the retained beneficial interest approximated its carrying value at November 30, 2003. The cost of the retained interest, offset in part by the related interest income earned on the retained interest, was borne by Time Warner. In December 2003, in anticipation of the closing of the sale of Old WMG that occurred effective as of March 1, 2004, Old WMG's participation in Time Warner's securitization facility ceased. Accordingly, the receivables sold to the SPE were re-purchased by Time Warner and transferred to Old WMG in satisfaction of the retained interest and intercompany receivable.

Cash Interest and Taxes

The Company made interest payments of approximately $151 million during the year ended September 30, 2005, $56 million during the seven months ended September 30, 2004 and $3 million during the three months ended February 29, 2004. The Company paid approximately $51 million, $31 million and $27 million of foreign income and withholding taxes in the year ended September 30, 2005, the seven months ended September 30, 2004 and the three months ended February 29, 2004, respectively. The Company received $6 million, $2 million and $1 million of foreign income tax refunds in the year ended September 30, 2005, the seven months ended September 30, 2004 and the three months ended February 29, 2004, respectively.

Warner Music Group Corp.

Notes to Consolidated and Combined Audited Financial Statements—(Continued)

Old WMG made interest payments of approximately $10 million during 2003. Old WMG paid approximately $80 million of foreign income and withholding taxes and received approximately $8 million of foreign income tax refunds in the year ended November 30, 2003. Old WMG did not reimburse Time Warner and its affiliated companies for any payments of federal, state and local income taxes made during the year ended November 30, 2003.

Non-cash Transactions

There were no significant non-cash activities for the year ended September 30, 2005.

Significant non-cash investing activities for the seven months ended September 30, 2004 included the allocation of the purchase price paid in connection with the Acquisition, as more fully described in Note 5. In addition, significant non-cash financing activities for the seven months ended September 30, 2004 included the declaration of a $342 million dividend to the Company's shareholders in the form of a note payable, as more fully described in Note 14.

Significant non-cash investing and financing activities during the three months ended February 29, 2004 included the non-cash recapitalization of certain inter-company receivables and payables between Old WMG and Time Warner, as disclosed in the statement of shareholders' and group equity. There were no significant non-cash investing and financing activities during the year ended November 30, 2003.

25. Subsequent Events

On October 3, 2005, the Company declared a dividend on its outstanding common stock as of October 24, 2005. The dividend was paid on November 23, 2005, at a rate of $0.13 per share, representing a dividend of approximately $19.3 million in the aggregate. The portion of the dividend with respect to unvested restricted stock of approximately $1 million will be paid at such time as such shares become vested.

On November 22, 2005 the Company reached a settlement with the Attorney General in connection with an investigation. As part of such settlement, the Company agreed to make $5 million in charitable payments and to abide by a list of permissible and impermissible promotional activities. Refer to Note 21.

WARNER MUSIC GROUP

2005 QUARTERLY FINANCIAL INFORMATION
(unaudited)

The following table sets forth the quarterly information for Warner Music Group (in millions, except per share data).

	Three months ended			
	September 30, 2005(a)	June 30, 2005(a)	March 31, 2005(a)	December 31, 2004(a)
Revenues	$ 905	$ 742	$ 767	$ 1,088
Costs and expenses				
Cost of revenues	(473)	(396)	(400)	(581)
Selling, general and administrative expenses[b][c]	(359)	(318)	(293)	(331)
Amortization of intangible assets	(47)	(47)	(47)	(46)
Loss on termination of management agreement	—	(73)	—	—
Restructuring Costs	(7)	—	—	—
Total costs and expenses	(886)	(834)	(740)	(958)
Operating (loss) income	19	(92)	27	130
Interest expense, net	(42)	(50)	(52)	(38)
Net investment related gains	—	1	—	—
Equity in the gains of equity-method investees	—	—	—	(1)
Loss on repayment of Holdings Notes	—	(35)	—	—
Unrealized gain (loss) on warrants	—	—	39	(22)
Minority interest expense	—	—	—	(5)
Other income (expense), net	2	1	—	4
Loss before income taxes	$ (21)	(175)	14	68
Income tax expense	(9)	(4)	(10)	(32)
Net loss	$ (30)	$ (179)	$ 4	$ 36
Net income (loss) per common share				
Basic	$ (0.21)	$ (1.41)	$ 0.04	$ 0.33
Diluted	$ (0.21)	$ (1.41)	$ 0.03	$ 0.31
Average common shares:				
Basic	141.2	127.0	107.7	107.5
Diluted	150.2	127.0	123.5	115.3

(a) The Company's business is seasonal. Therefore quarterly operating results are not necessarily indicative of the results that may be expected for the full fiscal year.

(b) The three months ended June 30, 2005 include one-time compensation expense consisting of a $10 million one-time bonus to employees related to the Company's Initial Common Stock Offering and $19 million of one-time payments to holder of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date.

(c) The three months ended September 30, 2005 include certain non-recurring charges of $24 million incurred in connection with the departure of the co-chairman of The Atlantic Records Group and the expensing of certain amounts paid in connection with the acquisition of the remaining interest in the Lava Records joint venture.

WARNER MUSIC GROUP

2004 QUARTERLY FINANCIAL INFORMATION
(unaudited)

	Successor		Combined	Successor	Predecessor	
	For the three months ended			For the one month ended	For the two months ended	For the three months ended
	September 30, 2004(a)	June 30, 2004(a)	March 31, 2004(a)	March 31, 2004(a)	February 29, 2004(a)	December 31, 2003(a)
Revenues	$ 798	$ 726	$ 735	$ 245	$ 490	$ 1178
Costs and expenses						
Cost of revenues	(421)	(393)	(388)	(130)	(258)	(648)
Selling, general and administrative expenses	(304)	(276)	(316)	(97)	(219)	(391)
Impairment of goodwill and other intangible assets	—	—	—	—	—	(1,019)
Amortization of intangible assets	(44)	(45)	(52)	(15)	(37)	(60)
Restructuring Costs	(26)	—	—	—	—	(8)
Total costs and expenses	$ (795)	(714)	(756)	(242)	(514)	(2,126)
Operating (loss) income	$ 3	$ 12	$ (21)	$ 3	$ (24)	$ (948)
Interest expense, net	$ (35)	(35)	(9)	(10)	1	(3)
Net investment related gains	—	—	—	—	—	(9)
Equity in the gains of equity-method investees	(2)	1	(3)	(1)	(2)	(9)
Deal-related transaction and other costs	—	—	—	—	—	(63)
Loss on repayment of bridge loan	—	(6)	—	—	—	—
Unrealized gain (loss) on warrants	(73)	(47)	—	—	—	—
Minority interest expense	(5)	(6)	(3)	(3)	—	—
Other income (expense), net	(4)	—	—	—	—	(7)
Income (loss) before income taxes	$ (116)	(81)	(36)	(11)	(25)	(1,039)
Income tax benefit (expense)	(21)	(10)	(12)	1	(13)	(107)
Net income (loss)	$ (137)	$ (91)	$ (48)	$ (10)	$ (38)	$ (1,146)
Net income (loss) per common share Basic	$ (1.27)	$ (0.85)				
Diluted	$ (1.27)	$ (0.85)				
Average common shares						
Basic	107.5	107.5				
Diluted	107.5	107.5				

(a) The Company's business is seasonal. Therefore, quarterly operating results are not necessarily indicative of the results that may be expected for the full fiscal year.

WARNER MUSIC GROUP CORP.

Supplementary Information
Condensed Consolidating Financial Statements

Warner Music Group Corp. (the "Company" or "Parent") was formed by a private equity consortium of Investors (the "Investor Group") on November 21, 2003. The Company is the direct parent of WMG Holdings Corp. ("Holdings"), which is the direct parent of WMG Acquisition Corp. ("New WMG" or "Acquisition Corp."). New WMG is the successor to substantially all of the interests of the recorded music and music publishing businesses of Time Warner Inc. ("Time Warner"). Such predecessor interests formerly owned by Time Warner are hereinafter referred to as "Old WMG" or the "Predecessor". Effective March 1, 2004, Old WMG was acquired from Time Warner by a private consortium of investors for approximately $2.6 billion.

Holdings issued (i) $250 million principal amount of Floating Rate Senior Notes due 2011 (the "Holdings Floating Rate Notes"), (ii) $397 million principal amount at maturity of 9.5% Senior Discount Notes due 2014, which had an initial issuance discount of $147 million (the "Holdings Discount Notes") and (iii) $200 million principal amount of Floating Rate Senior PIK Notes due 2014 (the "Holdings PIK Notes," and collectively, the "Holdings Notes"), which had an initial discount of $4 million. In June 2005, using proceeds from the Company's Initial Common Stock Offering and approximately $57 million of cash on hand, Holdings redeemed all of the Holdings Floating Rate Notes, all of the Holdings PIK Notes and 35% of the aggregate outstanding principal of the Holdings Discount Notes. The remaining Holdings Discount Notes are guaranteed by the Company. These guarantees are full, unconditional, joint and several. The following condensed consolidating financial statements are presented for the information of the holders of the remaining Holdings Discount Notes and present the results of operations, financial position and cash flows of (i) the Company, which is the guarantor of the remaining Holdings Discount Notes, (ii) Holdings, which is the issuer of the remaining Holdings Discount Notes, (ii) the subsidiaries of Holdings and (iii) the eliminations necessary to arrive at the information for the Company on a consolidated or on a combined basis. Investments in consolidated or combined subsidiaries are presented under the equity method of accounting.

The Company is a holding company with no independent operations or assets other than through its interests in its subsidiaries, such as Holdings and Acquisition Corp. Accordingly, the ability of the Company to obtain funds from its subsidiaries is restricted by the senior secured credit facility of Acquisition Corp., the indenture for the Subordinated Notes issued by Acquisition Corp., and the indenture for the Holdings Notes.

Consolidating Balance Sheet
September 30, 2005

	Warner Music Group Corp.	WMG Holdings Corp. (issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(in millions)		
Assets:					
Current assets:					
Cash and equivalents	$ 40	$ 1	$ 247	$ —	$ 288
Accounts receivable, net	15	(23)	645	—	637
Inventories	—	—	52	—	52
Royalty advances expected to be recouped within one year	—	—	190	—	190
Deferred tax assets	—	—	36	—	36
Other current assets	—	—	39	—	39
Total current assets	55	(22)	1,209	—	1,242
Royalty advances expected to be recouped after one year	—	—	190	—	190
Investments in and advances to (from) consolidated subsidiaries	43	235	—	(278)	21
Investments	—	—	21	—	—
Property, plant and equipment	—	—	157	—	157
Goodwill	—	—	869	—	869
Intangible assets subject to amortization	—	—	1,815	—	1,815
Intangible assets not subject to amortization	—	—	100	—	100
Other assets	—	4	100	—	104
Total assets	$ 98	$ 217	$ 4,461	$ (278)	$ 4,498
Liabilities and Shareholders' Equity:					
Current liabilities:					
Accounts payable	$ 1	$ —	$ 246	$ —	$ 247
Accrued royalties	—	—	1,057	—	1,057
Taxes and other withholdings	—	—	23	—	23
Current portion of long-term debt	—	—	17	—	17
Note payable to shareholders	—	—	—	—	—
Other current liabilities	1	—	403	—	404
Total current liabilities	2	—	1,746	—	1,748
Long-term debt	—	174	2,055	—	2,229
Deferred tax liabilities, net	—	—	201	—	201
Dividends payable	5	—	—	—	5
Other noncurrent liabilities	2	—	224	—	226
Total liabilities	9	174	4,226	—	4,409
Shareholder's equity	89	43	235	(278)	89
Total liabilities and shareholder's equity	$ 98	$ 217	$ 4,461	$ (278)	$ 4,498

Consolidating Balance Sheet
September 30, 2004

	Warner Music Group Corp.	WMG Holdings Corp. (issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(in millions)		
Assets:					
Current assets:					
Cash and equivalents	$ —	$ —	$ 555	$ —	$ 555
Accounts receivable, net	—	—	571	—	571
Inventories	—	—	65	—	65
Royalty advances expected to be recouped within one year	—	—	223	—	223
Deferred tax assets	—	—	38	—	38
Other current assets	—	—	86	—	86
Total current assets	—	—	1,538	—	1,538
Royalty advances expected to be recouped after one year	—	—	223	—	223
Investments in and advances to (from) consolidated subsidiaries	762	978	—	(1,740)	—
Investments	—	—	8	—	8
Property, plant and equipment	—	—	189	—	189
Goodwill	—	—	978	—	978
Intangible assets subject to amortization	—	—	1,937	—	1,937
Intangible assets not subject to amortization	—	—	100	—	100
Other assets	—	—	117	—	117
Total assets	$ 762	$ 978	$ 5,090	$ (1,740)	$ 5,090
Liabilities and Shareholders' Equity:					
Current liabilities:					
Accounts payable	$ —	$ —	$ 226	$ —	$ 226
Accrued royalties	—	—	1,003	—	1,003
Taxes and other withholdings	—	—	10	—	10
Current portion of long-term debt	—	—	12	—	12
Note payable to shareholders	342	—	—	—	342
Other current liabilities	140	19	432	(4)	587
Total current liabilities	482	19	1,683	(4)	2,180
Long-term debt	—	—	1,828	—	1,828
Deferred tax liabilities, net	—	—	265	—	265
Other noncurrent liabilities	—	—	333	—	333
Minority interest in preferred stock of subsidiary	—	—	—	204	204
Intercompany.	—	(3)	3	—	—
Total liabilities	482	16	4,112	200	4,810
Shareholder's equity (1)	280	962	978	(1,940)	280
Total liabilities and shareholder's equity	$ 762	$ 978	$ 5,090	$ (1,740)	$ 5,090

(1) WMG Holdings Corp. stockholder's equity consists of $762 million of common equity and $200 million of preferred equity. The preferred equity represents a direct contribution from the Investor Group of $400 million in exchange for 40,000 shares of cumulative preferred stock issued as part of the original Acquisition. Prior to September 30, 2004, 20,000 of such shares were redeemed for $200 million. The value of the preferred shares is classified as minority interest on the consolidated balance sheet of Warner Music Group Corp.

Consolidating Statement of Operations
For The Year Ended September 30, 2005

	Warner Music Group Corp.	WMG Holdings Corp. (issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(in millions)		
Revenues	$ —	$ —	$ 3,502	$ —	$ 3,502
Costs and expenses:	—	—	—	—	
Cost of revenues	—	—	(1,850)	—	(1,850)
Selling, general and administrative expenses	—	—	(1,301)	—	(1,301)
Amortization of intangible assets	—	—	(187)	—	(187)
Loss on termination of management agreement	—	—	(73)	—	(73)
Restructuring costs, net	—	—	(7)	—	(7)
Total costs and expenses	—	—	(3,418)	—	(3,418)
Operating income	—	—	84	—	84
Interest expense, net	(1)	(35)	(146)	—	(182)
Equity in the losses of equity-method investees, net	(185)	(110)	(1)	295	(1)
Net investment-related gains (losses)	—	—	1	—	1
Loss on repayment of Holdings Notes	—	(35)	—	—	(35)
Unrealized gain on warrant	17	—	—	—	17
Other expense, net	—	—	7	—	7
Minority interest expense	—	(5)	—	—	(5)
(Loss) income before income taxes	(169)	(185)	(55)	295	(114)
Income tax expense	—	—	(55)	—	(55)
Net (loss) income	$ (169)	$ (185)	$ (110)	$ 295	$ (169)

Consolidating Statement of Operations
For The Seven Months Ended September 30, 2004

	Warner Music Group Corp.	WMG Holdings Corp. (issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(in millions)		
Revenues	$ —	$ —	$ 1,769	$ —	$ 1,769
Costs and expenses:					
Cost of revenues	—	—	(944)	—	(944)
Selling, general and administrative expenses	—	—	(677)	—	(677)
Amortization of intangible assets	—	—	(104)	—	(104)
Restructuring costs, net	—	—	(26)	—	(26)
Total costs and expenses	—	—	(1,751)	—	(1,751)
Operating income	—	—	18	—	18
Interest expense, net	—	—	(80)	—	(80)
Equity in the losses of equity-method investees, net	(122)	(104)	(2)	226	(2)
Loss on repayment of bridge loan	—	—	(6)	—	(6)
Unrealized loss on warrant	(116)	(4)	—	—	(120)
Other expense, net	—	—	(4)	—	(4)
Minority interest expense	—	(14)	—	—	(14)
(Loss) Income before income taxes	(238)	(122)	(74)	226	(208)
Income tax expense	—	—	(30)		(30)
Net (loss) income	$ (238)	$ (122)	$ (104)	$ 226	$ (238)

Combining Statement of Operations
For The Three Months Ended February 29, 2004

	Warner Music Group Corp. (a)	WMG Holdings Corp. (issuer) (a)	WMG Acquisition Corp.	Eliminations	Old WMG Combined
			(In millions)		
Revenues			$ 779		$ 779
Costs and expenses:					
Cost of revenues			(415)		(415)
Selling, general and administrative expenses			(319)		(319)
Amortization of intangible assets			(56)		(56)
Total costs and expenses			(790)		(790)
Operating loss			(11)		(11)
Interest expense, net			(2)		(2)
Equity in the losses of equity-method investees, net			(2)		(2)
Loss before income taxes			(15)		(15)
Income tax expense			(17)		(17)
Net loss			$ (32)		$ (32)

(a) For periods prior to the Acquisition, Warner Music Group Corp. (formerly known as "WMG Parent Corp") and WMG Holdings Corp. did not exist.

Combining Statement of Operations
For The Ten Months Ended September 30, 2003 (unaudited)

	Warner Music Group Corp. (a)	WMG Holdings Corp. (issuer) (a)	WMG Acquisition Corp.	Eliminations	Old WMG Combined
			(in millions)		
Revenues			$ 2,487		$ 2,487
Costs and expenses:					
Cost of revenues			(1,449)		(1,449)
Selling, general and administrative expenses			(995)		(995)
Amortization of intangible assets			(201)		(201)
Loss on sale of physical distribution assets			(12)		(12)
Restructuring costs, net			(27)		(27)
Total costs and expenses			(2,684)		(2,684)
Operating loss			(197)		(197)
Interest expense, net			(5)		(5)
Net investment-related losses			(17)		(17)
Equity in the losses of equity-method investees, net			(32)		(32)
Deal-related transactions and other costs			(7)		(7)
Other expense, net			(10)		(10)
Loss before income taxes			(268)		(268)
Income tax benefit			67		67
Net loss			$ (201)		$ (201)

(a) For periods prior to the Acquisition, Warner Music Group Corp. and WMG Holdings Corp. did not exist.

Combining Statement of Operations
For The Year Ended November 30, 2003

	Warner Music Group Corp. (a)	WMG Holdings Corp. (Issuer) (a)	WMG Acquisition Corp.	Eliminations	Old WMG Combined
			(in millions)		
Revenues			$ 3,376		$ 3,376
Costs and expenses:					
Cost of revenues			(1,940)		(1,940)
Selling, general and administrative expenses			(1,286)		(1,286)
Impairment of goodwill and other intangible assets			(1,019)		(1,019)
Amortization of intangible assets			(242)		(242)
Loss on sale of physical distribution assets			(12)		(12)
Restructuring costs, net			(35)		(35)
Total costs and expenses			(4,534)		(4,534)
Operating loss			(1,158)		(1,158)
Interest expense, net			(5)		(5)
Net investment-related losses			(26)		(26)
Equity in the losses of equity-method investees, net			(41)		(41)
Deal-related transaction and other costs			(70)		(70)
Other expense, net			(17)		(17)
Loss before income taxes			(1,317)		(1,317)
Income tax expense			(36)		(36)
Net loss			$ (1,353)		$ (1,353)

(a) For periods prior to the Acquisition, Warner Music Group Corp. and WMG Holdings Corp. did not exist.

Consolidating Statement of Cash Flows
For The Year Months Ended September 30, 2005

	Warner Music Group Corp.	WMG Holdings Corp. (issuer)	WMG Acquisition Corp.	Eliminations	Consolidated
			(in millions)		
Cash flows from operating activities:					
Net loss	$ (169)	$ (185)	$ (110)	$ 295	$ (169)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Depreciation and amortization	—	—	239	—	239
Loss on repayment of Holdings Notes	—	35	—	—	35
Non-cash interest expense	—	31	37	—	68
Non-cash stock-based compensation expense	—	—	25	—	25
Net investment-related losses	—	—	(1)	—	(1)
Minority interest	—	5	—	—	5
Equity in the losses of equity-method investees	—	—	1	—	1
Equity in the gains (losses) of consolidated subsidiaries	185	110	—	(295)	—
Unrealized gain on warrant	(17)	—	—	—	(17)
Changes in operating assets and liabilities:					
Accounts receivable	—	—	(58)	—	(58)
Inventories	—	—	(3)	—	(3)
Royalty advances	—	—	—	—	—
Accounts payable and accrued liabilities	1	—	9	—	10
Other balance sheet changes	—	1	70	—	70
Net cash provided by (used in) operating activities	—	(3)	208	—	205
Cash flows from investing activities:					—
Investments and acquisitions	—	—	(78)	—	(78)
Investment proceeds	—	—	54	—	54
Capital expenditures	—	—	(30)	—	(30)
Net cash used in investing activities	—	—	(54)	—	(54)
Cash flows from financing activities:					
Issuance of Holdings debt	—	696	—	—	696
Repayment of Holdings debt	—	(574)	—	—	(574)
Additional term loan borrowings	—	—	250	—	250
Financing costs of borrowings	—	(17)	(3)	—	(20)
Debt repayments	—	—	(14)	—	(14)
Capital contributions received (paid)	(590)	517	73	—	—
Proceeds on the sale of restricted shares	1	—	—	—	1
Proceeds on the issuance of common stock	554		—	—	554
Costs of issuing common stock	(32)	—	—	—	(32)
Change in intercompany	(7)	18	(11)	—	—
Return of capital	(917)	(1,157)	(742)	1,899	(917)
Return of capital received	1,157	742	—	(1,899)	—
Repurchase of warrants	(126)	(12)	—	—	(138)
Return of capital to preferred shareholders	—	(200)	—	—	(200)
Dividends paid on preferred capital	—	(9)	—	—	(9)
Loans to third party	—	—	(10)	—	(10)
Other	—	—	(3)	—	(3)
Net cash provided by (used in) financing activities	40	4	(460)	—	(416)
Effect of foreign currency on cash	—	—	(2)	—	(2)
Net increase (decrease) in cash	40	1	(308)	—	(267)
Cash and equivalents at beginning of period	—	—	555	—	555

Cash and equivalents at end of period	$ 40	$ 41	$ 247	$ —	$ 288

Consolidating Statement of Cash Flows
For The Seven Months Ended September 30, 2004

	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Consolidated
			(in millions)		
Cash flows from operating activities:					
Net loss	$ (238)	$ (122)	$ (104)	$ 226	$ (238)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Depreciation and amortization	—	—	140	—	140
Deferred taxes	—	—	8	—	8
Loss on repayment of bridge loan	—	—	6	—	6
Non-cash interest expense	—	—	19	—	19
Equity in the losses of equity-method investees, including distributions	122	104	3	(226)	3
Minority interest	—	14	—	—	14
Unrealized loss on warrant	116	4	—	—	120
Changes in operating assets and liabilities:					
Accounts receivable	—	—	(33)	—	(33)
Inventories	—	—	(10)	—	(10)
Royalty advances	—	—	77	—	77
Accounts payable and accrued liabilities	—	—	(23)	—	(23)
Other balance sheet changes	—	—	3	—	3
Net cash provided by (used in) operating activities	—	—	86	—	86
Cash flows from investing activities:					
Acquisition of Old WMG	(853)	(1,250)	(2,638)	2,103	(2,638)
Investments and acquisitions	—	—	(10)	—	(10)
Capital expenditures	—	—	(15)	—	(15)
Net cash used in investing activities	(853)	(1,250)	(2,663)	2,103	(2,663)
Cash flows from financing activities:					
Borrowings	—	—	2,348	—	2,348
Financing costs of borrowings	—	—	(99)	—	(99)
Debt repayments	—	—	(631)	—	(631)
Capital contributions	—	850	1,250	(2,100)	—
Proceeds from the issuance of Class C Common Stock	85	—	—	—	85
Proceeds from the issuance of Class L Common Stock	765	—	—	—	765
Proceeds from the issuance of preferred stock	—	400	—	—	400
Repurchase of subsidiary preferred stock	—	(202)	—	—	(202)
Proceeds from the issuance of restricted shares	3	—	—	—	3
Return of capital (paid) received	—	210	(210)	—	—
Dividends paid on preferred capital	—	(8)	—	—	(8)
Change in amounts due to parent	—	—	3	(3)	—
Net cash provided by (used in) financing activities	853	1,250	2,661	(2,103)	2,661
Effect of foreign currency exchange rate changes on cash	—	—	—	—	—
Net increase in cash and equivalents	—	—	84	—	84
Cash and equivalents at beginning of period	—	—	471	—	471

Cash and equivalents at end of period	$ —	$ —	$ 555	$ —	$ 555

Combining Statement of Cash Flows
For The Three Months Ended February 29, 2004

	Warner Music Group Corp. (a)	WMG Holdings Corp. (Issuer) (a)	WMG Acquisition Corp.	Eliminations	Old WMG Combined
			(In millions)		
Cash flows from operating activities:					
Net loss			$ (32)		$ (32)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Depreciation and amortization			72		72
Deferred taxes			(4)		(4)
Non-cash interest expense			2		2
Equity in the losses of equity-method investees, including distributions			2		2
Changes in operating assets and liabilities:					
Accounts receivable			387		387
Inventories			6		6
Royalty advances			(4)		(4)
Accounts payable and accrued liabilities			(109)		(109)
Other balance sheet changes			1		1
Net cash provided by operating activities			321		321
Cash flows from investing activities:					
Investments and acquisitions			(2)		(2)
Investment proceeds			19		19
Capital expenditures			(3)		(3)
Net cash provided by investing activities			14		14
Cash flows from financing activities:					
Borrowings			—		—
Debt repayments			(124)		(124)
Capital contributions			262		262
Decrease (increase) in amounts due from Time Warner-affiliated companies			194		194
Dividends paid			(342)		(342)
Net cash used in financing activities			(10)		(10)
Effect of foreign currency exchange rate changes on cash			2		2
Net increase in cash and equivalents			327		327
Cash and equivalents at beginning of period			144		144
Cash and equivalents at end of period			$ 471		$ 471

(a) For periods prior to the Acquisition, Warner Music Group Corp. and WMG Holdings Corp. did not exist.

Combining Statement of Cash Flows
For The Ten Months Ended September 30, 2003 (unaudited)

	Warner Music Group Corp. (a)	WMG Holdings Corp. (issuer) (a)	WMG Acquisition Corp.	Eliminations	Old WMG Combined
			(in millions)		
Cash flows from operating activities:					
Net loss			$ (201)		$ (201)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Depreciation and amortization			272		272
Deferred taxes			(117)		(117)
Loss on sale of physical distribution assets			12		12
Non-cash interest expense			10		10
Net investment-related losses (gains)			17		17
Equity in the losses of equity-method investees, including distributions			35		35
Changes in operating assets and liabilities:					
Accounts receivable			275		275
Inventories			24		24
Royalty advances			38		38
Accounts payable and accrued liabilities			(116)		(116)
Other balance sheet changes			8		8
Net cash provided by operating activities			257		257
Cash flows from investing activities:					
Investments and acquisitions			(43)		(43)
Capital expenditures			(30)		(30)
Net cash used in investing activities			(73)		(73)
Cash flows from financing activities:					
Borrowings			114		114
Debt repayments			(101)		(101)
Capital contributions			132		132
Decrease (increase) in amounts due from Time Warner-Affiliated companies			(293)		(293)
Principal payments on capital leases			(3)		(3)
Net cash used in financing activities			(151)		(151)
Effect of foreign currency exchange rate changes on cash			6		6
Net increase in cash and equivalents			39		39
Cash and equivalents at beginning of period			41		41
Cash and equivalents at end of period			$ 80		$ 80

(a) For periods prior to the Acquisition, Warner Music Group Corp. and WMG Holdings Corp. did not exist.

Combining Statement of Cash Flows
For The Year Ended November 30, 2003

	Warner Music Group Corp. (a)	WMG Holdings Corp. (Issuer) (a)	WMG Acquisition Corp.	Eliminations	Old WMG Combined
			(In millions)		
Cash flows from operating activities:					
Net loss			$ (1,353)		$ (1,353)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Impairment of goodwill and other intangible assets			1,019		1,019
Depreciation and amortization			328		328
Deferred taxes			(19)		(19)
Loss on sale of physical distribution assets			12		12
Non-cash interest expense			11		11
Net investment-related losses (gains)			26		26
Equity in the losses of equity-method investees, including distributions			44		44
Changes in operating assets and liabilities:					
Accounts receivable			(121)		(121)
Inventories			12		12
Royalty advances			111		111
Accounts payable and accrued liabilities			169		169
Other balance sheet changes			39		39
Net cash provided by operating activities			278		278
Cash flows from investing activities:					
Investments and acquisitions			(52)		(52)
Investment proceeds			38		38
Capital expenditures			(51)		(51)
Net cash used in investing activities			(65)		(65)
Cash flows from financing activities:					
Borrowings			114		114
Debt repayments			(101)		(101)
Capital contributions			132		132
Decrease (increase) in amounts due from Time Warner-affiliated companies			(195)		(195)
Dividends paid			(68)		(68)
Principal payments on capital leases			(3)		(3)
Net cash used in financing activities			(121)		(121)
Effect of foreign currency exchange rate changes on cash			11		11
Net increase in cash and equivalents			103		103
Cash and equivalents at beginning of period			41		41
Cash and equivalents at end of period			$ 144		$ 144

(a) For periods prior to the Acquisition, Warner Music Group Corp. and WMG Holdings Corp. did not exist.

WARNER MUSIC GROUP CORP.

Schedule II—Valuation and Qualifying Accounts
Year Ended September 30, 2005
Seven Months Ended September 30, 2004,
Three Months Ended February 29, 2004, and
Year Ended November 30, 2003

Description	Balance at Beginning of Period	Additions Charged to Cost and Expenses	Deductions	Balance at End of Period
		(in millions)		
Year Ended September 30, 2005				
Reserve deducted from accounts receivable				
Allowance for doubtful accounts	$ 58	$ 1	$ (9)	$ 50
Reserves for sales returns and allowances	164	493	(489)	168
Allowance for deferred tax asset	293	86	(56)	323
	$ 515	$ 580	$ (554)	$ 541
Seven Months Ended September 30, 2004				
Reserve deducted from accounts receivable				
Allowance for doubtful accounts	$ 69	$ 7	$ (18)	$ 58
Reserves for sales returns and allowances	200	278	(314)	164
Allowance for deferred tax asset	—	293	—	293
	$ 269	$ 578	$ (332)	$ 515
Three Months Ended February 29, 2004				
Reserve deducted from accounts receivable				
Allowance for doubtful accounts	$ 67	$ 2	$ —	$ 69
Reserves for sales returns and allowances	224	128	(152)	200
Allowance for deferred tax asset	—	—	—	—
	$ 291	$ 130	$ (152)	$ 269
Year Ended November 30, 2003				
Reserve deducted from accounts receivable				
Allowance for doubtful accounts	$ 68	$ 9	$ (10)	$ 67
Reserves for sales returns and allowances	213	585	(574)	224
Allowance for deferred tax asset	21	—	(21)	—
	$ 302	$ 594	$ (605)	$ 291

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCE DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Certification

The certifications of the principal executive officer and the principal financial officer (or persons performing similar functions) required by Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Certifications") are filed as exhibits to this report. This section of the report contains the information concerning the evaluation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) ("Disclosure Controls") and changes to internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) ("Internal Controls") referred to in the Certifications and this information should be read in conjunction with the Certifications for a more complete understanding of the topics presented.

Introduction

Warner Music Group Corp. became subject to the periodic and other reporting requirements of the Securities Exchange Act of 1934, as amended, on May 10, 2005, the effective date of our registration statement relating to our Initial Common Stock Offering. WMG Acquisition Corp., our wholly owned subsidiary, became subject to the periodic and other reporting requirements of the Exchange Act on February 10, 2005, the effective date of WMG Acquisition Corp.'s registration statement relating to its exchange offer to exchange outstanding unregistered notes for freely tradeable exchange notes that were registered under the Securities Act of 1933, as amended.

SEC rules define "disclosure controls and procedures" as controls and procedures that are designed to ensure that information required to be disclosed by public companies in the reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms.

SEC rules define "internal control over financial reporting" as a process designed by, or under the supervision of, a public company's principal executive and principal financial officers, or persons performing similar functions, and effected by our board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles, or U.S. GAAP, including those policies and procedures that: (i) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the company, (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. GAAP, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Our management, including the principal executive officer and principal financial officer, does not expect that our Disclosure Controls or Internal Controls will prevent or detect all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the limitations in any and all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our company have been detected. Further, the design of any control system is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its

stated goals under all potential future conditions. Because of these inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected even when effective Disclosure Controls and Internal Controls are in place.

Internal Controls

In connection with the audit of WMG Acquisition Corp., and subsequently Warner Music Group Corp. for our prior 2004 fiscal year-end, our outside auditors identified a number of significant deficiencies that together constituted material weaknesses in our internal controls. A material weakness, as defined by the Public Company Accounting Oversight Board, is a significant deficiency that by itself, or in combination with other significant deficiencies, results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

Our outside auditors identified three material weaknesses as of the prior fiscal year. Specifically, there were certain content issues at our print business, there was a lack of entity level controls present and there were issues related to our royalty systems. In connection with the audit for our current 2005 fiscal year-end, our auditors noted that material weaknesses no longer exist for entity level controls due to the hiring of several key executives, establishing of an internal audit function and other changes in internal controls described below. The control issues of the print business are also no longer relevant since this business was sold during this fiscal year. Our outside auditors did note that our domestic operations continue to use different royalty systems, which has continued to create certain complexities in reconciling royalty expense and payables. While we recognize that additional staff is needed to cope with current requirements in royalty processing until a new system can be developed, we may not be able to hire and train additional staff. See also "Risk Factors—Our outside auditors have identified weaknesses in our internal controls that could affect our ability to ensure reliable financial reports."

Evaluation of Disclosure Controls and Procedures

Based on our management's evaluation (with the participation of our principal executive officer and principal financial officer), as of the end of the period covered by this report and as a result of the weaknesses in our internal controls described above and below, our principal executive officer and principal financial officer have concluded that our Disclosure Controls need to be improved so that they will provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act will be recorded, processed, summarized and reported within the time periods specified in SEC rules and forms. In addition, we continue to review our disclosure controls and procedures during the transition to a stand-alone business with the objective of implementing comprehensive periodic reporting standards as well as addressing the weaknesses in Internal Controls identified by our outside auditors. Since completion of the audit related to our fiscal 2004 year-end, we have taken a number of actions, as set forth below, to remedy the weaknesses discovered in our Internal Controls so that the Company's Disclosure Controls are effective in the future. We will continue to devote resources to improve our controls and remedy weaknesses related to our royalty systems that continued to be identified since the completion of the most recent audit for the 2005 fiscal year-end.

Changes in Internal Control over Financial Reporting

We have already taken a number of actions to begin to address the items identified by our outside auditors and to provide reasonable assurances that the objectives of our Disclosure Controls and Internal Controls will be met including:

- hiring a permanent chief financial officer;
- establishing an audit committee and appointing two independent directors, one of which is a financial expert and the chair of the committee;

- outsourcing our internal audit functions and hiring a director of internal audit;
- hiring internal and external resources to lead our Section 404 evaluation efforts;
- adopting a new code of conduct and hiring outside consultants to assist in the implementation of the new code of conduct;
- adopting a compliance program, appointing a chief compliance officer and hiring a deputy compliance officer;
- hiring other accounting and SEC experienced personnel to enhance the accounting department;
- hiring additional outside resources to assist our internal personnel with royalties accounting and SEC reporting;
- hiring a director of taxation and other tax department members; and
- entering into a joint venture with Universal Music Group, Exigen Group and Lightspeed Venture Partners to build a new uniform royalty system for all U.S. operations.

These actions have resulted in the elimination of the material weaknesses related to entity level controls identified at the time of our fiscal 2004 audit as noted above. We are committed to maintaining high standards of internal control over financial reporting, corporate governance and public disclosure and continue to improve and refine our Internal Controls as an ongoing process and will continue to take corrective actions and implement improvements as appropriate.

Other than as summarized above, there have been no changes in our Internal Controls over financial reporting or other factors that have materially affected, or are reasonably likely to materially affect, our Internal Controls.

Institution of Internal Controls in compliance with Section 404 of Sarbanes-Oxley

As a result of our registration with the Securities and Exchange Commission, we will be required to comply with Section 404 of the Sarbanes-Oxley Act of 2002 and regulations promulgated thereunder as of September 30, 2006. We are currently performing the system and process evaluation and testing required (and any necessary remediation) in an effort to comply with management certification and auditor attestation requirements of Section 404. In the course of our ongoing evaluation, we have identified areas of our internal controls requiring improvement, and plan to design enhanced processes and controls to address these and any other issues that might be identified through this review. As a result, we expect to incur additional expenses and diversion of management's time. We cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or the impact of the same on our operations and may not be able to ensure that the process is effective or that the internal controls are or will be effective in a timely manner. If we are not able to implement the requirements of Section 404 in a timely manner or with adequate compliance, our independent auditors may not be able to certify as to the effectiveness of our internal control over financial reporting and we may be subject to sanctions or investigation by regulatory authorities, such as the Securities and Exchange Commission. As a result, there could be an adverse reaction in the financial markets due to loss of confidence in the reliability of our financial statements. In addition, we may be required to incur costs in improving our internal control system and the hiring of additional personnel. Any such action could adversely affect our results. See also "Risk Factors—Our internal controls over financial reporting may not be adequate and our independent auditors may not be able to certify as to their adequacy, which could have a significant affect on our business and reputation."

ITEM 9B. OTHER INFORMATION

Item 9B is not applicable and has been omitted.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

In addition to the information set forth under the caption "Executive Officers of the Registrant" in Part I of this Form 10-K, the information required by this Item is incorporated by reference to our Proxy Statement for the fiscal 2005 Annual Meeting of Stockholders.

ITEM 11. EXECUTIVE COMPENSATION

The information called for by this item is hereby incorporated by reference to our Proxy Statement for the fiscal 2005 Annual Meeting of Stockholders.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information called for by this item is hereby incorporated by reference to our Proxy Statement for the fiscal 2005 Annual Meeting of Stockholders.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

The information called for by this item is hereby incorporated by reference to our Proxy Statement for the fiscal 2005 Annual Meeting of Stockholders.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The information called for by this item is hereby incorporated by reference to our Proxy Statement for the fiscal 2005 Annual Meeting of Stockholders.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a)(1) Financial Statements

The Financial Statements listed in the Index to Consolidated Financial Statements, filed as part of this Annual Report on Form 10-K.

(a)(2) Financial Statement Schedules

The Financial Statements Schedule listed in the Index to Consolidated Financial Statements, filed as part of this Annual Report on Form 10-K.

(a)(3) Exhibits

See Item 15(b) below.

(b) Exhibits

Exhibit No.	Description
2.1(1)	Purchase Agreement, dated as of November 24, 2003 between Time Warner Inc. and WMG Acquisition Corp., as amended
2.2(12)	Settlement Agreement, dated as of July 13, 2005, between Time Warner Inc. and WMG Acquisition Corp.
3.1(2)	Amended and Restated Certificate of Incorporation of Warner Music Group Corp.
3.2(2)	By-laws of Warner Music Group Corp.
4.1(3)	Indenture, dated as of April 8, 2004, among WMG Acquisition Corp., the Guarantors named therein and Wells Fargo Bank, National Association
4.2(3)	First Supplemental Indenture, dated as of November 16, 2004, among WMG Acquisition Corp., Wells Fargo Bank, National Association, as Trustee, WEA Urban LLC and WEA Rock LLC
4.3(7)	Second Supplemental Indenture, dated as of May 17, 2005, among WMG Acquisition Corp., Wells Fargo Bank, National Association, as Trustee, NonZero (since renamed Cordless Recordings LLC) and The Biz LLC
4.4(13)	Third Supplemental Indenture, dated as of September 28, 2005, among WMG Acquisition Corp., Wells Fargo Bank, National Association, as Trustee, and Lava Records LLC
4.5(14)	Fourth Supplemental Indenture, dated as of October 26, 2005, among WMG Acquisition Corp., Wells Fargo Bank, as Trustee, and BB Investments LLC
4.6**	Fifth Supplemental Indenture, dated as of November 29, 2005, among WMG Acquisition Corp., Wells Fargo Bank, as Trustee, and Perfect Game Recording Company LLC
4.7(4)	Indenture, dated as of December 23, 2004; between WMG Holdings Corp. and Wells Fargo Bank, National Association, as Trustee
4.8(12)	Guarantee of Warner Music Group Corp.
10.1(5)	Amended and Restated Credit Agreement, dated as of April 8, 2004, among WMG Acquisition Corp., the Overseas Borrowers from time to time party thereto, WMG Holdings Corp., each lender from time to time party thereto Banc of America Securities LLC and Deutsche Bank Securities Inc., as Joint Lead Arrangers and Joint Book Managers, Lehman Brothers Inc. and Merrill Lynch, Pierce, Fenner & Smith Incorporated, as Co-Arrangers and Joint Book Managers, Deutsche Bank Securities Inc. and Lehman Commercial Paper Inc., as Co-Syndication Agents, Merrill Lynch, Pierce, Fenner & Smith Incorporated, as Documentation Agent, and Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer.

Exhibit No.	Description
10.2(5)	Amendment No. 1 to the Credit Agreement, dated as of September 30, 2004, among WMG Acquisition Corp., the Overseas Borrowers party thereto, WMG Holdings Corp., the lenders party thereto, Banc of America Securities LLC and Deutsche Bank Securities Inc., as joint lead arrangers and joint book managers and various other parties
10.3(5)	Amendment No. 2 to the Credit Agreement, dated as of December 6, 2004, among WMG Acquisition Corp., the Overseas Borrowers party thereto, WMG Holdings Corp., the lenders party thereto, Banc of America Securities LLC and Deutsche Bank Securities Inc., as joint lead arrangers and joint book managers and various other parties
10.4(6)	Amendment No. 3 to the Credit Agreement, dated as of April 29, 2005 among WMG Acquisition Corp., the Overseas Borrowers parties thereto, WMG Holdings Corp., the lenders party thereto, Banc of America Securities LLC and Deutsche Bank Securities Inc., as joint lead arrangers and joint book and various other parties
10.5(5)	Security Agreement, dated as of February 27, 2004, from the Grantors named to therein to Bank of America, N.A.
10.6(5)	Subsidiary Guaranty, dated as of February 27, 2004, from the Guarantors named therein and the Additional Guarantors named therein in favor of the Secured Parties named in the Credit Agreement referred to therein
10.7(5)	Parent Guaranty, dated as of February 27, 2004, from WMG Holdings Corp. in favor of the Secured Parties named in the Credit Agreement referred to therein
10.8(5)	Company Guaranty, dated as of February 27, 2004, from WMG Acquisition Corp. in favor of the Secured Parties named in the Credit Agreement referred to therein
10.9(5)	Deed of Trust, Security Agreement, Assignment of Rents and Leases and Fixture Filing (Tennessee) by and from Warner Bros. Records, Inc. to Kay B. Housch in favor of Bank of America, N.A., dated as of February 29, 2004 (20, 24, 26 Music Square East)
10.10(5)	Deed of Trust, Security Agreement, Assignment of Rents and Leases and Fixture Filing (Tennessee) by and from Warner Bros. Records, Inc. to Kay B. Housch in favor of Bank of America, N.A., dated as of February 29, 2004 (21 Music Square East)
10.11(5)	Deed of Trust, Security Agreement, Assignment of Rents and Leases and Fixture Filing (California) by and from Warner Bros. Records, Inc. to MTC Financial Inc. in favor of Bank of America, N.A., dated as of February 29, 2004
10.12(5)	Trademark Security Agreement, dated as of February 29, 2004, made by the Grantors listed on the signature pages thereto in favor of the Bank of America, N.A.
10.13(5)	Copyright Security Agreement, dated as of February 29, 2004, made by the Grantors listed on the signature pages thereto in favor of the Bank of America, N.A.
10.14(5)	Stockholders Agreement, dated as of February 29, 2004, among WMG Parent Corp., WMG Holdings Corp., WMG Acquisition Corp. and Certain Stockholders of WMG Parent Corp. and WMG Holdings Corp.
10.15(5)	Amendment No. 1 to Stockholder's Agreement, dated as of July 30, 2004, among WMG Parent Corp., WMG Holdings Corp., WMG Acquisition Corp., each Person executing this Agreement and listed as an Investor on the signature pages hereto, each Person executing this Agreement and listed as a Seller on the signature pages hereto, each Person executing this Agreement and listed as a Manager on the signature pages hereto and such other Persons, if any, that from time to time become party hereto as holders of Other Holder Shares solely in the capacity of permitted assignees with respect to certain registration rights hereunder
10.16(7)	Amended and Restated Stockholders Agreement dated as of May 10, 2005 between Warner Music Group Corp., WMG Holdings Corp., WMG Acquisition Corp. and certain stockholders of Warner Music Group Corp.

Exhibit No.	Description
10.17(5)	Seller Administrative Services Agreement, dated as of February 29, 2004, between Time Warner Inc. and WMG Acquisition Corp.
10.18(5)	Amendment No. 1 to Seller Administrative Services Agreement, dated as of July 1, 2004, between Time Warner Inc. and WMG Acquisition Corp.
10.19(5)	Purchaser Administrative Services Agreement, dated as of February 29, 2004, between Time Warner Inc. and WMG Acquisition Corp.
10.20(5)	Management Agreement, dated as of February 29, 2004, among WMG Parent Corp., WMG Holdings Corp., WMG Acquisition Corp., THL Managers V, L.L.C., Bain Capital Partners, LLC, Providence Equity Partners IV Inc. and Music Partners Management, LLC
10.21(7)	Termination Agreement of the Management Agreement dated as of May 10, 2005, between Warner Music Group Corp., WMG Holdings Corp., WMG Acquisition Corp., THL Managers V, L.L.C., Bain Capital Partners, LLC, Providence Equity Partners IV Inc. and Music Partners Management, LLC
10.22(5)	Warrant Agreement (MMT Warrants), February 29, 2004, WMG Parent Corp., WMG Holdings Corp. and Historic TW Inc.
10.23(5)	Warrant Agreement (Three-Year Warrants), February 29, 2004, WMG Parent Corp., WMG Holdings Corp. and Historic TW Inc.
10.24(10)	Warrant Repurchase Agreement, dated as of April 21, 2005, between Warner Music Group Corp. and Historic TW Inc.
10.25(5)	Employment Agreement, effective as of March 1, 2004, between WMG Acquisition Corp. and Edgar Bronfman, Jr.
10.26(5)	Employment Agreement, dated as of January 25, 2004, between WMG Acquisition Corp. and Lyor Cohen
10.27(5)	Employment Agreement, dated as of November 28, 2002, between Warner Music International Services Ltd. and Paul-René Albertini, assumed by WMG Acquisition Corp. on March 1, 2004, as amended by the amendment dated October 21, 2004, and as further amended by the amendment dated December 17, 2004
10.28(5)	Employment Agreement, dated as of March 22, 1999, between Warner Music Inc. and Les Bider, as amended, assumed by WMG Acquisition Corp. on March 1, 2004
10.29(5)	Employment Agreement, dated as of December 15, 1998, between Warner Music Inc. and David H. Johnson, as amended, assumed by WMG Acquisition Corp. on March 1, 2004
10.30(5)	Employment Agreement, dated as of December 21, 2004, between Warner Music Inc. and Michael D. Fleisher
10.31(9)	Employment Agreement, dated as of March 17, 2005, between Warner/Chappell Music, Inc. and Richard Blackstone
10.32(8)	Separation Agreement and Release, dated as of March 31, 2005, between Warner Music Inc. (formerly known as Warner Music Group Inc.) and Les Bider
10.33(5)	Restricted Stock Award Agreement, dated as of March 1, 2004, between Warner Music Group Corp. (formerly known as WMG Parent Corp.) and Edgar Bronfman, Jr.
10.34(5)	Restricted Stock Award Agreement, dated as of March 1, 2004, between Warner Music Group Corp. (formerly known as WMG Parent Corp.) and Lyor Cohen
10.35(5)	Restricted Stock Award Agreement, dated as of January 28, 2005, between Warner Music Group Corp. (formerly known as WMG Parent Corp.) and David H. Johnson
10.36(5)	Restricted Stock Award Agreement, dated as of December 31, 2004, between Warner Music Group Corp. (formerly known as WMG Parent Corp.) and Michael D. Fleisher

Exhibit No.	Description
10.47(6)	Restricted Stock Award Agreement, dated as of October 1, 2004, between Warner Music Group Corp. (formerly known as WMG Parent Corp.) and Paul-René Albertini
10.38(9)	Restricted Stock Award Agreement, dated as of March 17, 2005, between Warner Music Group Corp. and Richard Blackstone
10.39(5)	Stock Option Agreement, dated as of October 1, 2004, between Warner Music Group Corp. (formerly known as WMG Parent Corp.) and Paul-René Albertini
10.40(6)	Deed of Variation to Restricted Stock Award Agreement of Paul-René Albertini, dated as of May 6, 2005, between Warner Music Group Corp. and Paul-René Albertini
10.41(5)	Stock Option Agreement, dated as of September 30, 2004, between Warner Music Group Corp. (formerly known as WMG Parent Corp.) and Les Bider
10.42(5)	Form of WMG Parent Corp. LTIP Stock Option Agreement
10.43(6)	Form of Warner Music Group Corp. 2005 Omnibus Award Plan
10.44(5)	Office Lease, June 27, 2002, by and between Media Center Development, LLC and Warner Music Group Inc., as amended
10.45(5)	Lease, dated as of February 1, 1996, between 1290 Associates, L.L.C. and Warner Communications Inc.
10.46(5)	Consent to Assignment of Sublease, dated as of October 5, 2001, between 1290 Partners, L.P. and Warner Music Group
10.47(5)	Lease, dated as of February 29, 2004, between Historical TW Inc. and Warner Music Group Inc. regarding 75 Rockefeller Plaza
10.48*(5)	U.S. Pick, Pack and Shipping Services Agreement, dated as of October 24, 2003, between Warner-Elektra-Atlantic Corporation and Cinram Distribution LLC
10.49*(5)	U.S. Manufacturing and Packaging Agreement, dated as of October 24, 2003, between Warner-Elektra-Atlantic Corporation and Cinram Manufacturing Inc.
10.50*(5)	International Pick, Pack and Shipping Services Agreement, dated as of October 24, 2003, between WEA International Inc. and Warner Music Manufacturing Europe GmbH Company
10.51*(5)	International Manufacturing and Packaging Agreement, dated as of October 24, 2003, between WEA International Inc. and Warner Music Manufacturing Europe GmbH Company
12.1**	Computation of Ratio of Earnings to Fixed Charges
14**	Code of Ethics
21.1**	List of Subsidiaries
23.1**	Consent of Ernst & Young LLP
31.1**	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended
31.2**	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act, as amended
32.1***	Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit No.	Description
32.2***	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(c)	Financial Statement Schedules
	Schedule II—Valuation and Qualifying Accounts

* Exhibit omits certain information that has been filed separately with the Securities and Exchange Commission pursuant to a confidential treatment request pursuant to Rule 406 promulgated under the Securities Act of 1933, as amended.

** Filed herewith

*** Pursuant to SEC Release No. 33-8212, this certification will be treated as "accompanying" this Annual Report on Form 10-K and not "filed" as part of such report for purposes of Section 18 of the Securities Exchange Act, as amended, or otherwise subject to the liability of Section 18 of the Securities Exchange Act, as amended, and this certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act, as amended, except to the extent that the registrant specifically incorporates it by reference.

(1) Incorporated by reference to WMG Acquisition Corp.'s Amendment No. 1 to the Registration Statement on Form S-4 (File No. 333-121322).
(2) Incorporated by reference to Warner Music Group Corp.'s Quarterly Report on Form 10-Q for the period ended March 31, 2005 (File No. 001-32502).

(3) Incorporated by reference to WMG Acquisition Corp.'s Registration Statement on Form S-4 (File No. 333-121322).
(4) Incorporated by reference to Warner Music Group Corp.'s Amendment No. 2 to the Registration Statement on Form S-1 (File No. 333-123249).
(5) Incorporated by reference to WMG Acquisition Corp.'s Amendment No. 2 to the Registration Statement on Form S-4 (File No. 333-121322).
(6) Incorporated by reference to Warner Music Group Corp.'s Amendment No. 4 to the Registration Statement on Form S-1 (File No. 333-123249).
(7) Incorporated by reference to Warner Music Group Corp.'s Current Report on Form 8-K filed May 19, 2005 (File No. 001-32502).
(8) Incorporated by reference to WMG Acquisition Corp.'s Current Report on form 8-K filed April 1, 2005 (File No. 333-121322).
(9) Incorporated by reference to WMG Acquisition Corp.'s Current Report on form 8-K filed April 11, 2005 (File No. 333-121322).
(10) Incorporated by reference to Warner Music Group Corp.'s Amendment No. 3 to the Registration Statement on Form S-1 (File No. 333-123249).
(11) Incorporated by reference to WMG Acquisition Corp.'s Amendment No. 3 to the Registration Statement on Form S-4 (File No. 333-121322).
(12) Incorporated by reference to Warner Music Group Corp.'s Registration Statement on Form S-4 (File No. 333-126786-01).
(13) Incorporated by reference to Warner Music Group Corp.'s Current Report on Form 8-K filed October 3, 2005 (File No. 001-32502).
(14) Incorporated by reference to Warner Music Group Corp.'s Current Report on Form 8-K filed October 27, 2005 (File No. 001-32502)

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on December 1, 2005.

WARNER MUSIC GROUP CORP.

By: /s/ EDGAR BRONFMAN, JR.

Name: Edgar Bronfman, Jr.
Title: Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)

By: /s/ MICHAEL D. FLEISHER

Name: Michael D. Fleisher
Title: Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons in the capacities indicated on December 1, 2005.

Signature	Title
/s/ EDGAR BRONFMAN, JR. Edgar Bronfman, Jr.	Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)
/s/ MICHAEL D. FLEISHER Michael D. Fleisher	Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)
/s/ LEN BLAVATNIK Len Blavatnik	Director
/s/ SHELBY W. BONNIE Shelby W. Bonnie	Director
/s/ RICHARD BRESSLER Richard Bressler	Director
/s/ CHARLES A. BRIZIUS Charles A. Brizius	Director
/s/ JOHN P. CONNAUGHTON John P. Connaughton	Director
/s/ SCOTT L. JAECKEL Scott L. Jaeckel	Director
/s/ SETH W. LAWRY Seth W. Lawry	Director

Signature	Title
/s/ THOMAS H. LEE Thomas H. Lee	Director
/s/ IAN LORING Ian Loring	Director
/s/ JONATHAN M. NELSON Jonathan M. Nelson	Director
/s/ MARK NUNNELLY Mark Nunnelly	Director
/s/ SCOTT M. SPERLING Scott M. Sperling	Director

Exhibit 4.6

WMG ACQUISITION CORP.
Issuer

PERFECT GAME RECORDING COMPANY LLC

And

WELLS FARGO BANK, NATIONAL ASSOCIATION,

Trustee

FIFTH SUPPLEMENTAL INDENTURE

Dated as of November 29, 2005

TO

INDENTURE

Dated as of April 8, 2004

as amended

U.S. Dollar-denominated 7⅞% Senior Subordinated Notes due 2014

Sterling-denominated 8⅛% Senior Subordinated Notes due 2014

This FIFTH SUPPLEMENTAL INDENTURE is dated as of this 29th day November, 2005 (the "Fifth Supplemental Indenture"), among WMG ACQUISITION CORP., a Delaware corporation (the "Company"), PERFECT GAME RECORDING COMPANY LLC (the "Subsidiary Guarantor") and WELLS FARGO BANK, NATIONAL ASSOCIATION, as indenture trustee (the "Trustee").

WHEREAS, the Company, the guarantors parties thereto and the Trustee entered into an Indenture dated as of April 8, 2004, as amended by the First Supplemental Indenture dated as of November 16, 2004 among the Company, the Trustee, WEA Urban LLC and WEA Rock LLC (since renamed Asylum Records LLC and East West Records LLC, respectively), as further amended by the Second Supplemental Indenture, dated as of May 17, 2005, among the Company, the Trustee, NonZero, LLC (since renamed Cordless Recordings LLC) and The Biz, LLC, as further amended by the Third Supplemental Indenture, dated as of September 28, 2005, among the Company, the Trustee, and Lava Records LLC, as further amended by the Fourth Supplemental Indenture, dated as of October 26, 2005, among the Company, the Trustee, and BB Investments LLC (collectively, the "Indenture"), for the benefit of each other and for the equal and ratable benefit of the Holders of the U.S. Dollar-denominated 7 3/8 % Senior Subordinated Notes due 2014 and the Sterling-denominated 8 1/8 % Senior Subordinated Notes due 2014 (the "Notes"). Capitalized terms used herein without definition have the meanings ascribed to such terms in the Indenture.

WHEREAS, Section 4.16 of the Indenture requires the Company to cause certain Restricted Subsidiaries to execute and deliver a supplemental indenture to the Indenture providing for issuance by such Restricted Subsidiary of a Subsidiary Guarantee of payment of the Notes.

WHEREAS, the foregoing amendment is permitted under Section 9.01(6) of the Indenture.

WHEREAS, the Company and the Subsidiary Guarantor desires and has requested the Trustee to join with it in the execution and delivery of this Fifth Supplemental Indenture,

NOW, THEREFORE, in consideration of the addition of the Subsidiary Guarantor named below as Subsidiary Guarantor hereunder, the Company and the Subsidiary Guarantor named below covenant and agree with the Trustee as follows:

1. Perfect Game Recording Company LLC shall become a Subsidiary Guarantor as of the date of this Fifth Supplemental Indenture by execution and delivery of this Fifth Supplemental Indenture.

2. The Indenture, as supplemented and amended by this Fifth Supplemental Indenture, is in all respects ratified and confirmed, and the Indenture and this Fifth Supplemental Indenture shall be read, taken and construed as one and the same instrument.

3. If any provision hereof limits, qualifies or conflicts with another provision hereof which is required to be included in this Fifth Supplemental Indenture by any of the provisions of the Trust Indenture Act, such required provision shall control.

4. All covenants and agreements in this Fifth Supplemental Indenture by the Company and the Subsidiary Guarantor shall bind their respective successors and assigns, whether so expressed or not.

5. In case any provision in this Fifth Supplemental Indenture shall be invalid, illegal or unenforceable, the validity, legality and enforceability of the remaining provisions shall not in any way be affected or impaired thereby.

6. Nothing in this Fifth Supplemental Indenture, expressed or implied, shall give to any Person, other than the parties hereto and their successors hereunder, and the Holders any benefit or any legal or equitable right, remedy or claim under this Fifth Supplemental Indenture.

7. THIS FIFTH SUPPLEMENTAL INDENTURE AND THE SECURITIES SHALL BE GOVERNED BY, AND CONSTRUED IN ACCORDANCE WITH, THE LAWS OF THE STATE OF NEW YORK.

8. All terms used in this Fifth Supplemental Indenture not otherwise defined herein that are defined in the Indenture shall have the meanings set forth therein.

9. This Fifth Supplemental Indenture may be executed in any number of counterparts, each of which shall be an original; but such counterparts shall together constitute but one and the same instrument.

10. The recitals contained herein shall be taken as statements of the Issuer and the Subsidiary Guarantor, and the Trustee assumes no responsibility for their correctness. The Trustee makes no representations as to the validity or sufficiency of the Indenture, this Fifth Supplemental Indenture or of the Notes and shall not be accountable for the use or application by the Company of the Notes or the proceeds thereof.

[REMAINDER OF PAGE INTENTIONALLY BLANK]

IN WITNESS WHEREOF, the parties have executed this Fifth Supplemental Indenture as of the date first written above.

WMG ACQUISITION CORP.

By: /s/ Paul Robinson

Name: Paul Robinson
Title: SVP & Deputy General Counsel

PERFECT GAME RECORDING COMPANY LLC

By: /s/ Paul Robinson

Name: Paul Robinson
Title: Vice President

WELLS FARGO BANK, NATIONAL ASSOCIATION, as Indenture Trustee

By: /s/ Jeffrey Rose

Name: Jeffrey Rose
Title: Vice President

Exhibit 12.1

Warner Music Group Corp.

Computation of Ratio of Earnings to Fixed Charges
(Unaudited)

	Ten Months Ended September 30, 2003	Three Months Ended February 29, 2004	Seven Months Ended September 30, 2004	Twelve Months Ended September 30, 2005
	(unaudited)	(audited)	(audited)	(audited)
(Loss) Income before income taxes (1)	$ (268)	$ (15)	$ (208)	$ (114)
Add:				
Fixed charges	50	8	99	149
Income as adjusted before income taxes	$ (218)	$ (7)	$ 25	$ 85
Fixed charges:				
Interest expense	36	4	91	132
Portion of rental expense representative of interest (2)	14	4	8	12
Preferred stock dividend requirements of consolidated subsidiaries (1)	—	—	—	5
Total fixed charges	50	8	99	149
Deficiency in earnings over fixed charges	$ (268)	$ (15)	$ (208)	$ (114)
Ratio of earnings to fixed charges	N/A	N/A	N/A	N/A

(1) The preferred stock dividend requirements of Holdings, a consolidated subsidiary, is included in fixed charges (i.e., the denominator of the ratio calculation) but excluded from the numerator of the ratio calculation because such amount was not deducted in arriving at Warner Music Group Corp.'s pre-tax income (loss) from continuing operations as defined. If Holdings did not incur fixed charges, the minority interest in pre-tax income of Holdings would be subtracted in determining earnings.

(2) Estimated at 1/3 of total rent expense.

Exhibit 14

Warner Music Group Corp.

warner | music | group

Code of Conduct

May 5, 2005

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1 Our Values

The core values of Warner Music Group Corp. ("WMG") form the basis of our corporate culture and inform every aspect of our business globally.

Creativity and Innovation: We emphasize creativity and the freedom of artistic expression, and we are committed to pursuing the most innovative and inventive ways to connect more people with the music they love.

Entrepreneurial Leadership: Our entrepreneurial spirit drives our success and growth. We are committed to taking bold risks, finding new approaches to old challenges, and executing quickly on smart ideas.

Integrity: We adhere to the highest professional and ethical standards in everything we do, whether transacting business, interacting with our artists, colleagues or suppliers or being a good corporate citizen.

Competitiveness: We love to win and have a clear understanding of what winning means. We firmly believe in our ability to successfully compete and to create lasting value for our investors, employees, customers and artists.

Collaboration: We focus our competitive spirit on the marketplace, not in the workplace. We focus on maintaining a collaborative work environment where people listen to and learn from each other, even when they disagree.

Diversity: As a leading global music company, we are committed to diversity in the workplace.

Community: We strive to be a force for positive change in the communities where we live and work.

2 Leadership Message

Dear Colleague:

Warner Music Group Corp. ("WMG") takes pride in being a global leader in the music industry and is dedicated to meeting the highest standards of creativity and integrity in every aspect of our business.

Our ability to deliver lasting value for our investors, employees, customers and artists depends upon our adherence to WMG's core values, which are the foundation of our business and the driving force behind our corporate culture, professional conduct and day-to-day business practices. They guide our business decisions and are the means by which we build our careers and evaluate and reward every member of the WMG family.

It is the responsibility of all WMG employees worldwide to follow these principles and to display the highest standards of professionalism in everything they do in the workplace. This requires a genuine commitment from each and every one of us at every level of WMG.

Employees faced with business or personal situations that are not covered in the WMG Code of Conduct are expected to exercise good judgment and to act ethically in their decision-making. They are also expected to follow all laws and regulations that impact our business. Any questions about these values or our Code of Conduct can always be directed to WMG's Compliance Officer.

Only by working together to uphold these values can we maintain a productive work environment and a reputation for quality, leadership, integrity and trust.

Sincerely,

Edgar Bronfman, Jr.
Chairman and Chief Executive Officer

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

3 Our Code of Conduct

This Code of Conduct (the "Code") is intended to provide all WMG employees with a basic understanding of the standards of conduct that apply to our business. This document is also a guide that can be used in our day-to-day activities, informing us of our responsibilities, as well as the resources available to assist us in living up to WMG's standards.

This Code cannot anticipate every situation that you may encounter. Because some ethical issues may arise that are not explicitly covered within the Code, each individual employee has the responsibility to exercise good judgment while seeking guidance when appropriate.

The Code is available in both hard copy and electronically in the U.S. on the WMG Intranet (http://bside.wmg.com). It can also be accessed via our external Internet site (www.wmg.com). In addition, frequently asked questions are found throughout the Code to illustrate how our standards may be applied in the workplace. Any changes, waivers or exceptions to the Code must be approved in writing by the WMG Compliance Officer, who may be required to seek approval from the Board of Directors and disclose such waivers publicly.

3.1 Acknowledgement

You are required to acknowledge that you have received and read the Code. WMG may ask you to re-submit this acknowledgment on an annual basis or whenever the Code is significantly updated.

Frequently Asked Questions

1) Why does WMG have a Code?

WMG is committed to high standards of ethics and integrity in all of our businesses. The Code is a guide to help our employees understand WMG's standards of conduct and our employees' role in upholding these standards.

2) To whom does the WMG Code apply?

The Code applies to all directors, officers and employees of WMG worldwide, regardless of title or tenure. These standards apply to you even if you do not acknowledge the Code, subject to applicable local law. Moreover, we will encourage all those who conduct business with WMG (e.g., vendors, consultants and business partners) and anyone on the WMG payroll to conduct themselves in a manner consistent with the Code.

3) Who oversees the Code?

Adherence to the Code is everyone's responsibility, and is monitored by the management of WMG and its operating companies and the WMG board of directors.

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

4 Seeking Advice and Reporting Concerns

Sections six through nine of the Code ("Our People," "Our Company and Shareholders," "Our Marketplace and Industry" and "Public and Community") describe particular WMG standards. Because not all situations are clearly "right" or "wrong," you should not hesitate to seek advice when you are unsure about an appropriate course of action. This would include, for instance, situations when:

- Applicable policies seem difficult to interpret under the circumstances
- The relevant laws or standards are complex
- You have limited experience dealing with the subject matter
- You find yourself in a "gray area" and need guidance

All WMG directors, officers and employees should report potential or suspected violations of this Code (See Section 4.1 below.) This includes instances where you suspect the following parties are – or are about to be – engaged in misconduct:

- Executives, managers or employees
- Members of the Board of Directors
- Vendors
- Consultants
- Business partners

4.1 Where to Seek Help

Depending upon the type of assistance you seek, there are several avenues for you to choose from:

- *Your Manager, Human Resources Representative or Business Unit Head.* Your manager is usually a good place to start, because he or she is likely to be familiar with the issue at hand. Additionally, because many of your questions may be answered by your Human Resources representative, typically this individual, or a business unit head acting in this capacity, should be your second point of contact.

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

- *WMG Compliance Officer.* If you are uncomfortable discussing the issue with your manager or Human Resources representative, or if they are unable to provide you with the answers you seek, you may contact the WMG Compliance Officer:

  WMG Compliance Officer
  Warner Music Group
  75 Rockefeller Plaza
  New York, NY 10019
  (212) 275-4780
  Facsimile: (212) 405-5297
  E-mail: conduct@wmg.com

- *Compliance Hotline.* WMG has established the *Compliance Hotline*, a confidential toll-free hotline (in the United States – 1-800-620-5549, International – see Appendix A for numbers) that you can use to seek guidance or report potential violations of the Code. The *Compliance Hotline* is available to all WMG employees 24 hours a day, 7 days a week and 365 days a year. When you call the *Compliance Hotline:*

  - You may raise your concern anonymously if you wish, and we will honor your request to the extent allowable by law.
  - We will investigate your concern in a timely manner and ensure that you receive an appropriate response.
  - We will keep your concern confidential to the extent allowable by law, and ensure that you are not retaliated against for raising a legitimate, good faith concern.

Frequently Asked Questions

1) Of the individuals who are available to help with a concern, which one should I call first?

If you have a question or concern, you should first try to resolve the issue by speaking with your manager, a Human Resources representative or your business unit head. Typically, if these individuals are unable to assist you, they will be able to direct you to other WMG resources who can. Of course, if you are uncomfortable raising a concern with your manager or Human Resources representative, or if doing so would be impractical under the circumstances, you can always call the *Compliance Hotline* or the WMG Compliance Officer.

2) When should I report a violation of the Code?

Any time you believe that a violation of the Code may have occurred or is about to occur, you should inform your manager, Human Resources representative or business unit head. You can also call the *Compliance Hotline* or the WMG Compliance Officer.

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

3) What if I want to report a violation of WMG standards anonymously?

You may report a violation of WMG standards anonymously through *Compliance Hotline*. Please note that unless you provide sufficient information and detail about your concern, WMG may be limited in its ability to respond. However, it is up to you whether you wish to remain anonymous. Regardless of whether you choose to identify yourself or remain anonymous, WMG will provide an opportunity for you to be generally informed regarding the general status or resolution of your issue, as appropriate or permitted by law.

4) What happens when I call the *Compliance Hotline?*

The following occurs when a call is placed to the *Compliance Hotline*:

- The call will be fielded by a trained professional from an outside firm skilled in identifying key issues associated with the matter you identify.
- The professional will ensure that the issue you raise gets an appropriate and timely response.
- You will be provided with a case number that allows you to call the *Compliance Hotline* after a specified period of time to get an updated status of the issue.

Please note that the *Compliance Hotline* has operators capable of speaking a variety of languages. For more information as to the appropriate number to dial, please see Appendix A.

5) What happens after I report a violation of the Code?

Your report will be promptly investigated under the direction of the WMG Compliance Officer. If your allegation is substantiated, corrective action will be taken. Allegations of a serious nature, including those related to fraudulent financial reporting or misappropriation of assets, will be disclosed promptly to the Board of Directors or the appropriate committee of the Board.

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

5 Our Responsibilities

5.1 Your Responsibilities

As a WMG employee, you are responsible for:

- Becoming familiar with, and upholding the standards contained in the Code, as well as other legal, professional, and ethical standards that apply to your job
- Seeking help or advice when you are unsure of the proper course of action
- Raising concerns or potential violations of the law or of the Code standards to WMG management or the appropriate committee of the Board of Directors

Frequently Asked Questions

What do I need to do to keep up to date on the standards, laws and regulations that apply to me as a WMG employee?

You should begin by reading this document. Subsequently, you should attend any required training that has been assigned to you. Finally, you should pay particular attention to company bulletins as these may contain important information about new policies and recent developments in our business.

5.2 Management Responsibilities

All employees with management or supervisory roles have additional responsibilities that include:

- Ensuring that WMG resources are available to help our employees seek advice or report misconduct
- Establishing clear goals that are achievable without violating WMG's standards of conduct
- Setting a positive example by conducting our business with honesty and integrity
- Enforcing WMG standards consistently and fairly
- Remaining accountable for their personal conduct and of those they supervise

Frequently Asked Questions

What should I do if I believe that my managers or colleagues are not living up to WMG's standards?

You should call the *Compliance Hotline* or contact the WMG Compliance Officer to discuss the specific nature of your concern. WMG is committed to addressing all issues that arise or are reported by WMG employees.

5.3 Enforcement

The standards addressed in the Code and its related policies are very serious matters. Individuals found to be in violation of WMG's standards may be subject to disciplinary action, up to and including termination.

Violating or compromising these standards may result in substantial legal fines, sanctions, or harm to your or WMG's reputation. In addition, certain violations may expose you to personal liability, which could result in criminal prosecution.

We never want to see any of our employees placed in this position, and WMG has established resources to help assist you in achieving compliance with the Code at all times.

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

6 Our People

WMG is committed to creating a safe and secure work environment that is free of discrimination and harassment.

6.1 Equal Employment Opportunity

WMG is an equal opportunity employer. All of our employment decisions (e.g., recruiting, hiring, training, promoting, compensating and terminating) will be made in accordance with applicable laws and regulations. Moreover, we will apply our employment decisions without regard to race, religion, national origin, color, sex, age, marital status, sexual orientation, disability, veteran status or any other category protected by the laws of the applicable country or local government.

6.2 Harassment-Free Work Environment

WMG is committed to creating and maintaining a work environment that is governed by mutual respect and tolerance. We will not tolerate behavior that can be construed as harassment, whether it is directed at a WMG employee or a third party. We also extend this prohibition to our agents, suppliers, vendors, consultants, contractors and other business partners. If you are aware of an incident of harassment, it is your responsibility to report it.

By way of example, forms of harassment may include, but are not limited to, physical, verbal, and nonverbal behavior that disrupts an employee's work performance or in any way contributes to an intimidating, hostile or offensive work environment.

Frequently Asked Questions

1) One possible type of harassment is sexual harassment. What are some examples of sexual harassment?

Some examples of behavior that may constitute sexual harassment include, but are not limited to:

- Unwelcome sexual advances
- Requests for sexual favors as a condition of employment or promotion
- Jokes, activities or conduct creating an offensive work environment
- Displaying or sending communications that contain sexual, derogatory or obscene content

At times, some people may find WMG's products or potential products to be objectionable. Please note that sending and receiving product-related communications in the ordinary course of business is permissible.

2) Are both men and women protected from sexual harassment?

Yes. WMG will seek to protect both women and men from sexual harassment, whether carried out by a person of the same or opposite sex.

3) What should I do if I witness what I think is harassment?

If you witness harassment or are the subject of harassment, you are encouraged to let the person who carried out the harassment know that his or her behavior is unwelcome and that it be stopped immediately. If for any reason you are uncomfortable with doing this, or, if after speaking with the individual the offensive behavior does not stop, you should report the incident (See Section 4.1 above.) Remember, you are protected from retaliation if you report a concern in good faith.

6.3 Health and Safety

WMG is committed to providing our employees with a safe working environment. As such, we ask you to comply with all applicable health and safety rules, taking appropriate measures to ensure your physical safety and that of your colleagues. Please also make yourself familiar with any injury and illness prevention programs that WMG may have in effect.

6.4 Drug-Free Work Environment

WMG does not permit substance abuse on company premises, or while representing WMG in a business capacity. If you feel you or a colleague may need help with a substance abuse problem, we encourage you to contact the appropriate Human Resources representative. In addition, many WMG companies in the U.S. have an employee assistance program available.

6.5 Employee Privacy

WMG will treat as confidential our employees' personal information (e.g., information relating to compensation, health status and employment records.) Our employees should not disclose private information of others that is gained as a result of their position with WMG unless such disclosure is lawful and properly authorized.

7 Our Company and Shareholders

WMG is committed to accurately recording our financial results, protecting our company assets and ensuring the security of our information systems.

7.1 Accurate Financial Reporting

Those who have financial reporting responsibilities must ensure financial reporting information is full, fair, accurate, timely and understandable. Honest and ethical conduct, including the ethical handling of actual or apparent conflicts of interest between personal and professional interests are required at all times. Please refer to the WMG Whistleblower Procedures if you have a concern about accurate financial reporting.

7.2 Securities Trading

Securities laws prohibit the buying or selling of securities while in the possession of material, non-public information, and this is commonly known as "insider trading." Material information is further defined as any non-public information that a reasonable investor would consider important in making a decision to purchase or sell securities. WMG employees must never act upon, or disclose to other parties, material non-public information. Please refer to the WMG Securities Trading Policy for more information.

Frequently Asked Questions

1) Does the securities trading policy apply to me?

If you work for any WMG operating company, our securities trading policy applies to you. Please contact your manager or Human Resources representative, or the *Compliance Hotline* if you have any questions about this policy.

2) What are some examples of "material information" as they pertain to the securities trading policy?

Examples of information that would be regarded as "material" include, but are not limited to:

- Projections of future earnings or losses
- News of a proposed or pending merger, acquisition or tender offer
- Changes in dividend policies or the declaration of a stock split or the offering of additional securities
- Changes in management
- Significant new deals or other new developments impacting the business
- Impending bankruptcy or financial liquidity problems

- Internal financial information
- The gain or loss of a major contract or major artist relationship
- Major litigation
- Significant actions by regulatory bodies

3) What if I learn of material non-public information of other companies we work with?

The same prohibition against insider trading applies to material non-public information obtained relating to other companies.

4) Can I pass along material non-public information to a family member or friend?

No. You are not permitted to give this information to others, and, under certain local law, you can be held liable for insider trading should this information be used to trade stock or other equities.

7.3 Proprietary and Confidential Information

You should be on guard to protect WMG's confidential information. Such information may include artist agreements, pricing structures and competitive strategy. Confidential information should only be shared internally on a need-to-know basis. You should not seek to personally benefit from, or divulge to a competitor or outside party any of our confidential information.

Be especially vigilant about any inquiries by members of the financial press, investment analysts or others in the financial community. You should refer all such inquiries to your local Corporate Communications group. Please refer to the WMG Regulation FD: Policy Regarding Communications with Analysts, Security Holders and Others for more information about these inquiries.

Please also remember that we must protect the confidential information of our vendors, consultants, and business partners. Such information is never to be disclosed except with the approval of WMG's Legal Department. Respecting the privacy of music consumers is a paramount concern. This includes respect for and strict observance of the privacy policy relating to our Internet sites.

7.4 Safeguarding of Company Assets

WMG's most important assets are its artists, copyrights and employees. We expect each employee to treat each with proper respect and care. Copyrights are the core of our business and it is crucial that we ensure their proper protection and preservation. In particular, pre-release materials must be safeguarded and distributed only to properly authorized individuals.

Additionally, we have physical assets including computer and office equipment which must be used responsibly and protected against misuse, damage or theft. Of special concern are our electronic information facilities, including computer and telecommunications networks. These assets are critical to our daily operations, and we expect each employee to remain vigilant against their misuse. You should protect the security of our communications and computer systems from computer viruses and hackers by exercising caution when downloading files, and by safeguarding your network password.

7.5 Electronic Communications

Employees must ensure that e-mail and the Internet are used responsibly. Reasonable personal use of WMG's electronic communication system is permitted but WMG reserves the right to monitor how its computers are being used and to review information contained in these systems, including all e-mail sent and received on the WMG system.

E-mail and the Internet may never be used for illegal or unethical purposes or for any activity which may compromise or harm our company. The use of unauthorized peer-to-peer networks is one example of such activity. Obscene and discriminatory material may never be transmitted, retrieved or stored. Please also note that all files downloaded from the Internet are subject to the limitation of copyright laws and WMG policy.

Frequently Asked Questions

Can I send personal e-mail when I am in the office?

Yes. We realize that work and personal lives sometimes overlap. Nevertheless, always use your discretion about when it is appropriate to send personal e-mails. Whenever possible, use an e-mail account that is not attached to the WMG name. Also, note that e-mails sent and received from WMG computers may be monitored.

Naturally, our electronic facilities must not be used for illegal activity, but please also be mindful that you should not use our systems and networks to solicit for your non-company business activity, or for religious, charitable or political causes.

7.6 Copyright Infringement

The illegal copying and distribution of recorded music (i.e., "piracy") is a serious issue within the music community and threatens our work at WMG. Therefore, downloading copyrighted music and/or burning CDs from unauthorized peer-to-peer networks are prohibited. If you have any questions about this or other copyright policies, contact your manager or the WMG Legal Department.

7.7 Records Management

There may be legal requirements which may make necessary the retention of company records and documents. This applies to e-mail messages, electronic and recorded data, as well as hard copies of our business documents.

In addition to any applicable statutory record retention requirements, the existence of pending litigation, investigations or subpoenas may require that our records be retained longer than usual. Accordingly, WMG's Legal Department will provide guidance on issues as they arise and will instruct that certain categories of documents not be discarded until any pending matters are resolved.

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

8 Our Marketplace and Industry

WMG is committed to treating all parties with which it does business in a fair and equitable manner. In addition, we will comply with all laws, rules and regulations applicable to our marketplace.

8.1 Conflicts of Interest

In the course of our business, conflicts of interest can arise in a variety of circumstances. These may include many situations where you, a member of your household or a family member's personal interests may conflict with that of WMG. In all cases, it is your responsibility to avoid conflicts of interest, or even the appearance of a conflict of interest. Please note that you may be required to complete an annual conflict of interest questionnaire designed to help identify and therefore mitigate potential conflicts of interest.

In the event that you, a member of your household or a family member experience an actual or even potential conflict of interest, it is your responsibility to report this situation directly to the WMG Compliance Officer who will help you address this situation. Potential conflicts of interest include, but are not limited to:

- Investing significantly in WMG competitors, vendors, consultants or other business partners
- Working for other companies, especially our competitors, vendors, consultants or business partners, while employed at WMG
- Doing business on behalf of WMG with a competitor, vendor, consultant or business partner if you or a family member has a personal or financial interest or stake in the other company
- Working with a member of your household or a family member, where the member of your household or family member is in a direct reporting relationship

Frequently Asked Questions

1) What are specific examples of conflicts of interest?

The following scenarios illustrate conflicts of interest that might occur at WMG, based on an action of a WMG employee or a member of an employee's immediate family or household:

- Engaging in the music business outside of WMG, including making contractual arrangements with artists
- Investing in a competitor such as another music company, where the investment is not exempt (see Question #2 below)
- Investing in a vendor such as a supplier to WMG where the investment is not exempt (see Question #2 below)

- Investing in a company if you have access to the company's material non-public information (See Section 7.2 – Securities Trading) based upon your work with WMG
- Working with a member of your household or a family member on the same WMG project and reporting to him or her or vice-versa
- Involvement in a competitive business or partnership by a member of your household or a family member
- Serving as a director of another company without written approval of the WMG Compliance Officer or WMG Conflicts Committee

Please note that you should always consult your manager or the WMG Compliance Officer when you are faced with a specific circumstance that may pose a conflict of interest.

2) What investments are "exempt" from conflict of interest requirements?

"Exempt investments" will not give rise to a conflict of interest and do not require any type of approval. They include:

- A portfolio investment (a group of stocks held through someone else such as deferred compensation account or another fund offered through WMG)
- Investments in mutual funds
- Publicly-traded securities (which can be held in any amount, except for those involving competitors, vendors, consultants or business partners, which is limited to investments of not more than 2% of the issued and outstanding stock of the corporation. Amounts under that amount are not considered "significant.")

8.2 Gifts and Entertainment

We encourage you to use common sense and good judgment when you entertain or exchange occasional gifts as a way to encourage good business relationships. Please note that any such gifts or entertainment, whether given or received, should be customary and reasonable. Our policy is that WMG employees should not accept a gift or other item greater than USD$100 or EUR100 (or equivalent) at any one time without pre-approval. No employee may accept more than USD$500 or EUR500 (or equivalent) in gifts in total for the calendar year without pre-approval. Questions about this policy may be directed to the WMG Compliance Officer, and you should review any other WMG policy relating to gifts and entertainment for more specific guidance.

Frequently Asked Questions

1) When can I accept a gift?

Nominal gifts such as flowers, candy, T-shirts, or the like are acceptable as long as you do not ask for them and as long as they do not influence, or appear to influence, your ability to make fair and objective business decisions. Gifts of cash, or cash equivalents such as vouchers or gift certificates, are never acceptable. As a rule of thumb, if accepting a gift will make you feel obligated, do not accept it. When in doubt, always seek to consult your manager or the WMG Compliance Officer.

2) If I am invited to a business dinner, convention, or other gathering, is having my expenses for the function paid by others a prohibited gift?

Functions such as business dinners, drinks or other meetings in a social context are not considered gifts if a significant purpose of the meeting is business-related. But this can be a tricky area. If you are given tickets to a sporting event for your personal use, this should be considered a gift. If you attend such a function with our business partners, it would not ordinarily be a gift, unless this occurs with a frequency that suggests an invalid business purpose.

8.3 Sales, Marketing and Promotions

WMG's reputation depends on fair dealing and ethical conduct, and we will not tolerate treating our potential customers, vendors, consultants and other business partners unfairly. Our business practices must always be above reproach and fully compliant with all applicable laws, including laws regarding so-called "payola" practices.

8.4 Fair Competition and Antitrust Laws

The countries we operate in have very complex antitrust laws, which are laws designed to protect free trade and competition. You should be aware that if we act in ways that reduce free marketplace competition, we may be violating these laws. Of particular concern are communications or conversations with competitors. You should never make agreements or hold discussions with our competitors on the following issues:

- Pricing
- Markets and prospective customers
- Boycotts of other competitors, customers, or suppliers

In addition you should not make any agreements with our vendors, consultants or business partners that tie their purchase of one product to another, or with respect to their resale price of our products. If you are working on a potential merger, acquisition, joint venture or any other

situation that causes you concern with regard to antitrust issues, you must consult with WMG's Legal Department, as the requirements and regulatory approvals in this area are complex and may vary from country to country.

Frequently Asked Questions

What type of agreements between WMG and its vendors, consultants, and business partners may violate antitrust and competition laws?

WMG negotiates many agreements with vendors, consultants and business partners. Two examples of agreements which raise significant concerns include:

- Fixing sale prices (agreeing with retailers or business partners to set a minimum price at which they will sell WMG products or services)
- "Tying" products (requiring a customer to purchase a product that it does not want in order to buy the product it does want)

8.5 Contracts and Procurement

WMG is committed to adhering to all the laws and regulations that apply to the procurement of goods or services, and will treat all parties with which we do business fairly. We expect all our employees to conduct themselves in an ethical manner when obtaining new business on behalf of WMG. All of our proposals and contracting arrangements should be based on price, quality, service, and our ability to meet our own needs, and those of our contracting party.

8.6 Doing Business with Governments

When conducting business with governments, WMG employees should be mindful of all laws and regulations concerning government bodies and their employees. We should be particularly sensitive to the Foreign Corrupt Practices Act ("FCPA"), a U.S. anti-bribery law which prohibits payments to or from foreign government officials in return for business or favorable treatment. The activity of all WMG employees, even those outside of the U.S., can expose us to legal liability based upon the FCPA. Please consult with WMG's Legal Department if you have any questions about this law or any dealings with domestic or foreign governments and their employees.

8.7 Doing Business Internationally

There are many different laws and regulations that affect the way we conduct our business around the globe. For example, certain countries restrict imports and exports, or the flow of trade and goods in and out of their borders. Certain countries and the European Union may have laws that affect business dealings with companies inside specific countries. Such laws may take the form of boycotts or sanctions for doing business with specific nations. If you are uncertain as to the laws relating to business conducted in a foreign country, or how you should proceed, consult the WMG Compliance Officer or WMG's Legal Department.

9 Public and Community

WMG is committed to good corporate citizenship, and we will observe all relevant laws and regulations while encouraging and expecting our employees to do the same.

9.1 Media and Public Relations

WMG will periodically issue press releases and make public disclosures about our financial situation. To ensure that all reports and press releases are accurate and consistent, employees must refer all inquiries from the media to the Corporate Communications group.

Only the Chief Executive Officer, Chief Financial Officer, Head of Investor Relations and Senior Vice President and Associate Director of Corporate Communications are authorized to respond to requests for financial and other company reports. Any contact with bankers, securities analysts or other securities markets professionals, such as brokers, investment advisors and mutual fund managers, or to our security holders must be forwarded to Corporate Communications and communications with these people should be made only by specifically designated people with prior approval.

Frequently Asked Questions

What if I am contacted by a member of the media concerning a particular artist or even about WMG itself?

You must refer all media inquiries to your local Corporate Communications group or your business unit head.

9.2 Political and Public Activity

It is important that you make a clear distinction between those situations where you are acting in your private capacity and acting, or appearing to act, on behalf of WMG. For example, you may make a political contribution as a private citizen, but you may not use the WMG name when you are doing so. Moreover, you should not pressure or direct your colleagues to join you in your political or other public activities.

WMG resources or services should not be used to support your political activities, and any contributions from our company to any candidate for public office may only be made through our Political Action Committee (PAC) in the U.S. or only with the approval of WMG's Legal Department.

Frequently Asked Questions

Can I make my own contributions to a political candidate or organization? Can I volunteer to work on a political campaign?

You are free to contribute your money, time or other resources to a political candidate, organization or campaign without the approval of the WMG Legal Department as long as you use your own (and not WMG's) resources and do so on your own time

9.3 Responding to Regulatory Investigations

WMG will respond to government inquiries in a timely, complete and coordinated manner. Employees who are contacted by government representatives or other third parties inquiring about company matters, must immediately notify WMG's Legal Department. You should not attempt to respond to such queries on your own either verbally or in writing, but rather refer such requests to the WMG Legal Department. This is especially critical if the requests pertain to a summons, subpoena, or other document requiring a court appearance or response. Please also report to WMG's Legal Department any inquiries or requests from outside attorneys, even if litigation is not pending or threatened.

9.4 Environmental Responsibility

Because violations of environmental laws or regulations may have serious consequences for WMG and the individuals involved, our employees must abide by all such laws and regulations. We must not falsify information on any environmental form, monitoring report, or in response to inquiries from a government agency.

10 Available Resources

There are several resources available that can provide you with additional information on the matters addressed in the Code. Some of these are listed below.

10.1 Contacts

WMG Compliance Officer (conduct@wmg.com)	(212) 275-4780
WMG Corporate Communications	(212) 275-2244
WMG Conflicts Committee	(212) 275-4780
WMG Legal Department	(212) 275-2030
WMI Legal Department	+44 20 7368 2830
WMG Human Resources	(212) 275-1990
WMI Human Resources	+44 20 7368 2805
WMG Investor Relations	(212) 275-4790
Employee Assistance Program (U.S.)	(800) 833-8707

10.2 Reference Materials Online

Materials such as this Code and other policies referenced in this Code are available to employees at (http://bside.wmg.com). If you are unable to view these materials on B-Side, please contact your manager, Human Resources representative or business unit head.

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

11 Acknowledgement Form

I hereby acknowledge that I have read and received this Code of Conduct (Version 1.0, May 2005.)

_____

Signed

_____

Name (Print)

_____

Title

_____

Employee ID #, if applicable

_____

Company Name

_____

Date

Warner Music Group Compliance Hotline
(U.S.) – 1-800-620-5549
(International) – See Appendix A

A *Compliance Hotline Numbers*

United States: 1-800-620-5549

Outside of the United States: Toll-free numbers are being established. Until such numbers are established, please call 678-250-7548 – feel free to call collect.

Exhibit 21.1

WARNER MUSIC GROUP CORP.

SUBSIDIARIES OF THE REGISTRANT

Legal Name	State or Jurisdiction of Incorporation or Organization
A.P. Schmidt Company	Delaware
Atlantic Recording Corporation	Delaware
Atlantic/143 L.L.C.	Delaware
Atlantic/MR II INC.	Delaware
Atlantic/MR Ventures Inc.	Delaware
Asylum Records LLC	Delaware
BB Investments LLC	Delaware
Berna Music, Inc.	California
Big Beat Records Inc.	Delaware
Big Tree Recording Corporation	Delaware
Bute Sound LLC	Delaware
Cafe Americana Inc.	Delaware
Chappell & Intersong Music Group (Australia) Limited	Delaware
Chappell And Intersong Music Group (Germany) Inc.	Delaware
Chappell Music Company, Inc.	Delaware
Cordless Recordings LLC	Delaware
Cota Music, Inc.	New York
Cotillion Music, Inc.	Delaware
CRK Music Inc.	Delaware
E/A Music, Inc.	Delaware
East West Records LLC.	Delaware
Eleksylum Music, Inc.	Delaware
Elektra Entertainment Group Inc.	Delaware
Elektra Group Ventures Inc.	Delaware
Elektra/Chameleon Ventures Inc.	Delaware
FHK, INC.	Tennessee
Fiddleback Music Publishing Company, Inc	Delaware
Foster Frees Music, Inc.	California
Foz Man Music LLC	Delaware
Inside Job, Inc.	New York
Intersong U.S.A., INC.	Delaware
Jadar Music Corp.	Delaware
Lava Records LLC	Delaware
Lava Trademark Holding Company LLC	Delaware
LEM America, INC.	Delaware
London-Sire Records Inc.	Delaware
McGuffin Music Inc.	Delaware
Mixed Bag Music, Inc.	New York
NC Hungary Holdings Inc.	Delaware
New Chappell Inc.	Delaware
Nonesuch Records Inc.	Delaware
NVC International Inc.	Delaware
Octa Music, Inc.	New York
Penalty Records L.L.C.	New York
Pepamar Music Corp.	New York
Perfect Game Recording Company LLC	Delaware
Revelation Music Publishing Corporation	New York
Rhino Entertainment Company	Delaware

Legal Name	State or Jurisdiction of Incorporation or Organization
Rick's Music Inc.	Delaware
Rightsong Music Inc.	Delaware
Rodra Music, Inc.	California
Sea Chime Music, Inc.	California
SR/MDM Venture Inc.	Delaware
Summy-Birchard, Inc.	Wyoming
Super Hype Publishing, Inc.	New York
T-Boy Music L.L.C.	New York
T-Girl Music L.L.C.	New York
The Biz LLC	Delaware
The Rhythm Method Inc.	Delaware
Tommy Boy Music, Inc.	New York
Tommy Valando Publishing Group, Inc.	Delaware
Tri-Chappell Music Inc.	Delaware
TW Music Holdings Inc.	Delaware
Unichappell Music Inc.	Delaware
W.B.M. Music Corp.	Delaware
Walden Music, Inc.	New York
Warner Alliance Music Inc.	Delaware
Warner Brethren Inc.	Delaware
Warner Bros. Music International Inc.	Delaware
Warner Bros. Records Inc.	Delaware
Warner Custom Music Corp.	California
Warner Domain Music Inc.	Delaware
Warner Music Bluesky Holding Inc.	Delaware
Warner Music Discovery Inc.	Delaware
Warner Music Distribution Inc.	Delaware
Warner Music Inc.	Delaware
Warner Music Latina Inc.	Delaware
Warner Music SP Inc.	Delaware
Warner Sojourner Music Inc.	Delaware
WarnerSongs Inc.	Delaware
Warner Special Products Inc.	Delaware
Warner Strategic Marketing Inc.	Delaware
Warner-Elektra-Atlantic Corporation	New York
Warner-Tamerlane Publishing Corp.	California
Warner/Chappell Music (Services), Inc.	New Jersey
Warner/Chappell Music, Inc.	Delaware
Warprise Music Inc.	Delaware
WB Gold Music Corp.	Delaware
WB Music Corp.	California
WBM/House of Gold Music, Inc.	Delaware
WBPI Holdings LLC	Delaware
WBR Management Services Inc.	Delaware
WBR/QRI Venture, Inc.	Delaware
WBR/Ruffnation Ventures, Inc.	Delaware
WBR/Sire Ventures Inc.	Delaware
We Are Musica Inc.	Delaware
WEA Europe Inc.	Delaware
WEA Inc.	Delaware
WEA International Inc.	Delaware

Legal Name	State or Jurisdiction of Incorporation or Organization
WEA Latina Musica Inc.	Delaware
WEA Management Services Inc.	Delaware
Wide Music, Inc.	California
WMG Acquisition Corp.	Delaware
WMG Holdings Corp.	Delaware
WMG Management Services Inc.	Delaware
WMG Trademark Holding Company LLC	Delaware

Exhibit 23.1

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in the Registration Statement (Form S-8 No. 333-127900) pertaining to the Restricted Stock Agreements of Warner Music Group Corp. and the Registration Statement (Form S-8 No. 333-127899) pertaining to the Stock Option Agreements, 2005 Omnibus Award Plan and the LTIP Stock Option Agreements of Warner Music Group Corp. of our reports dated November 15, 2005 and March 10, 2005, with respect to the consolidated and combined financial statements and schedule of Warner Music Group Corp. included in the Annual Report (Form 10-K) for the year ended September 30, 2005.

December 1, 2005
New York, New York

/s/ Ernst & Young LLP

Exhibit 31.1

CHIEF EXECUTIVE OFFICER CERTIFICATION

I, Edgar Bronfman, Jr., Chief Executive Officer and Chairman of the Board of Directors of Warner Music Group Corp., certify that:

1. I have reviewed this annual report on Form 10-K of Warner Music Group Corp. (the "Registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Registrant and we have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared; and

b) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and

5. Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Dated: December 1, 2005

/s/ EDGAR BRONFMAN, JR.

Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)

Exhibit 31.2

CHIEF FINANCIAL OFFICER CERTIFICATION

I, Michael D. Fleisher, Chief Financial Officer of Warner Music Group Corp., certify that:

1. I have reviewed this annual report on Form 10-K of Warner Music Group Corp. (the "Registrant");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Registrant and we have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared; and

b) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter (the Registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and

5. Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Dated: December 1, 2005

/s/ MICHAEL D. FLEISHER

Chief Financial Officer (Principal Financial and Accounting Officer)

Exhibit 32.1

Certification of the Chief Executive Officer
Pursuant to 18 U.S.C. Section 1350,
As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report of Warner Music Group Corp. (the "Company") on Form 10-K for the period ended September 30, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Edgar Bronfman, Jr., Chief Executive Officer of Warner Music Group Corp., certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: December 1, 2005

/s/ EDGAR BRONFMAN, JR.

Edgar Bronfman, Jr.
Chief Executive Officer

Exhibit 32.2

Certification of the Chief Financial Officer
Pursuant to 18 U.S.C. Section 1350,
As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report of Warner Music Group Corp. (the "Company") on Form 10-K for the period ended September 30, 2005 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Michael D. Fleisher, Chief Financial Officer of Warner Music Group Corp., certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: December 1, 2005

/s/ MICHAEL D. FLEISHER

Michael D. Fleisher
Chief Financial Officer

Created by 10KWizard www.10KWizard.comSource: Warner Music Group C, 10-K, December 01, 2005

EXHIBIT CO 0945

10kWIZARD
SEC POWER SEARCH

FORM 10-Q

Warner Music Group Corp. - WMG

Filed: August 03, 2006 (period: June 30, 2006)

Quarterly report which provides a continuing view of a company's financial position

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Part I.

Financial Information

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EX-32.1 (CERTIFICATION OF THE CHIEF EXECUTIVE OFFICER PURSUANT TO SECTION 906)

EX-32.2 (CERTIFICATION OF THE CHIEF FINANCIAL OFFICER PURSUANT TO SECTION 906)

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, 2006

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.)

75 Rockefeller Plaza
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 is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒

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

As of July 27, 2006, the number of shares of the Registrant's common stock, par value $0.001 per share, outstanding was 148,505,691.787.

WARNER MUSIC GROUP CORP.
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Source: Warner Music Group C, 10-Q, August 03, 2006

ITEM 1. FINANCIAL STATEMENTS

Warner Music Group Corp.
Consolidated Balance Sheets

	June 30, 2006 (unaudited)	September 30, 2005 (audited)
	(In millions)	
Assets		
Current assets:		
Cash and equivalents	$ 306	$ 288
Short-term investments	29	—
Accounts receivable, less allowances of $205 and $218 million	524	637
Inventories	50	52
Royalty advances expected to be recouped within one year	209	190
Deferred tax assets	40	36
Other current assets	47	39
Total current assets	1,205	1,242
Royalty advances expected to be recouped after one year	209	190
Investments	24	21
Property, plant and equipment, net	144	157
Goodwill	946	869
Intangible assets subject to amortization, net	1,746	1,815
Intangible assets not subject to amortization	100	100
Other assets	109	104
Total assets	$ 4,483	$ 4,498
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	$ 202	$ 247
Accrued royalties	1,146	1,057
Taxes and other withholdings	34	23
Current portion of long-term debt	17	17
Dividends payable	22	—
Other current liabilities	336	404
Total current liabilities	1,757	1,748
Long-term debt	2,234	2,229
Dividends payable	3	5
Deferred tax liabilities, net	193	201
Other noncurrent liabilities	216	226
Total liabilities	4,403	4,409
Commitments and Contingencies (See Note 10)		
Shareholders' equity:		
Common stock ($0.001 par value; 500,000,000 shares authorized; 148,503,900 and 148,455,313 shares issued and outstanding)	—	—
Additional paid-in capital	560	548
Accumulated deficit	(509)	(480)
Accumulated other comprehensive income, net	29	21
Total shareholders' equity	80	89
Total liabilities and shareholders' equity	$ 4,483	$ 4,498

See accompanying notes.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Consolidated Statements of Operations (Unaudited)
Three Months Ended June 30, 2006 and 2005

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005
	(In millions, except per share amounts)	
Revenues (b)	$ 822	$ 742
Costs and expenses:		
Cost of revenues (a)	(445)	(396)
Selling, general and administrative expenses (a) (b)	(301)	(318)
Amortization of intangible assets	(48)	(47)
Loss on termination of management agreement	—	(73)
Total costs and expenses	(794)	(834)
Operating income (loss)	28	(92)
Interest expense, net	(45)	(50)
Net investment related gains	—	1
Loss on repayment of Holdings Notes	—	(35)
Other income, net	1	1
Loss before income taxes	(16)	(175)
Income tax benefit (expense)	2	(4)
Net loss	$ (14)	$ (179)
Net loss per common share:		
Basic and diluted	$ (0.10)	$ (1.41)
Weighted average common shares:		
Basic and diluted	143.7	127.0
(a) Includes depreciation expense of	$ (10)	$ (12)
(b) Includes the following expenses resulting from transactions with related companies:		
Revenues	$ 8	$ —
Selling, general and administrative expense	$ (2)	$ (1)

See accompanying notes.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Consolidated Statements of Operations (Unaudited)
Nine Months Ended June 30, 2006 and 2005

	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(In millions, except per share amounts)	
Revenues (b)	$ 2,662	$ 2,597
Costs and expenses:		
Cost of revenues (a)	(1,384)	(1,377)
Selling, general and administrative expenses (a) (b)	(918)	(942)
Amortization of intangible assets	(143)	(140)
Loss on termination of management agreement	—	(73)
Total costs and expenses	(2,445)	(2,532)
Operating income	217	65
Interest expense, net (b)	(135)	(140)
Net investment related gains	—	1
Equity in the gains (losses) of equity-method investees, net	1	(1)
Loss on repayment of Holdings Notes	—	(35)
Unrealized gain on warrants	—	17
Minority interest expense (b)	—	(5)
Other income, net	3	5
Income (loss) before income taxes	86	(93)
Income tax expense	(38)	(46)
Net income (loss)	$ 48	$ (139)
Net income (loss) per common share:		
Basic	$ 0.34	$ (1.22)
Diluted	$ 0.32	$ (1.22)
Weighted average common shares:		
Basic	142.3	114.1
Diluted	150.8	114.1
(a) Includes depreciation expense of	$ (32)	$ (40)
(b) Includes the following expenses resulting from transactions with related companies:		
Revenues	12	—
Selling, general and administrative expense	(10)	(6)
Interest expense	—	(1)
Minority interest expense	—	(5)

See accompanying notes.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Consolidated Statements of Cash Flows (Unaudited)
Nine Months Ended June 30, 2006 and 2005

	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(In millions)	
Cash flows from operating activities		
Net income (loss)	$ 48	$ (139)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	175	180
Non-cash interest expense	39	52
Non-cash, stock-based compensation expense	12	18
Deferred taxes	(17)	(7)
Net investment related gains	—	(1)
Equity in the (gains) losses of equity-method investees, including distributions	(1)	1
Loss on repayment of debt	—	35
Unrealized gain on warrants	—	(17)
Minority interest expense	—	5
Changes in operating assets and liabilities:		
Accounts receivable	121	77
Inventories	3	6
Royalty advances	(54)	(2)
Accounts payable and accrued liabilities	(81)	(22)
Other balance sheet changes	(22)	(14)
Net cash provided by operating activities	223	172
Cash flows from investing activities		
Investments and acquisitions	(95)	(84)
Investments in short-term investments	(29)	—
Investment proceeds	—	50
Capital expenditures	(18)	(20)
Net cash used in investing activities	(142)	(54)
Cash flows from financing activities		
Borrowings, net of financing costs	—	926
Debt repayments	(13)	(584)
Cash paid to repurchase warrant	—	(138)
Proceeds from the issuance of common stock	—	554
Costs to issue common stock	—	(27)
Proceeds from the issuance of restricted shares	—	1
Repurchase of subsidiary preferred stock	—	(200)
Dividends paid on subsidiary preferred stock	—	(9)
Dividends and returns of capital paid	(55)	(917)
Loans to third parties	—	(10)
Other	—	(3)
Net cash used in financing activities	(68)	(407)
Effect of foreign currency exchange rate changes on cash	5	(1)
Net increase (decrease) in cash and equivalents	18	(290)
Cash and equivalents at beginning of period	288	555
Cash and equivalents at end of period	$ 306	$ 265

See accompanying notes.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Consolidated Statement of Shareholders' Equity (Unaudited)
Nine Months Ended June 30, 2006

	Common Stock		Additional Paid-in	Retained Earnings	Accumulated Other Comprehensive	Total Shareholders'
	Shares	Value	Capital	(Deficit)	Income (Loss)	Equity
	(in millions, except number of common shares)					
Balance at September 30, 2005	148,455,313	$ —	$ 548	$ (480)	$ 21	$ 89
Comprehensive income:						
Net income	—	—	—	48	—	48
Foreign currency translation adjustment	—	—	—	—	(4)	(4)
Deferred gains on derivative financial instruments	—	—	—	—	12	12
Total comprehensive income	—	—	—	48	8	56
Dividends	—	—	—	(76)	—	(76)
Issuance of stock options and restricted shares of common stock, net	48,587	—	12	—	—	12
Other	—	—	—	(1)	—	(1)
Balance at June 30, 2006	148,503,900	$ —	$ 560	$ (509)	$ 29	$ 80

See accompanying notes.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)

1. Description of Business

Warner Music Group Corp. (the "Company") was formed by a private equity consortium of Investors (the "Investor Group") 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 content companies and the successor to substantially all of the interests of the recorded music and music publishing businesses of Time Warner Inc. ("Time Warner"). Effective March 1, 2004, Acquisition Corp. acquired such interests from Time Warner for approximately $2.6 billion (the "Acquisition"). On May 10, 2005, the Company sold 32,600,000 shares of its common stock in an initial public offering (the "Initial Common Stock Offering") and became a public company.

The Company classifies its business interests into two fundamental areas: recorded music and music publishing. A brief description of those operations is presented below.

The Company's business is seasonal. Therefore, operating results for the three and nine month periods ended June 30, 2006 are not necessarily indicative of the results that may be expected for fiscal 2006.

Recorded Music Operations

The Company's recorded music operations consist of the discovery and development of artists and the related marketing and distribution of recorded music produced by such artists. In addition to the more traditional methods of discovering and developing artists, the Company has implemented new initiatives to identify and nurture artists earlier in the development process and reduce development costs by leveraging its independent distribution network. The Company refers to these new business models as incubator initiatives. Asylum and East West are the current recorded music incubator labels. In addition, the Company launched Cordless Recordings an "e-label" that gives artists the ability to come to market with one or several songs in digital formats without the need to create an entire album. Asylum, East West and Cordless Recordings are a part of the Company's Independent Label Group ("ILG"). The Company has also entered into strategic ventures with other record labels.

The Company's recorded music operations also include a catalog division called Rhino Entertainment ("Rhino"). Rhino specializes in marketing the Company's music catalog through compilations and reissuances of previously released music and video titles, as well as in the licensing of tracks to and from third parties for various uses, including film and television soundtracks.

On May 31, 2006, the Company completed the acquisition of Ryko Corporation ("Ryko"), a leading independent, integrated music and entertainment company. See Note 3.

The Company's principal recorded music distribution operations include Warner-Elektra-Atlantic Corporation ("WEA Corp."), which primarily distributes the Company's music products to retailers and wholesale distributors in the U.S.; a 90% interest in Alternative Distribution Alliance ("ADA"), a distribution company which primarily distributes the products of independent record labels to retailers and wholesale distributors; Ryko Distribution, which distributes music and DVD releases from Rykodisc, Ryco's recorded music label, and third-party record and video labels; various distribution centers and ventures operated internationally; an 80% interest in Word Entertainment, whose distribution operations specialize in the distribution of music products in the Christian retail marketplace; and ADA U.K., which provides ADA's distribution services to independent labels in Europe.

In the U.S., the Company's recorded music operations are conducted principally through its major record labels—Warner Bros. Records Inc. and The Atlantic Records Group. In markets outside the U.S., recorded music activities are conducted through the Warner Music International ("WMI") division and its various subsidiaries, affiliates and non-affiliated licensees.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

The Company plays an integral role in virtually all aspects of the music value chain from discovering and developing talent, to producing albums and promoting artists and their product. After an artist has entered into a contract with one of the Company's record labels, a master recording of the artist's music is created. The recording is then replicated for sale to consumers primarily in CD and digital formats. In the U.S., WEA Corp. and ADA market, sell and deliver products, either directly or through sub–distributors and wholesalers, to thousands of record stores, mass merchants and other retailers throughout the country. Recorded music products are also sold in physical form to Internet physical retailers. In addition, the Internet and wireless networks have become increasingly important sales channels for records in non–physical forms.

Music Publishing Operations

The Company's music publishing business is focused on the exploitation of songs as intellectual property. 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. In addition to the more traditional methods, the Company has implemented new initiatives to promote and develop emerging songwriters. For example, the Company's music publishing business has its own incubator label, Perfect Game Recording Co.

Warner/Chappell is the Company's 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. The music publishing library includes many standard titles that span multiple music genres. Warner/Chappell also administers the music and soundtracks of several third–party television and film producers and studios, including Lucasfilm, Ltd. and Hallmark Entertainment.

The Company also previously owned Warner Bros. Publications ("WBP"), which printed and distributed a broad selection of sheet music, books and educational materials, orchestrations, folios, personality books, and arrangements from the catalogs of Warner/Chappell and other music publishers. On May 31, 2005, the Company sold WBP to Alfred Publishing. See Note 3.

Music publishing revenues are derived from four main sources:

- *Mechanical:* the licensor receives royalties with respect to compositions embodied in recordings sold in any format or configuration, including singles, albums, CDs, digital downloads and mobile phone ringtones.

- *Performance:* the licensor receives royalties when the composition is performed publicly (*e.g.*, broadcast radio and television, movie theater, concert, nightclub or Internet and wireless streaming).

- *Synchronization:* the licensor receives royalties or fees for the right to use the composition in combination with visual images (*e.g.*, in films, television commercials and programs and videogames).

- *Other:* the licensor receives royalties from other uses such as stage productions.

2. Basis of Presentation

Interim Financial Statements

The accompanying consolidated financial statements are unaudited but, in the opinion of management, contain all the adjustments (consisting of those of a normal recurring nature) considered necessary to present

Source: Warner Music Group C, 10-Q, August 03, 2006

fairly the financial position and the results of operations and cash flows for the periods presented in conformity with accounting principles generally accepted in the U.S. ("U.S. GAAP") applicable to interim periods. The accompanying consolidated financial statements should be read in conjunction with the audited consolidated financial statements of the Company included in its Annual Report on Form 10-K for the fiscal year ended September 30, 2005 (Registration No. 001-32502).

Recapitalization

As discussed above, on May 10, 2005, the Company sold 32,600,000 shares of its common stock in the Initial Common Stock Offering. In connection with the Initial Common Stock Offering, the Company (i) converted all its formerly outstanding shares of Class L Common Stock into shares of Class A Common Stock, (ii) renamed all of its formerly outstanding shares of Class A Common Stock as "common stock", which had the effect of eliminating from the Company's authorized capital stock the Class L Common Stock, and Class A Common Stock and (iii) authorized an approximately 1,139 to 1 split of the Company's common stock (collectively, the "Recapitalization").

Accordingly, historical financial statements have been restated to reflect the Recapitalization for all periods occurring after the Acquisition that was effective as of March 1, 2004. Such restatement primarily related to common stock and equivalent shares information, net income per common share computations and stock-based compensation disclosures.

Reclassifications

Certain reclassifications have been made to the prior period's financial information in order to conform to the current period's presentation.

Basis of Consolidation

The consolidated accounts include 100% of the assets, liabilities, revenues, expenses, income, losses and cash flows of the Company and all entities in which the Company has a controlling voting interest and/or variable interest entities required to be consolidated in accordance with U.S. GAAP. Significant intercompany balances and transactions have been eliminated in consolidation.

Short-term Investments

The Company considers all investments with maturities greater than three months, but less than one year, when purchased to be short-term investments. Short-term investments include high-quality, investment grade securities such as taxable auction rate securities as well as commercial paper and corporate bonds. Auction rate securities are classified as available for sale and are carried at fair value. Unrealized gains and losses on such securities are included in accumulated other comprehensive income (loss). Commercial paper and corporate bonds that the Company has both the positive intent and ability to hold to maturity are carried at cost and classified as held to maturity.

Stock-Based Compensation

In December 2004, the Financial Accounting Standards Board (FASB) issued FASB Statement No. 123(R), "Share-Based Payment," ("FAS 123(R)") which revises FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("FAS 123"). FAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized as compensation expense based on their fair value. Effective March 1, 2004, in connection with the Acquisition, the Company adopted the fair value recognition provisions of FAS 123 to account for all stock-based compensation plans adopted subsequent to the Acquisition. Under the fair value

Source: Warner Music Group C, 10-Q, August 03, 2006

recognition provisions of FAS 123, stock-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the vesting period. The Company expenses deferred stock-based compensation on an accelerated basis over the vesting period of the stock award. Effective October 1, 2005, the Company adopted FAS 123(R) using the modified prospective method. There was no impact to the Company's results of operations or financial position as a result of the adoption of FAS 123(R).

Comprehensive (Loss) Income

Comprehensive (loss) income consists of net (loss) income and other gains and losses affecting equity that, under U.S. GAAP, are excluded from net income. For the Company, the components of other comprehensive income primarily consist of foreign currency translation gains and losses and deferred gains and losses on financial instruments designated as hedges under FASB Statement No. 133, "Accounting for Derivative and Hedging Activities", which include interest-rate swaps and foreign exchange contracts. The following summary sets forth the components of comprehensive (loss) income, net of related taxes, for the three and nine months ended June 30, 2006 and 2005 (in millions):

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
Net (loss) income	$ (14)	$ (179)	$ 48	$ (139)
Foreign currency translation gains (losses)	(2)	13	(4)	1
Derivative financial instruments gains	3	—	12	10
Comprehensive (loss) income	$ (13)	$ (166)	$ 56	$ (128)

Net Income (Loss) Per Common Share

The Company computes net income (loss) per common share in accordance with FASB Statement No. 128, "Earnings per Share" ("FAS 128"). Under the provisions of FAS 128, basic net income (loss) per common share is computed by dividing the net income (loss) applicable to common shares after preferred dividend requirements, if any, by the weighted average of common shares outstanding during the period. Diluted net income (loss) per common share adjusts basic net income (loss) per common share for the effects of stock options, warrants and other potentially dilutive financial instruments, only in the periods in which such effect is dilutive.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

The following table sets forth the computation of basic and diluted net income (loss) per common share (in millions, except per share amounts):

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
Basic and diluted net (loss) income per common share:				
Numerator:				
Net (loss) income for basic calculation	$ (14)	$ (179)	$ 48	$ (139)
Net (loss) income for diluted calculation	$ (14)	$ (179)	$ 48	$ (139)
Denominator:				
Weighted average common shares outstanding for basic calculation (a)	143.7	127.0	142.3	114.1
Weighted average common outstanding shares for diluted calculation	143.7	127.0	150.8	114.1
Net income (loss) per common share—basic	$ (0.10)	$ (1.41)	$ 0.34	$ (1.22)
Net income (loss) per common share—diluted	$ (0.10)	$ (1.41)	$ 0.32	$ (1.22)

(a) The denominator excludes the effect of unvested common shares subject to repurchase or cancellation.

The calculation of diluted net income (loss) per common share for each of the periods includes the effects of the assumed exercise of any outstanding stock options or warrants and the assumed vesting of shares of restricted stock where dilutive. The assumed exercise of outstanding stock options and warrants and the assumed vesting of restricted stock represent the following dilutive effect (in millions of shares):

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
Stock options	3.0	3.0	2.8	6.3
Restricted stock	4.5	6.6	5.7	2.2
Warrants	—	—	—	1.5
	7.5	9.6	8.5	10.0

The Company recognized a net loss for the three months ended June 30, 2006, the three months ended June 30, 2005 and the nine months ended June 30, 2005. Therefore, the effects from the assumed exercise of any outstanding stock options or warrants, or the assumed vesting of shares of restricted stock, during such periods would be antidilutive. Accordingly, they have not been included in the presentation of diluted net income (loss) per common share for the respective periods.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.

Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

See Note 19 in the Company's audited consolidated financial statements for the year ended September 30, 2005 for a summary of the terms of the warrants that were issued to Time Warner in connection with the Acquisition. In connection with the Initial Common Stock Offering, the Company repurchased the warrants from Time Warner in May 2005 for approximately $138 million, which approximated fair value at that date.

3. Significant Acquisitions and Dispositions

Acquisition of Ryko Corporation

On May 31, 2006, the Company completed the acquisition of Ryko, a leading independent, integrated music and entertainment company, for approximately $67.5 million in cash. Ryko consists of a recorded music label, Rykodisc, which focuses on a range of contemporary music and comedy releases and numerous film and television soundtracks and Ryko Distribution, which distributes music and DVD releases from Rykodisc as well as from independent third-party record and video labels. Additionally, Ryko owns a catalog of more than 1,000 titles of rock, folk, jazz, world, blues and alternative albums including Restless Records' catalog of punk, new wave and soundtrack recordings. The catalog and roster includes artists such as Frank Zappa, Joe Jackson, Soul Asylum, The Flaming Lips and They Might Be Giants. The transaction was accounted for under the purchase method of accounting, and the results of operations of Ryko are included in the Company's results of operations from the acquisition date of Ryko. The purchase price was preliminarily allocated to the underlying net assets acquired in proportion to the estimated fair value, principally recorded music catalog and goodwill.

Formation of Bad Boy Records LLC

On April 8, 2005, the Company entered into an agreement with an affiliate of Sean "Diddy" Combs to form Bad Boy Records LLC ("Bad Boy"), a joint venture, owned 50% by the Company and 50% by the affiliate. The Company purchased its 50% membership interest in Bad Boy Records LLC for approximately $30 million in cash. Mr. Combs is the CEO of the joint venture and supervises its staff and day-to-day operations. The Company provides funding, marketing, promotion and certain back-office services for the joint venture. The transaction was accounted for under the purchase method of accounting, and the results of operations of Bad Boy are included in the Company's results of operations from its acquisition date.

Sale of Warner Bros. Publications

In May 2005, the Company sold WBP, which conducted the Company's sheet music operations, to Alfred Publishing. As part of the transaction, the Company agreed to license the right to use its music publishing copyrights in the exploitation of printed sheet music and songbooks for a twenty-year period of time. No gain or loss was recognized on the transaction as the historical book basis of the net assets being sold was adjusted to fair value in connection with the accounting for the Acquisition. Due to the Company's continuing involvement with WBP, it was not reported as discontinued operations.

For the three months ended June 30, 2005, the operations sold generated revenues of approximately $8 million; operating income of $1 million; operating income before depreciation and amortization expense of $1 million; and net income of approximately $1 million. For the nine months ended June 30, 2005, the operations sold generated revenues of approximately $34 million; operating income of $1 million; operating income before depreciation and amortization expense of $1 million; and net income of approximately $1 million.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

Acquisition of Maverick Recording Company

In November 2004, the Company acquired an additional 30% interest in Maverick Recording Company ("Maverick") from its existing partner for approximately $17 million and certain amounts previously owed by such partner to the Company, bringing its total interest in Maverick to 80%. The transaction was accounted for under the purchase method of accounting and the purchase price was allocated to the underlying net assets of Maverick in proportion to the estimated fair value, principally artist contracts and recorded music catalog.

On July 14, 2006, the Company acquired the remaining 20% interest in Maverick from its existing partner. The additional purchase price will be allocated to the underlying net assets of Maverick in proportion to the estimated fair value, principally goodwill.

4. Inventories

Inventories consist of the following (in millions):

	June 30, 2006	September 30, 2005
	(unaudited)	(audited)
Compact discs, cassettes and other music-related products	$ 89	$ 84
Published sheet music and song books	2	2
	91	86
Less reserve for obsolescence	(41)	(34)
	$ 50	$ 52

5. Intangible Assets

Intangible assets consist of the following (in millions):

	September 30, 2005	Acquisitions	Other (a)	June 30, 2006
	(audited)			(unaudited)
Intangible assets subject to amortization:				
Record music catalog	$ 1,242	$ 32	$ 6	$ 1,280
Music publishing copyrights	817	16	18	851
Artist contracts	31	5	—	36
Trademarks	10	—	—	10
Other intangible assets	4	—	—	4
	2,104	53	24	2,181
Accumulated amortization	(289)			(435)
Total net intangible assets subject to amortization	1,815			1,746
Intangible assets not subject to amortization:				
Trademarks and brands	100			100
Total net other intangible assets	$ 1,915			$ 1,846

(a) Other represents foreign currency translation adjustments.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

6. Restructuring Costs

Acquisition-Related Restructuring Costs

As of June 30, 2006, the Company had approximately $34 million of liabilities for Acquisition-related restructuring costs that were recognized as part of the cost of the Acquisition. These liabilities represent estimates of future cash obligations for all restructuring activities that have been implemented, as well as for all restructuring activities that have been committed to by management but have yet to occur. The outstanding balance of these liabilities primarily relates to extended payment terms for severance obligations and long-term lease obligations for vacated facilities. These remaining lease obligations are expected to be settled by 2019. The Company expects to pay the majority of the remaining employee termination costs in fiscal 2006.

	Employee Terminations	Other Exit Costs	Total
		(in millions)	
Liability as of September 30, 2005	$ 14	$ 35	$ 49
Cash paid during the nine months ended June 30, 2006	(8)	—	(8)
Non-cash reductions during the nine months ended June 30, 2006 (a)	—	(3)	(3)
Reversal of excess liabilities (b)	(1)	(3)	(4)
Liability as of June 30, 2006	$ 5	$ 29	$ 34

(a) Principally relates to changes in foreign currency exchange rates and the non-cash write-off of the carrying value of advances relating to terminating certain artist, songwriter and co-publisher contracts.

(b) Excess liabilities were reversed through the statement of operations, or were recorded as a reduction of the initial purchase price of the Acquisition.

7. Debt

The Company's long-term debt consists of (in millions):

	June 30, 2006	September 30, 2005
	(unaudited)	(audited)
Senior secured credit facility:		
Revolving credit facility	$ —	$ —
Term loan	1,417	1,430
	1,417	1,430
7.375% U.S. dollar-denominated Senior Subordinated Notes due 2014—Acquisition Corp	465	465
8.125% Sterling-denominated Senior Subordinated Notes due 2014—Acquisition Corp	183	177
9.5% Senior Discount Notes due 2014—Holdings	186	174
Total debt	2,251	2,246
Less current portion	(17)	(17)
Total long term debt	$ 2,234	$ 2,229

The Holdings Refinancing

In December 2004, Holdings issued $847 million principal amount at maturity of debt consisting of (i) $250 million principal amount of Floating Rate Senior Notes due 2011 (the "Holdings Floating Rate Notes"), (ii) $397

Source: Warner Music Group C, 10-Q, August 03, 2006

million principal amount at maturity of 9.5% Senior Discount Notes due 2014, which had an initial issuance discount of $147 million (the "Holdings Discount Notes") and (iii) $200 million principal amount of Floating Rate Senior PIK Notes due 2014 (the "Holdings PIK Notes", and collectively, the "Holdings Notes"), which had an initial discount of $4 million. The gross proceeds of $696 million received from the issuance of the Holdings Notes were used to (i) redeem the remaining shares of cumulative preferred stock of Holdings at a redemption price of $209 million, including $9 million of accrued and unpaid dividends, (ii) pay a return of capital to the Company's shareholders in the aggregate amount of $472 million and (iii) pay debt-related issuance costs of approximately $15 million.

The Holdings Redemption

In June 2005, using proceeds from the Company's Initial Common Stock Offering and approximately $57 million of cash on hand, Holdings redeemed all of the Holdings Floating Rate Notes, all of the Holdings PIK Notes, and 35% of the aggregate outstanding principal at maturity of the Holdings Discount Notes.

The Holdings Discount Notes were issued at a discount and have an initial accreted value of $630.02 per $1,000 principal amount at maturity. Prior to December 15, 2009, no cash interest payments are required. However, interest accrues on the Holdings Discount Notes in the form of an increase in the accreted value of such notes such that the accreted value of the Holdings Discount Notes will equal the principal amount at maturity on December 15, 2009. Thereafter, cash interest on the Holdings Discount Notes is payable semiannually at a fixed rate of 9.5% per annum. The Holdings Discount Notes mature on December 15, 2014. The Company redeemed 35% of the Holdings Discount Notes on June 15, 2005.

In connection with the redemption of the Holdings Floating Rate Notes and 35% of the Holdings Discount Notes, the Company was required to pay redemption premiums of $10 million and $9 million, respectively, which the Company paid on June 15, 2005 and recorded as a loss on the repayment of the notes in the consolidated statement of operations for the three and nine months ended June 30, 2005. The Company also wrote off the remaining balance of debt-issuance costs of $12 million related to the notes redeemed and the remaining unamortized original issue discount of $4 million related to the Holdings PIK Notes. Such amounts, $35 million in the aggregate, were recorded as a loss on the repayment of the notes in the consolidated statement of operations for the three- and nine-month periods ended June 30, 2005.

The Company was also required to pay all accrued interest as of the redemption date related to the Holdings Notes that were redeemed. This amount consisted of $5 million related to the Holdings Floating Rate Notes, $9 million related to the Holdings PIK notes, and $4 million in accreted value of the 35% of the Holdings Discount Notes redeemed. Of such amount, $8 million had been expensed in previous quarters and $10 million was recorded as interest expense in the consolidated statement of operations for the three months ended June 30, 2005.

The Company has fully and unconditionally guaranteed the remaining Holdings Discount Notes. The Holdings Discount Notes are unsecured and subordinated to all of Holdings' existing and future secured debt, including Holdings' guarantee of borrowings by Acquisition Corp. under the Company's senior secured credit facility. In addition, the Holdings Discount Notes are structurally subordinated to the Senior Subordinated Notes of Acquisition Corp.

The indenture governing the Holdings Notes limits Holdings' ability and the ability of its restricted subsidiaries to (i) incur additional indebtedness or issue certain preferred shares, (ii) pay dividends on or make other distributions in respect of its capital stock or make other restricted payments, (iii) make certain

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

investments, (iv) sell certain assets, (v) create liens on certain debt without securing the notes, (vi) consolidate, merge, sell or otherwise dispose of all or substantially all of its assets, (vii) enter into certain transactions with affiliates and (viii) designate its subsidiaries as unrestricted subsidiaries.

Restricted Net Assets

The Company is a holding company that conducts substantially all its business operations through its subsidiary, Acquisition Corp. and its subsidiaries. Accordingly, the ability of the Company to obtain funds from its subsidiaries is restricted by the senior secured credit facility of Acquisition Corp., the indenture for the Acquisition Corp. Senior Subordinated Notes issued by Acquisition Corp. and the indenture for the Holdings Notes.

8. Stock-based Compensation

The following table represents the expense recorded by the Company with respect to its stock-based awards for the three- and nine-month periods ended June 30, 2006 and 2005 by segment and on a consolidated basis (in millions):

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
Recorded Music	$ 3	$ 6	$ 7	$ 12
Music Publishing	—	1	1	2
Corporate expenses	1	2	4	4
Total	$ 4	$ 9	$ 12	$ 18

Certain of the stock options and restricted shares of common stock awarded by the Company vest upon the occurrence of a 3x liquidity event, which is defined with respect to the awards as the occurrence of an event that implies an aggregate value for the equity held by the Investor Group of 3x its initial value, as adjusted for prior dividends or other returns of capital received. In April 2006, the 3x liquidity event, as defined, occurred, which resulted in the vesting of 1,169,932 shares of restricted common stock awarded to or purchased by employees of the Company and 516,719 stock options awarded to employees of the Company. In addition, the Company paid out accrued dividends owed to restricted stockholders of $1.3 million upon the occurrence of the 3x liquidity event and the subsequent vesting of their restricted shares. In accordance with the requirements of FAS 123(R), the Company recognizes the compensation for these awards over the employee's requisite service period. Accordingly, there is no impact of this event to the Company's statement of operations for the three- and nine-month periods ended June 30, 2006.

Payments Relating to Executive Compensation

Concurrent with the Initial Common Stock Offering, the Company determined that certain shares of restricted stock issued in 2004 and early 2005 may have been sold at prices below fair market value on the applicable date of sale and certain options to purchase shares of the Company's stock granted may have had exercise prices below fair market value on the applicable date of grant. As a result, certain U.S. employee holders of the restricted stock who made elections under Section 83(b) of the Internal Revenue Code would be subject to additional ordinary income tax to the extent of the fair market value of the restricted stock received over the purchase price they paid for such stock. In other cases, certain employees who did not make such an election will be subject to higher taxes on their restricted shares at the time of vesting than would have been the case had they

Source: Warner Music Group C, 10-Q, August 03, 2006

purchased the shares for fair market value. In addition, under the provisions of the American Jobs Creation Act of 2004, signed into law in October 22, 2004, U.S. employee option holders whose options vest with exercise prices below fair market value on the date of grant are subject to significant penalties under new Section 409A of the Internal Revenue Code. IRS Notice 2005-1 provides transitional guidance on the application of Section 409A which, among other things, permits options with exercise prices below the fair market value of the underlying stock on the date of grant to be amended or replaced with new options having an exercise price at least equal to the fair market value on the grant date. Non-U.S. employee holders of restricted stock or options may be subject to similar or other related issues. In order for the Company to address these issues the Company's Board of Directors, based on a re-assessment of fair market values on the applicable dates, approved the actions discussed below.

Restricted Stock

The Company was authorized to pay a cash bonus to each employee who purchased restricted stock at prices that were below fair market value on the date of purchase. The bonus was calculated as either an amount equal to the tax liability incurred by the employee on the grant date or an estimate of the additional future tax which would be incurred by the employee upon the vesting of the shares, depending upon the employee's Section 83(b) election. Additionally, the Company paid the employees an amount necessary to pay the related taxes on the bonus. This resulted in total cash payments of approximately $10 million, which the Company expensed in the quarter ended June 30, 2005.

Options

The Company revised the exercise prices of certain options to purchase its common stock to prices equal to the applicable re-determined fair market values of the common stock on the dates of the respective grants. The Company compensated the grantees with a cash bonus representing the loss of value created by this adjustment to the option exercise prices. This resulted in total cash bonuses paid of approximately $9 million. The Company treated the revision of the exercise prices as a modification of these awards and $6 million related to the modification was expensed in the quarter ended June 30, 2005.

Further, in connection with the $100.5 million cash dividend the Company declared and paid to holders of its common stock, consisting of the Investor Group and certain members of management who held shares of common stock prior to the Initial Common Stock Offering, the Company made an adjustment to all options to purchase common stock outstanding at the time of declaration of the dividend. The adjustment consisted of a cash make-whole payment to each option holder equal to the pro-rata amount that would have been received per share had all outstanding options been exercised at the time of the declaration of the dividend. The amounts were adjusted down to reflect a present value discount based on the earliest possible exercise dates. The Company recorded approximately $3 million of expense related to such payments in the quarter ended June 30, 2005.

9. Shareholders' Equity

Return of Capital and Dividends Paid

In September 2004, the Company declared a $342 million dividend to its Class L common shareholders in the form of a note payable. The note payable was paid in October 2004 using proceeds received from a return of capital previously invested in Acquisition Corp.

In connection with the Holdings Refinancing, the Company paid a $465 million return of capital to its Class L common shareholders, of which $422 million was paid in December 2004 and $43 million was paid in March 2005. The remaining $7 million from the Holdings Refinancing was declared and paid as a dividend to the Company's shareholders in May 2005.

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

On October 3, 2005, December 29, 2005, March 14, 2006 and June 7, 2006, the Company declared dividends on its outstanding common stock at a rate of $0.13 per share. The dividends were paid on November 23, 2005, February 17, 2006, May 3, 2006, and July 27, 2006, respectively, except for the portion of the dividends with respect to unvested restricted stock, which will be paid at such time as such shares become vested.

During the nine months ended June 30, 2006, 2,479,501 shares of restricted stock purchased by or awarded to certain employees vested.

10. Commitments and Contingencies

Radio Promotion Activities

On September 7, 2004, November 22, 2004 and March 31, 2005, the Attorney General of the State of New York served the Company with requests for information in connection with an industry–wide investigation of the relationship between music companies and radio stations, including the use of independent promoters and accounting for any such payments. The investigation was pursuant to New York Executive Law §63(12) and New York General Business Law §349, both of which are consumer fraud statutes. On November 22, 2005, the Company reached a settlement with the Attorney General in connection with this investigation. As part of such settlement, the Company agreed to make $5 million in charitable payments and to abide by a list of permissible and impermissible promotional activities. The Attorney General has also reached settlements with all of the other major music companies in connection with this investigation. Two independent labels have filed related antitrust suits against the Company alleging that its radio promotion activities are anticompetitive. *Radikal Records, Inc. v. Warner Music Group, et al.* was filed on March 21, 2006 in U.S. District Court in the Central District of California, Western Division. *TSR Records, Inc. v. Warner Music Group, et al.* was filed on March 28, 2006 in U.S. District Court in the Central District of California, Western Division. The Company filed a Notice of Related Case and was successful in having both of these cases consolidated. On May 23, 2006, the Company filed a Motion to Dismiss in both cases. Decisions on these motions are pending. The Company intends to defend against these lawsuits vigorously, but is unable to predict the outcome of these suits. Any litigation the Company may become involved in as a result of the settlement with the Attorney General, regardless of the merits of the claim, could be costly and divert the time and resources of management.

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 the form of a subpoena duces tecum and subpoena ad testificandum in connection with an industry–wide investigation as to whether the practices of industry participants concerning the pricing of digital music downloads violate Section 1 of the Sherman Act, New York State General Business Law §§ 340 et seq., New York Executive Law §63(12), and related statutes. On February 28, 2006, the U.S. Department of Justice served the Company with a request for information in the form of a Civil Investigative Demand as to whether its activities relating to the pricing of digitally downloaded music violate Section 1 of the Sherman Act (15 U.S.C. Section 1). The Company intends to fully cooperate with the Attorney General's and Department of Justice's industry–wide inquiries. Subsequent to the announcements of the above governmental investigations, a total of twenty–seven putative class action lawsuits concerning the pricing of digital music downloads have been filed. The Company has not yet been served in some of the cases but expects they will all be consolidated into one case. The lawsuits are all based on the same general subject matter as the Attorney General's request for information alleging a conspiracy among record companies to fix prices for downloads, and, accordingly to some of the complaints, protect allegedly inflated prices for compact discs. The complaints generally seek unspecified compensatory, statutory and treble damages. The Company intends to defend against these lawsuits vigorously, but is unable to predict the outcome of these suits. Any litigation the Company may

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

become involved in as a result of the inquiries of the Attorney General and Department of Justice, regardless of the merits of the claim, could be costly and divert the time and resources of management.

Other Matters

In addition to the matters discussed above, the Company is involved in other litigation arising in the normal course of our business. Management does not believe that any legal proceedings pending against the Company will have, individually, or in the aggregate, a material adverse effect on its business. However, the Company cannot predict with certainty the outcome of any litigation or the potential for future litigation. Regardless of the outcome, litigation can have an adverse impact on the Company, including its brand value, because of defense costs, diversion of management resources and other factors.

11. Derivative Financial Instruments

During the nine months ended June 30, 2006, the Company did not enter into additional interest rate swap agreements to hedge the variability of its expected future cash interest payments or any new foreign currency hedge programs. However, the Company extended the terms of certain existing interest rate swap agreements. As of June 30, 2006, the Company had interest rate swap agreements to hedge a total notional debt amount of $897 million and recorded deferred gains in comprehensive income of $21 million. Additionally, as of June 30, 2006 the Company had less than $1 million of deferred net losses in comprehensive income related to foreign currency hedging.

The Company recorded unrealized gains of $17 million on its stock warrants issued to Time Warner in connection with the Acquisition for the nine-months ended June 30, 2005. On May 16, 2005, the Company repurchased the three-year warrants from Time Warner at a cost of approximately $138 million, which approximated fair value at that date.

12. 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 areas: recorded music and music publishing. 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 Company accounts for inter-segment 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 June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(In millions)			
Revenues				
Recorded music	$ 678	$ 588	$ 2,274	$ 2,149
Music publishing	150	161	410	470
Corporate expenses and eliminations	(6)	(7)	(22)	(22)
Total revenues	$ 822	$ 742	$ 2,662	$ 2,597

Source: Warner Music Group C, 10-Q, August 03, 2006

Warner Music Group Corp.
Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(in millions)			
OIBDA				
Recorded music	$ 92	$ 47	$ 379	$ 313
Music publishing	23	28	91	99
Corporate expenses and eliminations	(29)	(108)	(78)	(167)
Total OIBDA	$ 86	$ (33)	$ 392	$ 245

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(in millions)			
Depreciation of Property, Plant and Equipment				
Recorded music	$ 6	$ 7	$ 20	$ 25
Music publishing	—	2	2	4
Corporate expenses and eliminations	4	3	10	11
Total depreciation	$ 10	$ 12	$ 32	$ 40

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(in millions)			
Amortization of Intangibles Assets				
Recorded music	$ 34	$ 34	$ 101	$ 100
Music publishing	14	13	42	40
Corporate expenses and eliminations	—	—	—	—
Total amortization	$ 48	$ 47	$ 143	$ 140

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(in millions)			
Operating Income (Loss)				
Recorded music	$ 52	$ 6	$ 258	$ 188
Music publishing	9	13	47	55
Corporate expenses and eliminations	(33)	(111)	(88)	(178)
Total operating income (loss)	$ 28	$ (92)	$ 217	$ 65

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(in millions)			
Reconciliation of OIBDA to Operating Income (Loss)				
OIBDA	$ 86	$ (33)	$ 392	$ 245
Depreciation expense	(10)	(12)	(32)	(40)
Amortization expense	(48)	(47)	(143)	(140)
Operating income	$ 28	$ (92)	$ 217	$ 65

Warner Music Group Corp.

Notes to Consolidated Interim Financial Statements (Unaudited)—(Continued)

13. Additional Financial Information

Cash Interest and Taxes

The Company made interest payments of approximately $118 million and $129 million during the nine months ended June 30, 2006 and 2005, respectively. The Company paid approximately $49 million and $36 million of income and withholding taxes in the nine months ended June 30, 2006 and 2005, respectively. The Company received $5 million and $8 million of income tax refunds in the nine months ended June 30, 2006 and 2005, respectively.

Non-cash Transactions

There were no significant non-cash investing and financing activities during the nine months ended June 30, 2006 and 2005.

14. Subsequent Event

The major record companies have reached a global out-of-court settlement of international copyright litigation against the operators of the Kazaa peer-to-peer network. Under the terms of the settlement, the Kazaa defendants have agreed to pay $100,000,000 in compensation to the record companies that brought the action. Kazaa will also introduce filtering technologies to prevent the continued infringement in the Kazaa system. The settlement money is being held in escrow until the plaintiffs agree on the proper allocation of the funds. The Company does not know yet what its portion of the settlement will be.

Source: Warner Music Group C, 10-Q, August 03, 2006

WARNER MUSIC GROUP CORP.
Supplementary Information
Condensed Consolidating Financial Statements of Registrant

The Company is the direct parent of Holdings, which is the direct parent of Acquisition Corp.

Holdings has issued and outstanding the Holdings Discount Notes. The Holdings Discount Notes are guaranteed by the Company. These guarantees are full, unconditional, joint and several. The following condensed consolidating financial statements are presented for the information of the holders of the Holdings Discount Notes and present the results of operations, financial position and cash flows of (i) the Company, which is the guarantor of the Holdings Discount Notes, (ii) Holdings, which is the issuer of the Holdings Discount Notes, (iii) the subsidiaries of Holdings (WMG Acquisition Corp. is the only direct subsidiary of Holdings) and (iv) the eliminations necessary to arrive at the information for the Company on a consolidated basis. Investments in consolidated subsidiaries are presented under the equity method of accounting.

The Company and Holdings are holding companies that conduct substantially all their business operations through Acquisition Corp. Accordingly, the ability of the Company to obtain funds from its subsidiaries is restricted by the senior secured credit facility of Acquisition Corp., the indenture for the Senior Subordinated Notes issued by Acquisition Corp. and the indenture for the Holdings Notes.

Source: Warner Music Group C, 10-Q, August 03, 2006

WARNER MUSIC GROUP CORP.
Supplementary Information
Condensed Consolidating Balance Sheet (unaudited)
June 30, 2006

	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(in millions)		
Assets:					
Current assets:					
Cash and equivalents	$ 37	$ —	$ 269	$ —	$ 306
Short-term investments	28	—	1	—	29
Accounts receivable, net	—	—	524	—	524
Due from (to) affiliates	(3)	—	3	—	—
Inventories	—	—	50	—	50
Royalty advances expected to be recouped within one year	—	—	209	—	209
Deferred tax assets	—	—	40	—	40
Other current assets	—	—	47	—	47
Total current assets	62	—	1,143	—	1,205
Royalty advances expected to be recouped after one year	—	—	209	—	209
Investments in and advances to (from) consolidated subsidiaries	46	228	—	(274)	—
Investments	—	—	24	—	24
Property, plant and equipment	—	—	144	—	144
Goodwill	—	—	946	—	946
Intangible assets subject to amortization	—	—	1,746	—	1,746
Intangible assets not subject to amortization	—	—	100	—	100
Other assets	—	4	105	—	109
Total assets	$ 108	$ 232	$ 4,417	$ (274)	$ 4,483
Liabilities and Shareholders' Equity:					
Current liabilities:					
Accounts payable	$ —	$ —	$ 202	$ —	$ 202
Accrued royalties	—	—	1,146	—	1,146
Taxes and other withholdings	—	—	34	—	34
Current portion of long-term debt	—	—	17	—	17
Dividends payable	22	—	—	—	22
Other current liabilities	3	—	333	—	336
Total current liabilities	25	—	1,732	—	1,757
Long-term debt	—	186	2,048	—	2,234
Dividends payable	3	—	—	—	3
Deferred tax liabilities, net	—	—	193	—	193
Other noncurrent liabilities	—	—	216	—	216
Total liabilities	28	186	4,189	—	4,403
Total shareholders' equity	80	46	228	(274)	80
Total liabilities and shareholders' equity	$ 108	$ 232	$ 4,417	$ (274)	$ 4,483

Source: Warner Music Group C, 10-Q, August 03, 2006

WARNER MUSIC GROUP CORP.
Supplementary Information
Condensed Consolidating Balance Sheet (audited)
September 30, 2005

	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(In millions)		
Assets:					
Current assets:					
Cash and equivalents	$ 40	$ 1	$ 247	$ —	$ 288
Accounts receivable, net	—	—	637	—	637
Due from (to) affiliates	15	(23)	8	—	—
Inventories	—	—	52	—	52
Royalty advances expected to be recouped within one year	—	—	190	—	190
Deferred tax assets	—	—	36	—	36
Other current assets	—	—	39	—	39
Total current assets	55	(22)	1,209	—	1,242
Royalty advances expected to be recouped after one year	—	—	190	—	190
Investments in and advances to (from) consolidated subsidiaries	43	235	—	(278)	—
Investments	—	—	21	—	21
Property, plant and equipment	—	—	157	—	157
Goodwill	—	—	869	—	869
Intangible assets subject to amortization	—	—	1,815	—	1,815
Intangible assets not subject to amortization	—	—	100	—	100
Other assets	—	4	100	—	104
Total assets	$ 98	$ 217	$ 4,461	$ (278)	$ 4,498
Liabilities and Shareholders' Equity:					
Current liabilities:					
Accounts payable	$ 1	$ —	$ 246	$ —	$ 247
Accrued royalties	—	—	1,057	—	1,057
Taxes and other withholdings	—	—	23	—	23
Current portion of long-term debt	—	—	17	—	17
Other current liabilities	1	—	403	—	404
Total current liabilities	2	—	1,746	—	1,748
Long-term debt	—	174	2,055	—	2,229
Dividends payable	5	—	—	—	5
Deferred tax liabilities, net	—	—	201	—	201
Other noncurrent liabilities	2	—	224	—	226
Total liabilities	9	174	4,226	—	4,409
Total shareholders' equity	89	43	235	(278)	89
Total liabilities and shareholders' equity	$ 98	$ 217	$ 4,461	$ (278)	$ 4,498

Source: Warner Music Group C, 10-Q, August 03, 2006

WARNER MUSIC GROUP CORP.
Supplementary Information
Condensed Consolidating Statements of Operations (unaudited)
For The Three Months Ended June 30, 2006 and June 30, 2005

	Three months ended June 30, 2006				
	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(In millions)		
Revenues	$ —	$ —	$ 822	$ —	$ 822
Costs and expenses:					
Cost of revenues	—	—	(445)	—	(445)
Selling, general and administrative expenses	—	—	(301)	—	(301)
Amortization of intangible assets	—	—	(48)	—	(48)
Total costs and expenses	—	—	(794)	—	(794)
Operating income	—	—	28	—	28
Interest expense, net	—	(4)	(41)	—	(45)
Equity in the gains (losses) of consolidated subsidiaries	(14)	(10)	—	24	—
Other expense, net	—	—	1	—	1
Income (loss) before income taxes	(14)	(14)	(12)	24	(16)
Income tax expense	—	—	2	—	2
Net (loss) income	$(14)	$ (14)	$ (10)	$ 24	$ (14)

	Three months ended June 30, 2005				
	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(In millions)		
Revenues	$ —	$ —	$ 742	$ —	$ 742
Costs and expenses:					
Cost of revenues	—	—	(396)	—	(396)
Selling, general and administrative expenses	—	—	(318)	—	(318)
Amortization of intangible assets	—	—	(47)	—	(47)
Loss on termination of management fee	—	—	(73)	—	(73)
Total costs and expenses	—	—	(834)	—	(834)
Operating income	—	—	(92)	—	(92)
Interest expense, net	—	(13)	(37)	—	(50)
Equity in the losses of equity-method investees, net	(179)	(131)	—	310	—
Net investment related gains	—	—	1	—	1
Loss on repayment of Holdings debt	—	(35)	—	—	(35)
Other expense, net	—	—	1	—	1
(Loss) income before income taxes	(179)	(179)	(127)	310	(175)
Income tax expense	—	—	(4)	—	(4)
Net (loss) income	$(179)	$ (179)	$ (131)	$ 310	$ (179)

Source: Warner Music Group C, 10-Q, August 03, 2006

WARNER MUSIC GROUP CORP.
Supplementary Information
Condensed Consolidating Statements of Operations (unaudited)
For The Nine Months Ended June 20, 2006 and June 30, 2005

	Nine months ended June 30, 2006				
	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(In millions)		
Revenues	$ —	$ —	$ 2,662	$ —	$ 2,662
Costs and expenses:					
Cost of revenues	—	—	(1,384)	—	(1,384)
Selling, general and administrative expenses	—	—	(918)	—	(918)
Amortization of intangible assets	—	—	(143)	—	(143)
Total costs and expenses	—	—	(2,445)	—	(2,445)
Operating income	—	—	217	—	217
Interest expense, net	—	(12)	(123)	—	(135)
Equity in the gains (losses) of equity method investees	—	—	1	—	1
Equity in the gains (losses) of consolidated subsidiaries	48	60	—	(108)	—
Other income, net	—	—	3	—	3
Income before income taxes	48	48	98	(108)	86
Income tax expense	—	—	(38)	—	(38)
Net income (loss)	$ 48	$ 48	$ 60	$ (108)	$ 48

	Nine months ended June 30, 2005				
	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Warner Music Group Corp. Consolidated
			(In millions)		
Revenues	$ —	$ —	$ 2,597	$ —	$ 2,597
Costs and expenses:					
Cost of revenues	—	—	(1,377)	—	(1,377)
Selling, general and administrative expenses	—	—	(942)	—	(942)
Amortization of intangible assets	—	—	(140)	—	(140)
Loss on termination of management fee	—	—	(73)	—	(73)
Total costs and expenses	—	—	(2,532)	—	(2,532)
Operating income	—	—	65	—	65
Interest expense, net	(1)	(31)	(108)	—	(140)
Net investment-related gains	—	—	1	—	1
Equity in the losses of equity-method investees, net	(155)	(84)	(1)	239	(1)
Loss on repayment of Holdings debt	—	(35)	—	—	(35)
Unrealized gain on warrant	17	—	—	—	17
Minority interest expense	—	(5)	—	—	(5)
Other expense, net	—	—	5	—	5
(Loss) income before income taxes	(139)	(155)	(38)	239	(93)
Income tax expense	—	—	(46)	—	(46)
Net (loss) income	$(139)	$ (155)	$ (84)	$ 239	$ (139)

Source: Warner Music Group C, 10-Q, August 03, 2006

WARNER MUSIC GROUP CORP.
Supplementary Information
Condensed Consolidating Statement of Cash Flows (unaudited)
For The Nine Months Ended June 30, 2006

	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Consolidated
			(in millions)		
Cash flows from operating activities:					
Net income	$ 48	$ 48	$ 60	$ (108)	$ 48
Adjustments to reconcile net income to net cash provided by (used in) operating activities:					
Depreciation and amortization	—	—	175	—	175
Non-cash interest expense	—	12	27	—	39
Non-cash stock compensation expense	—	—	12	—	12
Deferred taxes	—	—	(17)	—	(17)
Equity in the losses of equity-method investees, including distributions	—	—	(1)	—	(1)
Equity in the losses of consolidated subsidiaries	(48)	(60)	—	108	—
Changes in operating assets and liabilities:					
Accounts receivable	—	—	121	—	121
Inventories	—	—	3	—	3
Royalty advances	—	—	(54)	—	(54)
Accounts payable and accrued liabilities	—	—	(81)	—	(81)
Other balance sheet changes	(2)	—	(20)	—	(22)
Net cash (used in) provided by operating activities	(2)	—	225	—	223
Cash flows from investing activities:					
Investments and acquisitions	—	—	(95)	—	(95)
Investments in short term investments	(28)	—	(1)	—	(29)
Capital expenditures	—	—	(18)	—	(18)
Net cash used in investing activities	(28)	—	(114)	—	(142)
Cash flows from financing activities:					
Quarterly debt repayments	—	—	(13)	—	(13)
Capital contributions received/paid	(3)	3	—	—	—
Increase in intercompany	3	(8)	5	—	—
Returns of capital and dividends paid	27	4	(86)	—	(55)
Net cash provided by (used in) financing activities	27	(1)	(94)	—	(68)
Effect of foreign currency exchange rate changes on cash	—	—	5	—	5
Net increase (decrease) in cash and equivalents	(3)	(1)	22	—	18
Cash and equivalents at beginning of period	40	1	247	—	288
Cash and equivalents at end of period	$ 37	$ —	$ 269	$ —	$ 306

Source: Warner Music Group C, 10-Q, August 03, 2006

WARNER MUSIC GROUP CORP.
Supplementary Information
Condensed Consolidating Statement of Cash Flows (unaudited)
For The Nine Months Ended June 30, 2005

	Warner Music Group Corp.	WMG Holdings Corp. (Issuer)	WMG Acquisition Corp.	Eliminations	Consolidated
			(in millions)		
Cash flows from operating activities:					
Net loss	$ (139)	$ (155)	$ (84)	$ 239	$ (139)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:					
Depreciation and amortization	—	—	180	—	180
Deferred taxes	—	—	(7)	—	(7)
Loss on repayment of debt	—	35	—	—	35
Non-cash interest expense	—	26	26	—	52
Non-cash stock compensation expense			18		18
Net investment-related gains			(1)		(1)
Equity in the losses of equity-method investees, including distributions	155	84	1	(239)	1
Minority interest	—	5	—	—	5
Unrealized gain on warrant	(17)	—	—	—	(17)
Changes in operating assets and liabilities:					
Accounts receivable	—	—	77	—	77
Inventories	—	—	6	—	6
Royalty advances	—	—	(2)	—	(2)
Accounts payable and accrued liabilities	—	—	(22)	—	(22)
Other balance sheet changes	1	2	(17)	—	(14)
Net cash provided by (used in) operating activities	—	(3)	175	—	172
Cash flows from investing activities:					
Investments and acquisitions	—	—	(84)	—	(84)
Investment proceeds	—	—	50	—	50
Capital expenditures	—	—	(20)	—	(20)
Net cash used in investing activities	—	—	(54)	—	(54)
Cash flows from financing activities:					
Borrowings, net of financing costs	—	679	247	—	926
Debt repayments		(574)	(10)	—	(584)
Capital contributions	(590)	517	73	—	—
Proceeds from the issuance of common stock	554	—	—	—	554
Costs to issue common stock	(27)	—	—	—	(27)
Repurchase of warrants	(126)	(12)	—	—	(138)
Repurchase of subsidiary preferred stock	—	(200)	—	—	(200)
Dividends paid to minority interest shareholders	—	(9)	—	—	(9)
Proceeds from the issuance of restricted shares	1	—	—	—	1
Return of capital received	1,157	742	—	(1,899)	—
Return of capital paid	(917)	(1,157)	(742)	1,899	(917)
Change in inter-company	(12)	18	(6)	—	—
Loan to third party	—	—	(10)	—	(10)
Other	—	—	(3)	—	(3)
Net cash provided by (used in) financing activities	40	4	(451)	—	(407)
Effect of foreign currency exchange rate changes on cash		—	(1)	—	(1)
Net increase (decrease) in cash and equivalents	40	1	(331)	—	(290)
Cash and equivalents at beginning of period	—	—	555	—	555
Cash and equivalents at end of period	$ 40	$ 1	$ 224	$ —	$ 265

Source: Warner Music Group C, 10-Q, August 03, 2006

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

You should read the following discussion of our results of operations and financial condition with the unaudited interim financial statements included elsewhere in this Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2006 (the "Quarterly Report"). This discussion contains forward-looking statements and involves numerous risks and uncertainties. Actual results may differ materially from those contained in any forward-looking statements.

We make available on our Internet website free of charge our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K as soon as practicable after we electronically file such reports with the Securities and Exchange Commission (the "SEC"). Our website address is www.wmg.com. The information contained in our website is not incorporated by reference in this Quarterly Report.

"SAFE HARBOR" STATEMENT UNDER PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This Quarterly Report includes "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements other than statements of historical facts included in this Quarterly Report, including, without limitation, statements regarding our future financial position, business strategy, budgets, projected costs, savings and plans and objectives of management for future operations, are forward-looking statements. In addition, forward-looking statements generally can be identified by the use of forward-looking terminology such as "may," "will," "expect," "intend," "estimate," "anticipate," "believe" or "continue" or the negative thereof or variations thereon or similar terminology. Such statements include, among others, statements regarding our ability to develop talent and attract future talent, to reduce future capital expenditures, to monetize our music content, including through new distribution channels and formats, to effectively deploy our capital, the development of digital music and the effect of digital distribution channels on our business, including whether or not the Internet will become an important sales channel and whether we will be able to achieve higher margins from digital sales, our success in limiting piracy, our ability to compete in the highly competitive markets in which we operate, the growth of the music industry and the effect of our and the music industry's efforts to combat piracy on the industry, our intention to pay regular quarterly dividends, the adequacy of our existing sources of cash to support our existing operations the next twelve months, the effect of litigation and other investigations on us and the impact of recent developments regarding EMI Group plc ("EMI") and Sony BMG Music Entertainment ("Sony BMG") on us. Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to have been correct.

There are a number of risks and uncertainties that could cause our actual results to differ materially from the forward-looking statements contained in this Quarterly Report. Additionally important factors could cause our actual results to differ materially from the forward-looking statements we make in this Quarterly Report. As stated elsewhere in this Quarterly Report, such risks, uncertainties and other important factors include, among others:

- the impact of our substantial leverage on our ability to raise additional capital to fund our operations, on our ability to react to changes in the economy or our industry and on our ability to meet our obligations under our indebtedness;

- the decline over the past five years in the global physical recorded music industry and the rate of overall decline in the music industry;

- our ability to continue to identify, sign and retain desirable talent at manageable costs;

- the threat posed to our business by piracy of music by means of home CD-R activity and Internet peer-to-peer file-sharing;

Source: Warner Music Group C, 10-Q, August 03, 2006

- the significant threat posed to our business and the music industry by organized industrial piracy;
- the popular demand for particular recording artists and/or songwriters and albums and the timely completion of albums by major recording artists and/or songwriters;
- the diversity and quality of our portfolio of songwriters;
- the diversity and quality of our album releases;
- significant fluctuations in our results of operations and cash flows due to the nature of our business;
- our involvement in intellectual property litigation;
- the possible downward pressure on our pricing and profit margins;
- the seasonal and cyclical nature of recorded music sales;
- our ability to continue to enforce our intellectual property rights in digital environments;
- the ability to develop a successful business model applicable to a digital environment;
- the ability to maintain product pricing in a competitive environment;
- the impact of heightened and intensive competition in the recorded music and music publishing businesses and our inability to execute our business strategy;
- risks associated with our non-U.S. operations, including limited legal protections of our intellectual property rights and restrictions on the repatriation of capital;
- the impact of legitimate music distribution on the Internet or the introduction of other new music distribution formats;
- the impact of rate regulations on our music publishing business;
- the impact of rates on other income streams that may be set by arbitration proceedings on our business;
- risks associated with the fluctuations in foreign currency exchange rates;
- our ability and the ability of our joint venture partners to operate our existing joint ventures satisfactorily;
- the enactment of legislation limiting the terms by which an individual can be bound under a "personal services" contract;
- potential loss of catalog if it is determined that recording artists have a right to recapture recordings under the U.S. Copyright Act;

- changes in law and government regulations;
- legal or other developments related to pending litigation or investigations by the Attorney General of the State of New York and the Department of Justice;
- trends that affect the end uses of our musical compositions (which include uses in broadcast radio and television, film and advertising businesses);
- the growth of other products that compete for the disposable income of consumers;
- risks inherent in relying on one supplier for manufacturing, packaging and distribution services in North America and Europe;
- risks inherent in our acquiring or investing in other businesses;
- the possibility that our owners' interests will conflict with ours or yours;
- our ability to act as a stand-alone company;

Source: Warner Music Group C, 10-Q, August 03, 2006

- increased costs and diversion of resources associated with complying with the internal control reporting or other requirements of Sarbanes–Oxley;
- weaknesses in our internal controls related to U.S. royalties that could affect our ability to ensure reliable financial reports;
- the effects associated with the formation of Sony BMG; and
- failure to attract and retain key personnel.

There may be other factors not presently known to us or which we currently consider to be immaterial that may cause our actual results to differ materially from the forward–looking statements.

All forward–looking statements attributable to us or persons acting on our behalf apply only as of the date of this Quarterly Report and are expressly qualified in their entirety by the cautionary statements included in this Quarterly Report. We disclaim any duty to publicly update or revise forward–looking statements to reflect events or circumstances after the date made or to reflect the occurrence of unanticipated events.

INTRODUCTION

Warner Music Group Corp. (the "Company") was formed by a private equity consortium of Investors (the "Investor Group") 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 content companies and the successor to substantially all of the interests of the recorded music and music publishing businesses of Time Warner Inc. ("Time Warner"). Effective March 1, 2004, Acquisition Corp. acquired such interests from Time Warner for approximately $2.6 billion (the "Acquisition").

The Company and Holdings are holding companies that conduct substantially all of their business operations through their subsidiaries. The terms "we," "us," "our," "ours," and the "Company" refer collectively to Warner Music Group Corp. and its consolidated subsidiaries, except where otherwise indicated.

Management's discussion and analysis of results of operations and financial condition ("MD&A") is provided as a supplement to the unaudited financial statements and footnotes included elsewhere herein to help provide an understanding of our financial condition, changes in financial condition and results of our operations. MD&A is organized as follows:

- *Overview.* This section provides a general description of our business, as well as recent developments that we believe are important in understanding our results of operations and financial condition and in anticipating future trends.
- *Results of operations.* This section provides an analysis of our results of operations for the three and nine months ended June 30, 2006 and 2005. This analysis is presented on both a consolidated and segment basis.
- *Financial condition and liquidity.* This section provides an analysis of our cash flows for the nine months ended June 30, 2006 and 2005, as well as a discussion of our financial condition and liquidity as of June 30, 2006. The discussion of our financial condition and liquidity includes (i) our available financial capacity under the revolving credit portion of our senior secured credit facility and (ii) a summary of our key debt compliance measures under our debt agreements.

Use of OIBDA

We evaluate our operating performance based on several factors, including our primary financial measure of operating income (loss) before non–cash depreciation of tangible assets and non–cash amortization of intangible assets (which we refer to as "OIBDA"). We consider OIBDA to be an important indicator of the operational strengths and performance of our businesses, including the ability to provide cash flows to service debt.

Source: Warner Music Group C, 10-Q, August 03, 2006

However, a limitation of the use of OIBDA as a performance measure is that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in our businesses. Accordingly, OIBDA should be considered in addition to, not as a substitute for, operating income (loss), net income (loss) and other measures of financial performance reported in accordance with U.S. GAAP.

OVERVIEW

Description of Business

We are one of the world's major music content companies. We classify our business interests into two fundamental areas: Recorded Music and Music Publishing. A brief description of each of those operations is presented below.

Our business is seasonal. Therefore, operating results for the three- and nine-month periods ended June 30, 2006 are not necessarily indicative of the results that may be expected for fiscal 2006.

Recorded Music Operations

Our Recorded Music business consists of the discovery and development of artists and the related marketing, distribution and licensing of recorded music produced by such artists. In the U.S., our operations are conducted principally through our major record labels—Warner Bros. Records Inc. and The Atlantic Records Group. Internationally, our Recorded Music operations are conducted through our Warner Music International division ("WMI"), which includes various subsidiaries, affiliates and non-affiliated licensees in more than 50 countries outside the U.S. In addition to the more traditional methods of discovering and developing artists, we have implemented new initiatives to identify and nurture artists earlier in the development process and reduce development costs by leveraging our independent distribution network. We refer to these new business models as incubator initiatives. Asylum and East West are the current recorded music incubator labels. In addition, we have launched Cordless Recordings, an "e-label" that gives its artists the ability to come to market with one or several songs in the digital formats without the need to create an entire album. Asylum, East West and Cordless Recordings are a part of our Independent Label Group ("ILG"). We have also entered into strategic ventures with other record labels.

Our Recorded Music operations also include a catalog division named Rhino Entertainment ("Rhino"). Rhino specializes in marketing our music catalog through compilations and reissuances of previously released music and video titles, as well as in the licensing of recordings to and from third parties for various uses, including film and television soundtracks.

On May 31, 2006, we completed our acquisition of Ryko Corporation, a leading independent, integrated music and entertainment company.

Our principal Recorded Music distribution operations include Warner-Elektra-Atlantic Corporation ("WEA Corp."), which primarily markets and sells music products to retailers and wholesale distributors in the U.S.; a 90% interest in Alternative Distribution Alliance, a distribution company that primarily distributes the products of independent labels to retail and wholesale distributors in the U.S.; Ryko Distribution, which distributes music and DVD releases from Rykodisc, Ryko's record music label, and third-party record and video labels, various distribution centers and ventures operated internationally; an 80% interest in Word Entertainment, whose distribution operations specialize in the distribution of music products in the Christian retail marketplace; and ADA U.K., which provides ADA's distribution services to independent labels in Europe.

Our principal recorded music revenue sources are sales of CDs, digital downloads and other recorded music products and license fees received for the ancillary uses of our recorded music catalog. The principal costs associated with our Recorded Music operations are as follows:

- artist and repertoire costs—the costs associated with (i) signing and developing artists, (ii) creating master recordings in the studio, (iii) creating artwork for album covers and liner notes and (iv) paying royalties to artists, producers, songwriters, other copyright holders and trade unions;

Source: Warner Music Group C, 10-Q, August 03, 2006

- manufacturing, packaging and distribution costs—the costs to manufacture and distribute product to wholesale and retail distribution outlets;

- marketing and promotion costs—the costs associated with the promotion of artists and recorded music products, including costs to produce music videos for promotional purposes and artist tour support; and

- administration costs—the costs associated with general overhead and other administrative costs, as well as costs associated with anti-piracy initiatives.

Music Publishing Operations

Our Music Publishing operations include Warner/Chappell Music, Inc. and its wholly owned subsidiaries, and certain other music publishing affiliates. We own or control the rights to more than one million musical compositions, including numerous pop music hits, American standards, folk songs and motion picture and theatrical compositions. Our Music Publishing operations also formerly included Warner Bros. Publications ("WBP"), which marketed printed versions of our music throughout the world. On May 31, 2005, we sold WBP to Alfred Publishing. In addition to the more traditional methods, we have implemented new initiatives to promote and develop emerging songwriters. For example, our music publishing business has its own incubator label, Perfect Game Recording Co.

Publishing revenues are derived from four main sources:

- *Mechanical:* the licensor receives royalties with respect to compositions embodied in recordings sold in any format or configuration, including singles, albums, CDs, digital downloads and mobile phone ringtones.

- *Performance:* the licensor receives royalties if the composition is performed publicly (e.g., broadcast radio and television, movie theater, concert, nightclub or Internet and wireless streaming).

- *Synchronization:* the licensor receives royalties or fees for the right to use the composition in combination with visual images (e.g., in films, television commercials and programs and videogames).

- *Other:* the licensor receives royalties from other uses such as stage productions.

The principal costs associated with our Music Publishing operations are as follows:

- artist and repertoire costs—the costs associated with (i) signing and developing songwriters and (ii) paying royalties to songwriters, co-publishers and other copyright holders in connection with income generated from the exploitation of their copyrighted works; and

- administration costs—the costs associated with general overhead and other administrative costs.

Recent Developments

EMI

On May 1, 2006, EMI made an unsolicited proposal to acquire the Company for $28.50 per share (consisting of $20 per share in cash and $8.50 per share in EMI stock). Our board unanimously rejected that proposal on May 2, 2006, determining that it was not in the best interests of our shareholders. On June 14, 2006, we made a proposal to purchase EMI for 315 pence per share in cash. EMI rejected that proposal on June 23, 2006, when it made its revised proposal to acquire us for $31 per share in cash. On June 27, 2006, our board unanimously rejected EMI's revised proposal, determining that it was not in the best interests of our shareholders. We simultaneously made a revised proposal to purchase EMI for 320 pence per share in cash. On June 28, 2006, EMI rejected our revised proposal. On July 13, 2006, the European Court of First Instance annulled the European Commission's decision approving the formation of Sony BMG. Sony and Bertelsmann

Source: Warner Music Group C, 10-Q, August 03, 2006

will now have to re–apply to the European Commission to seek clearance for the formation of Sony BMG and the European Commission will have to re–examine the combination. As a result of this re–examination, the European Commission could clear the transaction without conditions, clear the transaction with conditions or block the transaction forcing Sony BMG to unwind. In the interim, the European Commission, Sony or Bertelsmann can appeal the ruling to the European Court of Justice. We cannot predict what actions will be taken by the European Commission, Sony or Bertelsmann as a result of the ruling or the outcome or timing of the European Commission's re–examination of Sony BMG or the appeal of the ruling. On July 27, 2006, EMI announced that, against this backdrop, the Board of EMI has decided not to pursue a combination with us for the time being. The EMI Board noted that it will review this position in the light of future developments. Later on July 27, 2006, we announced that the ruling of the European Court of First Instance regarding Sony BMG had created uncertainty regarding a potential combination of us and EMI. We further announced that we would monitor the situation carefully, but until matters become clearer, for instance as a result of the re–review of Sony BMG by the European Commission or through an appeal to the European Court of Justice, we did not believe that it would be prudent to pursue a combination of us and EMI. Accordingly, we do not intend to make an offer for EMI at this time. There can be no certainty that any transaction between the two companies will take place.

Factors Affecting Results of Operations and Financial Condition

Market Factors

Over the past five years, the recorded music industry has been unstable, which has adversely affected our operating results. The industry–wide decline can be attributed primarily to digital piracy. Other drivers of this decline are the bankruptcies of record retailers and wholesalers, growing competition for consumer discretionary spending and retail shelf space and the maturation of the CD format, which has slowed the historical growth pattern of recorded music sales. However, new avenues for selling recorded music product have been created, including the legal downloading of digital music using the Internet and DVD–Audio formats and the distribution of music on mobile devices, and revenue streams from these new sources are beginning to emerge. As reported by the International Federation of the Phonographic Industry (IFPI), sales of music via the Internet and mobile phones generated sales of $1.1 billion for record companies in 2005, up from $380 million in the prior–year. As of July 30, 2006, year–to–date U.S. recorded music sales (excluding sales of digital tracks) are down approximately 5.5% year–over–year. However, sales of music through new avenues are beginning to offset the declines seen in prior–years. It is too soon to determine if the industry has stabilized or the impact of sales of music through new channels might have on the industry and the recorded music industry performance may continue to negatively impact our operating results. In addition, a declining recorded music industry could continue to have an adverse impact on the music publishing business. This is because our music publishing business generates a significant portion of its revenues from mechanical royalties received from the sale of music in CD and other recorded music formats.

Restructuring

Due in part to the development of the new channels mentioned above and ongoing anti–piracy initiatives, we believe that the recorded music industry is positioned to improve over the coming years. However, the industry may relapse into a period of decline. In addition, there can be no assurances as to the timing or the extent of any improvement in the industry. Accordingly, in connection with the Acquisition, we executed a number of cost–saving initiatives in an attempt to realign our cost structure with the changing economics of the industry. These initiatives, primarily implemented in fiscal 2004 and the first half of fiscal 2005, included significant headcount reductions from the consolidation of operations and the streamlining of corporate and label overhead, exiting certain leased facilities in an effort to consolidate locations and the sale of our manufacturing, packaging and physical distribution operations. We completed substantially all of our restructuring efforts in fiscal 2005.

Initial Common Stock Offering

In May 2005, we completed the initial public offering of our common stock (the "Initial Common Stock Offering"). Prior to the consummation of the Initial Common Stock Offering, we, among other things, renamed all of our outstanding shares of Class A Common Stock as common stock and authorized an approximately 1,139 for 1 split of our common stock. We contributed the net proceeds from the Initial Common Stock Offering of

Source: Warner Music Group C, 10-Q, August 03, 2006

$517 million to Holdings as an equity capital contribution. Holdings used all of such funds and approximately $57 million of cash received through dividends from Acquisition Corp. to redeem its outstanding notes as discussed below.

In addition, in connection with the Initial Common Stock Offering, we, among other things, repurchased the warrants issued as part of the initial purchase price consideration for the Acquisition from Time Warner for $138 million, we declared and paid a dividend to our stockholders prior to the Initial Common Stock Offering of $100.5 million, terminated a management agreement with the Investor Group as discussed below, borrowed an additional $250 million under the term loan portion of our senior secured credit facility and paid a $10 million cash bonus to our employees.

Payments Relating to Executive Compensation

Concurrent with the Initial Common Stock Offering, we determined that certain shares of restricted stock issued in 2004 and early 2005 may have been sold at prices below fair market value on the applicable date of sale and certain options to purchase shares of our stock granted may have had exercise prices below fair market value on the applicable date of grant. As a result, certain U.S. employee holders of the restricted stock who made elections under Section 83(b) of the Internal Revenue Code would be subject to additional ordinary income tax to the extent of the fair market value of the restricted stock received over the purchase price they paid for such stock. In other cases, certain employees who did not make such an election will be subject to higher taxes on their restricted shares at the time of vesting than would have been the case had they purchased the shares for fair market value. In addition, under the provisions of the American Jobs Creation Act of 2004, signed into law in October 22, 2004, U.S. employee option holders whose options vest with exercise prices below fair market value on the date of grant are subject to significant penalties under new Section 409A of the Internal Revenue Code. IRS Notice 2005–1 provides transitional guidance on the application of Section 409A which, among other things, permits options with exercise prices below the fair market value of the underlying stock on the date of grant to be amended or replaced with new options having an exercise price at least equal to the fair market value on the grant date. Non–U.S. employee holders of restricted stock or options may be subject to similar or other related issues. In order for us to address these issues our Board of Directors, based on a re–assessment of fair market values on the applicable dates, approved the actions discussed below.

Restricted Stock. We were authorized to pay a cash bonus to each employee who purchased restricted stock at prices that were below fair market value on the date of purchase. The bonus was calculated as either an amount equal to the tax liability incurred by the employee at the grant date or an estimate of the additional tax which would be incurred by the employee upon vesting of the shares, depending upon the employee's Section 83(b) election. Additionally, we paid the employees an amount necessary to pay the related taxes on the bonus. This resulted in total cash payments of approximately $10 million, which we expensed in the quarter ended June 30, 2005.

Options. We revised the exercise prices of certain options to purchase our common stock to prices equal to the applicable re–determined fair market values of the common stock on the dates of the respective grants. We compensated the grantees with a cash bonus representing the loss of value created by this adjustment to the option exercise prices. This resulted in total cash bonuses paid of approximately $9 million. The revision of the exercise prices was treated as a modification of these awards and $6 million related to this modification was expensed in the quarter ended June 30, 2005.

Further, in connection with the $100.5 million cash dividend we declared and paid to holders of our common stock, consisting of the Investor Group and certain members of management who held shares of common stock prior to the Initial Common Stock Offering, we made an adjustment to all options to purchase common stock outstanding at the time of declaration of the dividend. The adjustment consisted of a cash make– whole payment to each option holder equal to the pro–rata amount that would have been received per share had all outstanding options been exercised at the time of the declaration of the dividend. The amounts were adjusted down to reflect a present value discount based on the earliest possible exercise dates. We recorded approximately $3 million of expense related to such payments in the quarter ended June 30, 2005.

Source: Warner Music Group C, 10-Q, August 03, 2006

Holdings Refinancing and Redemption

In December 2004, Holdings issued $847 million principal amount of debt. The $847 million principal amount of Holdings' debt consisted of (i) $250 million principal amount of Floating Rate Senior Notes due 2011 (the "Holdings Floating Rate Notes"), (ii) $397 million principal amount at maturity of 9.5% Senior Discount Notes due 2014, which had an initial issuance discount of $147 million (the "Holdings Discount Notes") and (iii) $200 million principal amount of Floating Rate Senior PIK Notes due 2014 (the "Holdings PIK Notes", and collectively, the "Holdings Notes").

In connection with the Initial Common Stock Offering, we used $517 million of proceeds from the offering along with $57 million of available cash to redeem certain of the Holdings Notes outstanding. As of June 30, 2006, Holdings had $186 million of debt on its balance sheet relating to such securities, net of issuance discounts.

The Holdings Floating Rate Notes were redeemed in full on June 15, 2005. From the issuance date through the redemption date, the notes bore interest at a quarterly floating rate based on three-month LIBOR rates plus a margin equal to 4.375%. Interest was payable quarterly in cash beginning on March 15, 2005.

The Holdings Discount Notes were issued at a discount and had an initial accreted value of $630.02 per $1,000 principal amount at maturity. Prior to December 15, 2009, no cash interest payments are required. However, interest accrues on the Holdings Discount Notes in the form of an increase in the accreted value of such notes such that the accreted value of the Holdings Discount Notes will equal the principal amount at maturity on December 15, 2009. Thereafter, cash interest on the Holdings Discount Notes is payable semiannually at a fixed rate of 9.5% per annum. The Holdings Discount Notes mature on December 15, 2014. The Company redeemed 35% of the Holdings Discount Notes on June 15, 2005.

The Holdings PIK Notes were redeemed in full on June 15, 2005. From the date of issuance through the date of redemption, the notes bore interest at a semi-annual floating rate based on six-month LIBOR rates plus a margin equal to 7%. Interest was accrued in the form of additional PIK notes at the election of the Company. Such amounts were also repaid in connection with the redemption.

In connection with the redemption of the Holdings Floating Rate Notes and 35% of the Holdings Discount Notes, we were required to pay redemption premiums of $10 million and $9 million, respectively, which the we paid on June 15, 2005 and recorded as a loss on the repayment of the notes in the consolidated statement of operations for the three and nine months ended June 30, 2005. We also wrote off the remaining balance of debt-issuance costs of $12 million related to the notes redeemed and the remaining unamortized original issue discount of $4 million related to the Holdings PIK Notes. Such amounts $35 million in the aggregate, were recorded as a loss on the repayment of the notes in the consolidated statement of operations for the three months and nine ended June 30, 2005.

Termination of Management/Monitoring Agreement

As described in Note 20 to our audited consolidated financial statements for the year ended September 30, 2005, we entered into a management monitoring agreement (the "Management Agreement") with the Investor Group in connection with the Acquisition.

Under the Management Agreement, we were required to pay the Investor Group an aggregate annual fee of $10 million per year (the "Periodic Fees") in consideration for ongoing consulting and management advisory services.

The Management Agreement provided that it would continue in full force and effect until December 30, 2014, provided, however, that the Investor Group could cause the agreement to terminate at any time. In the event of the termination of the Management Agreement, the Company, Holdings and Acquisition Corp. were required by the terms of the agreement to pay each of the Investor Group any unpaid portion of the Periodic Fees,

Source: Warner Music Group C, 10-Q, August 03, 2006

any Subsequent Fees and any expenses due with respect to periods prior to the date of termination plus the net present value (using a discount rate equal to the then yield on U.S. Treasury Securities of like maturity) of the Periodic Fees that would have been payable with respect to the period from the date of termination until December 30, 2014.

The Investor Group terminated the Management Agreement and on May 16, 2005, we paid the Investor Group a $73 million termination fee, which was reflected in our statement of operations for the three and nine months ended June 30, 2005. As a result, certain fees paid in prior periods do not appear in subsequent periods. We paid $1 million and $6 million of Periodic Fees under the Management Agreement during the three and nine months ended June 30, 2005, respectively. We no longer pay any Periodic Fees following the termination of the agreement.

Sale of Warner Bros. Publications

In May 2005, we sold WBP, which conducted our sheet music operations, to Alfred Publishing. No gain or loss was recognized on the transaction, as the historical book basis of the net assets being sold was adjusted to fair value in connection with the accounting for the Acquisition. Due to our continuing involvement with WBP, it was not reported as discontinued operations. For the three months ended June 30, 2005, the operations sold generated revenues of approximately $8 million; operating income of $1 million; operating income before depreciation and amortization expense of $1 million; and net income of approximately $1 million. For the nine months ended June 30, 2005, the operations sold generated revenues of approximately $34 million; operating income of $1 million; operating income before depreciation and amortization expense of $1 million; and net income of approximately $1 million.

RESULTS OF OPERATIONS

Three Months Ended June 30, 2006 Compared to Three Months Ended June 30, 2005

The following table summarizes our historical results of operations:

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)
	(In millions)	
Revenues	$ 822	$ 742
Costs and expenses:		
Cost of revenues	(445)	(396)
Selling, general and administrative expenses (1)	(301)	(318)
Amortization of intangible assets	(48)	(47)
Loss on termination of management agreement	—	(73)
Total costs and expenses	(794)	(834)
Operating income (loss)	28	(92)
Interest expense, net	(45)	(50)
Net investment-related gains	—	1
Loss on repayment of Holdings Notes	—	(35)
Other income, net	1	1
Loss before income taxes	$ (16)	$ (175)
Income tax benefit (expense)	2	(4)
Net loss	$ (14)	$ (179)

(1) Includes depreciation expense of $10 million and $12 million for the three months ended June 30, 2006 and 2005, respectively.

Source: Warner Music Group C, 10-Q, August 03, 2006

Consolidated Historical Results

Revenues

Our revenues increased $80 million, or 11%, to $822 million for the three months ended June 30, 2006 as compared to $742 million for the three months ended June 30, 2005. Excluding a $4 million unfavorable impact of foreign currency exchange rates and prior–year revenue of $8 million related to our sheet music business, which was sold in May 2005, total revenue increased by $92 million or 13%. Recorded Music revenues increased by $90 million, to $678 million for the three months ended June 30, 2006. Excluding a $4 million unfavorable impact of foreign currency exchange rates, Recorded Music revenues rose $94 million, or 16%, comprised of a $44 million increase in physical sales and a $50 million increase in digital sales. Music Publishing revenues declined by $11 million to $150 million for the three months ended June 30, 2006. Excluding $8 million of prior–year revenue related to our sheet music business sold in May 2005, Music Publishing revenue declined $3 million or 2%. International operations represented $416 million of consolidated revenues for the three months ended June 30, 2006 as compared to $375 million for the three months ended June 30, 2005, comprising 51% of total revenues for each period.

Overall digital revenues grew to $92 million for the three months ended June 30, 2006, as compared to $90 million for the three months ended March 31, 2006 and $44 million for the three months ended June 30, 2005. Digital revenues represented 11% of consolidated revenues for the three months ended June 30, 2006, consistent with the most recent reported quarter and up from 6% in the prior–year quarter. Total digital revenues for the three months ended June 30, 2006 was comprised of U.S. revenues of $68 million, or 74% of total digital revenues, and international revenues of $24 million, or 26% of total digital revenues. The increase in digital revenues resulted from continued efforts to develop our digital business including efforts to further monetize existing content through new formats and new distribution channels and the increased usage of legal, online and mobile distribution channels for the music industry.

See "Business Segment Results" presented hereinafter for a discussion of revenue by business segment.

Cost of revenues

Our cost of revenues increased $49 million, or 12%, to $445 million for the three months ended June 30, 2006 as compared to $396 million for the three months ended June 30, 2005. Excluding a $2 million benefit of foreign currency exchange rates and $5 million of costs related to our sheet music business, which was sold in May 2005, our cost of revenues increased by $56 million. Expressed as a percent of revenues, cost of revenues was 54% and 53% for the three months ended June 30, 2006 and 2005, respectively. The increase related primarily to an increase in product costs of $20 million as a result of higher physical sales and an increase in artist and repertoire costs and licensing costs of $36 million related to increased royalty expense resulting from the increases in both physical and digital sales. While recorded music artist and repertoire costs remained consistent as a percentage of sales, music publishing artist and repertoire costs, excluding the impact of the sheet music business, increased as a percentage of sales due to increased investment in our music publishing business.

Selling, general and administrative expenses

Our selling, general and administrative expenses decreased by $17 million, to $301 million for the three months ended June 30, 2006 as compared to $318 million for the three months ended June 30, 2005. Expressed as a percent of revenues, selling, general and administrative expenses were 37% and 43% for the three months ended June 30, 2006 and 2005, respectively. Excluding a $1 million benefit of foreign currency exchange rates and $2 million of expenses related to our print operations which were sold in May 2005, selling, general and administrative expenses decreased by $14 million, or 4%, primarily related to $29 million of one–time compensation expenses recorded in the three months ended June 30, 2005, consisting of a $10 million one–time

Source: Warner Music Group C, 10-Q, August 03, 2006

bonus to employees related to the Company's Initial Common Stock Offering and $19 million of one-time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date. This decline was offset by a $6 million increase in selling and marketing expense, which was the result of the timing of marketing costs incurred in relation to our product release schedule in the current quarter, and a $6 million increase in distribution costs, directly related to the increase in physical sales. Stock compensation expense amounted to $4 million for the three months ended June 30, 2006 and $9 million for the three months ended June 30, 2005.

Loss on termination of management agreement

Concurrent with our Initial Common Stock Offering, the Investor Group terminated the Management Agreement with us. Under the Management Agreement, we were required to pay the Investor Group annual fees in consideration for ongoing consulting and management advisory services and transaction based fees for services provided in connection with any future acquisition, disposition or financing. The Investor Group terminated the Management Agreement on May 10, 2005 and on May 16, 2005 we paid a $73 million termination fee.

Reconciliation of Consolidated Historical OIBDA to Operating Income (Loss) and Net Loss

As previously described, we use OIBDA as our primary measure of financial performance. The following table reconciles OIBDA to operating income (loss) and further provides the components from operating income (loss) to net loss for purposes of the discussion that follows:

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005
	(unaudited)	(unaudited)
	(In millions)	
OIBDA	$ 86	$ (33)
Depreciation expense	(10)	(12)
Amortization expense	(48)	(47)
Operating income (loss)	28	(92)
Interest expense, net	(45)	(50)
Net investment-related gains	—	1
Loss on repayment of Holdings Notes	—	(35)
Other income, net	1	1
Loss before income taxes	$ (16)	$ (175)
Income tax benefit (expense)	2	(4)
Net loss	$ (14)	$ (179)

OIBDA

Our OIBDA increased $119 million to $86 million for the three months ended June 30, 2006 as compared to a loss of $33 million for the three months ended June 30, 2005. Expressed as a percentage of revenues, total OIBDA margin was 11% for the three months ended June 30, 2006 as compared to (4)% for the three months ended June 30, 2005. The increase was primarily a result of the increased revenues and absence of certain one-time expenses which were included in the three months ended June 30, 2005, including the $73 million payment on termination of the Management Agreement and $29 million of one-time compensation expenses, consisting of a $10 million one-time bonus to employees related to the Company's Initial Common Stock Offering and $19 million of one-time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date, which are more fully discussed above. See "Business Segment Results" presented hereinafter for a discussion of OIBDA by business segment.

Source: Warner Music Group C, 10-Q, August 03, 2006

Depreciation expense

Our depreciation expense decreased by $2 million to $10 million for the three months ended June 30, 2006 as compared to $12 million for the three months ended June 30, 2005. The decrease primarily relates to lower capital spending since the date of the Acquisition.

Amortization expense

Our amortization expense increased by $1 million, or 2%, to $48 million for the three months ended June 30, 2006 as compared to $47 million for the three months ended June 30, 2005. The increase is due to various acquisitions of recorded music catalogs and music publishing copyrights since the prior-year.

Operating income (loss)

Our operating income increased $120 million, to $28 million for the three months ended June 30, 2006 as compared to an operating loss of $92 million for the three months ended June 30, 2005. The increase in operating income was primarily a result of the increase in OIBDA, which is more fully discussed above. See "Business Segment Results" presented hereinafter for a discussion of operating income by business segment.

Interest expense, net

Our interest expense decreased to $45 million for the three months ended June 30, 2006 compared to $50 million for the three months ended June 30, 2005. The decrease in interest expense is due to a higher average debt balance in the prior-year, as the three months ended June 30, 2005 included interest expense related to the outstanding Holdings Floating Rate Notes and Holdings PIK Notes, which were fully redeemed in June 2005, as well as the Holdings Discount Notes, which were partially redeemed in June 2005. The decline was partially offset by the additional interest on an additional $250 million borrowed under the term loan portion of our senior secured credit facility in connection with the Initial Common Stock Offering in May 2005, as well as higher interest rates on outstanding debt during the current period. See "—Financial Condition and Liquidity" for more information.

Net investment-related gains

We recognized a $1 million investment-related gain for the three months ended June 30, 2005 primarily related to the sale of our interest in an equity-method investment. We did not recognize any investment-related gains or losses for the three months ended June 30, 2006.

Loss on repayment of Holdings Notes

In June 2005, we redeemed all of the outstanding Holdings Floating Rate Notes, all of the outstanding Holdings PIK Notes and 35% of the outstanding Holdings Discount Notes. In connection with the redemption, we paid approximately $19 million of redemption premiums, and wrote off approximately $12 million related to the carrying value of the unamortized debt issuance costs related to our Holdings Notes and approximately $4 million related to the carrying value of the unamortized discount on the issuance of the Holdings Notes. See "—Financial Condition and Liquidity" for more information.

Other income, net

Other income, net relates to foreign currency exchange rate movements associated with intercompany receivables and payables that are short-term in nature, and therefore required to be recognized in the statement of operations under U.S. GAAP. We recognized $1 million of other income, net for each of the three months ended June 30, 2006 and 2005 as a result of favorable foreign currency exchange rate movements.

Source: Warner Music Group C, 10-Q, August 03, 2006

Income tax benefit (expense)

We provided an income tax benefit of $2 million and income tax expense of $4 million for the three months ended June 30, 2006 and 2005, respectively. The current quarter tax benefit related to a discreet period item that resulted from the completion in the current quarter of an analysis of the allocation of our operating expenses charged to affiliates. The analysis resulted in a higher percentage of operating expenses being allocated to foreign income, thereby reducing foreign income taxes. In connection with the Acquisition we made a joint election with Time Warner under Section 338(h)(10) of the U.S. Internal Revenue Code to treat the Acquisition as an asset purchase. There was no offsetting income tax benefit on U.S. domestic tax losses recognized due to the uncertain nature of these deferred tax assets. Our income tax expense for the three months ended June 30, 2005 primarily relates to the tax provisions on foreign income.

Net loss

Our net loss declined $165 million, to a net loss of $14 million for the three months ended June 30, 2006 as compared to a net loss of $179 million for the three months ended June 30, 2005. The decrease is primarily the result of increases in revenues and the absence of certain one-time expenses which were included in the three months ended June 30, 2005, including the $73 million payment on termination of the Management Agreement, $29 million of one-time compensation expenses and the $35 million loss on the repayment of the Holdings Notes, which are more fully discussed above.

Business Segment Results

Revenue, OIBDA and operating income (loss) by business segment are as follows:

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)
	(In millions)	
Recorded Music		
Revenue	$ 678	$ 588
OIBDA	$ 92	$ 47
Operating income	$ 52	$ 6
Music Publishing		
Revenue	$ 150	$ 161
OIBDA	$ 23	$ 28
Operating income	$ 9	$ 13
Corporate and Revenue Eliminations		
Revenue	$ (6)	$ (7)
OIBDA	$ (29)	$ (108)
Operating loss	$ (33)	$ (111)
Total		
Revenue	$ 822	$ 742
OIBDA	$ 86	$ (33)
Operating income (loss)	$ 28	$ (92)

Recorded Music

Recorded Music revenues increased by $90 million, or 15%, to $678 million for the three months ended June 30, 2006 from $588 million for the three months ended June 30, 2005. Excluding a $4 million unfavorable impact of foreign currency exchange rates, Recorded Music revenues increased by $94 million, or 16%, which was driven by an increase in digital sales of approximately $50 million and an increase in physical sales of $44

Source: Warner Music Group C, 10-Q, August 03, 2006

million. Digital sales totaled $88 million, or 13% of Recorded Music revenues for the three months ended June 30, 2006 compared to $38 million, or 6%, for the three months ended June 30, 2005. Digital sales totaled $86 million, or 13% for the immediately preceding three months ended March 31, 2006. Worldwide physical sales increased as a result of significant sales of new releases in the three months ended June 30, 2006, as well as increased sales of a number of carryover and catalog releases. Domestic physical sales increased $18 million, and excluding the impact of foreign currency exchange rates, international physical sales increased $26 million.

Recorded Music revenues represented 82% and 79% of consolidated revenues, prior to corporate and revenue eliminations, for the three months ended June 30, 2006 and 2005, respectively. U.S. Recorded Music revenues were $347 million and $292 million, or 51% and 50% of consolidated Recorded Music revenues for the three months ended June 30, 2006 and 2005, respectively. International Recorded Music revenues were $331 million and $296 million, or 49% and 50% of consolidated Recorded Music revenues for the three months ended June 30, 2006 and 2005, respectively.

Recorded Music OIBDA increased by $45 million, to $92 million for the three months ended June 30, 2006 compared to $47 million for the three months ended June 30, 2005. Expressed as a percentage of Recorded Music revenues, Recorded Music OIBDA was 14% and 8% for the three months ended June 30, 2006 and 2005, respectively. The increase in OIBDA was primarily a result of the $90 million increase in revenues more fully described above and a $22 million decrease in general and administrative expense, primarily due to the absence of a $20 million impact related to one-time compensation expenses consisting of a one-time bonus to employees related to the Company's Initial Common Stock Offering and one-time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date. These increases in OIBDA were offset by (i) a $20 million increase in product costs and a $6 million increase in distribution costs directly related to the increase in physical sales previously described and (ii) a $24 million increase in artist and repertoire costs primarily related to increased royalty expense as a result of our increases in both physical and digital sales previously described. As a percentage of Recorded Music revenues, artist and repertoire costs were flat, excluding the impact of foreign currency exchange rates, as compared to the prior-year quarter.

Recorded Music operating income was $52 million for the three months ended June 30, 2006 as compared to $6 million for the three months ended June 30, 2006. Recorded Music operating income included the following components:

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)
	(In millions)	
OIBDA	$ 92	$ 47
Depreciation and amortization	(40)	(41)
Operating income	$ 52	$ 6

The $46 million increase in Recorded Music operating income related to the $45 million increase in Recorded Music OIBDA more fully discussed above, and a decrease in Recorded Music depreciation and amortization of $1 million.

Music Publishing

Music Publishing revenues decreased $11 million, or 7%, to $150 million for the three months ended June 30, 2006 as compared to $161 million for the three months ended June 30, 2005. Excluding prior-year revenue of $8 million from our sheet music business, which was sold in May 2005, Music Publishing revenues

Source: Warner Music Group C, 10-Q, August 03, 2006

declined $3 million, or 2%, and such decline was comprised of a $4 million decrease in mechanical revenue and a $12 million decline in synchronization revenue, offset by increases in performance revenue of $8 million and other revenues of $5 million. Mechanical revenue declines reflect prior-year industry declines in physical record sales. Synchronization revenues declined as a result of variability in the film and television commercial markets as well as the timing of payments received from key licensors of our copyrights. The increase in performance revenue reflects a change in the timing of payments received from a U.S. performing rights organization. Other revenue consists primarily of print licensing fees and royalties from other sources such as stage productions. Music Publishing revenues consisted of $62 million of mechanical revenues, $58 million of performance revenues, $21 million of synchronization revenues, $4 million of revenues from digital sales and $5 million of other revenues. Digital sales represented 3% and 4% of Music Publishing revenues for the three months ended June 30, 2006 and 2005, respectively. Music Publishing revenues represented 18% and 22% of consolidated revenues, prior to corporate and revenue eliminations, for the three months ended June 30, 2006 and 2005, respectively.

Music Publishing OIBDA declined $5 million to $23 million for the three months ended June 30, 2006 as compared to $28 million for the three months ended June 30, 2005. Excluding $1 million in prior-year OIBDA from our sheet music business, OIBDA decreased by $4 million primarily as a result of the decrease in revenues discussed above. Expressed as a percentage of Music Publishing revenues, Music Publishing OIBDA was 15% and 17% for the three months ended June 30, 2006 and 2005, respectively.

Music Publishing operating income was $9 million for the three months ended June 30, 2006 as compared to $13 million for the three months ended June 30, 2005. Music Publishing operating income includes the following components:

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)
	(In millions)	
OIBDA	$ 23	$ 28
Depreciation and amortization	(14)	(15)
Operating income	$ 9	$ 13

The $4 million decline in Music Publishing operating income related to the $5 million decrease in Music Publishing OIBDA, more fully discussed above, and a $1 million decrease in depreciation and amortization.

Corporate Expenses and Eliminations

Corporate expenses before depreciation and amortization expense decreased $79 million to $29 million for the three months ended June 30, 2006 as compared to $108 million for the three months ended June 30, 2005. Corporate expenses decreased primarily due to the lack of a $73 million payment on termination of management fee, described more fully above. Additionally, prior-year corporate expenses were impacted by $8 million of one-time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date.

Source: Warner Music Group C, 10-Q, August 03, 2006

Nine Months Ended June 30, 2006 Compared to Nine Months Ended June 30, 2005

The following table summarizes our historical results of operations:

	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(unaudited)	(unaudited)
	(In millions)	
Revenues	$ 2,662	$ 2,597
Costs and expenses:		
Cost of revenues(1)	(1,384)	(1,377)
Selling, general and administrative expenses	(918)	(942)
Amortization of intangible assets	(143)	(140)
Loss on termination of management agreement	—	(73)
Total costs and expenses	(2,445)	(2,532)
Operating income	217	65
Interest expense, net	(135)	(140)
Net investment-related gains	—	1
Equity in the gains (losses) of equity-method investees, net	1	(1)
Loss on repayment of Holdings Notes	—	(35)
Unrealized gain on warrants	—	17
Minority interest expense	—	(5)
Other income, net	3	5
Income (loss) before income taxes	86	(93)
Income tax expense	(38)	(46)
Net income (loss)	$ 48	$ (139)

(1) Includes depreciation expense of $32 million and $40 million for the nine months ended June 30, 2006 and 2005, respectively.

Consolidated Historical Results

Revenues

Our revenues increased $65 million, or 3%, to $2.662 billion for the nine months ended June 30, 2006 as compared to $2.597 billion for the nine months ended June 30, 2005. Excluding a $62 million unfavorable impact of foreign currency exchange rates and prior-year revenue of $34 million related to our sheet music business, which was sold in May 2005, total revenue increased by $161 million, or 6%, primarily due to significant increases in digital sales. Recorded Music revenues increased by $125 million, to $2.274 billion for the nine months ended June 30, 2006. Excluding the impact of foreign currency exchange rates, Recorded Music revenues increased by $173 million or 8%, primarily driven by an increase in worldwide Recorded Music digital sales of $148 million and an increase in worldwide Recorded Music licensing revenue and physical sales of $25 million. Music Publishing revenues declined by $60 million, to $410 million for the nine months ended June 30, 2006. Excluding the impact of foreign currency exchange rates and the prior-year revenue related to our sheet music business, Music Publishing revenue declined $12 million, or 3%. International operations represented $1.380 billion of consolidated revenues for each of the nine months ended June 30, 2006 and 2005, comprising 52% and 53% of total revenues, respectively.

Overall digital revenues grew $147 million to $251 million for the nine months ended June 30, 2006 as compared to $104 million for the nine months ended June 30, 2005. Digital revenues represented 9% and 4% of consolidated revenues for the nine months ended June 30, 2006 and 2005, respectively. Total digital revenues for the nine months ended June 30, 2006 were comprised of U.S revenues of $181 million, or 72% of total digital

Source: Warner Music Group C, 10-Q, August 03, 2006

revenues, and international revenues of $70 million, or 28% of total digital revenues. The increase in digital revenues resulted from continued efforts to develop our digital business including efforts to further monetize existing content through new formats and new distribution channels and the increased usage of legal, online and mobile distribution channels for the music industry.

See "Business Segment Results" presented hereinafter for a discussion of revenue by business segment.

Cost of revenues

Our cost of revenues increased by $7 million, or 1%, to $1.384 billion for the nine months ended June 30, 2006 as compared to $1.377 billion for the nine months ended June 30, 2005. Expressed as a percent of revenues, cost of revenues was 52% and 53% for the nine months ended June 30, 2006 and 2005, respectively. Excluding a $38 million favorable impact of foreign currency exchange rates and $22 million of expenses related to our sheet music business, which was sold in May 2005, our cost of revenues increased $67 million, or 5%. The increase was primarily due to an increase in product costs of $45 million, directly related to our higher physical sales and a $22 million increase in artist and repertoire and licensing expenses related primarily to increased royalty expense as a result of our increases in physical and digital sales.

Selling, general and administrative expenses

Our selling, general and administrative expenses decreased by $24 million, or 3%, to $918 million for the nine months ended June 30, 2006 as compared to $942 million for the nine months ended June 30, 2005. Expressed as a percent of revenues, selling, general and administrative expenses were 34% and 36% for the nine months ended June 30, 2006 and 2005, respectively. Excluding a $17 million benefit of foreign currency exchange rates and $11 million of expenses related to our sheet music business, selling, general and administrative expenses increased by $4 million. The increase primarily related to (i) a $35 million increase in selling and marketing due to the timing of marketing costs incurred in relation to our product release schedule in the current period and (ii) a $7 million increase in distribution costs related to our increase in physical sales. These increases were offset by an $18 million decrease in general and administrative expenses, primarily due to the absence of $29 million of one–time compensation expenses recorded in the nine months ended June 30, 2005, consisting of a $10 million one–time bonus to employees related to the Company's Initial Common Stock Offering and $19 million of one–time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date and $6 million of management fees incurred related to the terminated Management Agreement described below. This was partially offset by a severance payment of $8 million related to the departure of the chairman of WMI recorded in the nine months ended June 30, 2006. Additionally, the increase was offset by an $8 million decrease in depreciation expense, discussed more fully below. Stock compensation expense amounted to $12 million for the nine months ended June 30, 2006 and $18 million for the nine months ended June 30, 2005.

Loss on termination of management agreement

Concurrent with our Initial Common Stock Offering, the Investor Group terminated the Management Agreement. Under the Management Agreement, we were required to pay the Investor Group annual fees in consideration for ongoing consulting and management advisory services and transaction based fees for services provided in connection with any future acquisition, disposition, or financing. The Investor Group terminated the Management Agreement on May 10, 2005 and on May 16, 2005 we paid a $73 million termination fee.

Source: Warner Music Group C, 10-Q, August 03, 2006

Reconciliation of Consolidated Historical OIBDA to Operating Income and Net Income (Loss)

As previously described, we use OIBDA as our primary measure of financial performance. The following table reconciles OIBDA to operating income and further provides the components from operating income to net income (loss) for purposes of the discussion that follows:

	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(unaudited)	(unaudited)
	(in millions)	
OIBDA	$ 392	$ 245
Depreciation expense	(32)	(40)
Amortization expense	(143)	(140)
Operating income	217	65
Interest expense, net	(135)	(140)
Net investment-related gains	—	1
Equity in the gains (losses) of equity-method investees, net	1	(1)
Loss on repayment of Holdings Notes	—	(35)
Unrealized gain on warrants	—	17
Minority interest expense	—	(5)
Other income, net	3	5
Income (loss) before income taxes	86	(93)
Income tax expense	(38)	(46)
Net income (loss)	$ 48	$ (139)

OIBDA

Our OIBDA increased $147 million to $392 million for the nine months ended June 30, 2006 as compared $245 million for the nine months ended June 30, 2005. Expressed as a percentage of revenues, total OIBDA margin was 15% for the nine months ended June 30, 2006 as compared to 9% for the nine months ended June 30, 2005. The increase was primarily a result of the increase in Recorded Music revenue and the absence of certain one-time expenses which were included in the nine months ended June 30, 2005, including the $73 million payment on termination of the Management Agreement and $29 million of one-time compensation expenses, consisting of a $10 million one-time bonus to employees related to the Company's Initial Common Stock Offering and $19 million of one-time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date, which are more fully discussed above. See "Business Segment Results" presented hereinafter for a discussion of OIBDA by business segment.

Depreciation expense

Our depreciation expense decreased by $8 million to $32 million for the nine months ended June 30, 2006 as compared to $40 million for the nine months ended June 30, 2005. The decrease primarily relates to lower capital spending since the date of the Acquisition.

Amortization expense

Our amortization expense increased by $3 million, or 2%, to $143 million for the nine months ended June 30, 2006 as compared to $140 million for the nine months ended June 30, 2005. The increase is due to various acquisitions of recorded music catalogs and music publishing copyrights since the prior-year.

Source: Warner Music Group C, 10-Q, August 03, 2006

Operating income

Our operating income increased $152 million, to $217 million for the nine months ended June 30, 2006 as compared to $65 million for the nine months ended June 30, 2005. The increase in operating income was primarily a result of the increase in OIBDA and the decrease in depreciation expense, which are more fully discussed above. See "Business Segment Results" presented hereinafter for a discussion of operating income by business segment.

Interest expense, net

Our interest expense decreased $5 million to $135 million for the nine months ended June 30, 2006 as compared to $140 million for the nine months ended June 30, 2005. The nine months ended June 30, 2005 include several months of interest expense related the outstanding Holdings Floating Rate Notes and Holdings PIK Notes, which were issued in December 2004 and fully redeemed in June 2005, as well as the Holdings Discount Notes, which were issued in December 2004 and partially redeemed in June 2005. The decline is partially offset by interest expense related to an additional outstanding term loan of $250 million borrowed in May 2005, which is reflected in only one of the nine months ended June 30, 2005, as well as higher interest rates on outstanding debt during the current period. See "—Financial Condition and Liquidity" for more information.

Net investment–related gains

We recognized a $1 million investment–related gain for the nine months ended June 30, 2005 primarily related to the sale of our interest in an equity–method investment. We did not recognize any investment–related gains or losses for the nine months ended June 30, 2006.

Equity in the gains (losses) of equity–method investees, net

The nine months ended June 30, 2006 includes $1 million of equity in the gains of equity–method investees, as compared to $1 million of equity in the losses of equity–method investees during the nine months ended June 30, 2005.

Loss on repayment of Holdings Notes

In June 2005 we redeemed all of the outstanding Holdings Floating Rate Notes, all of the outstanding Holdings PIK Notes and 35% of the outstanding Holdings Discount Notes. In connection with the redemption, we paid approximately $19 million of redemption premiums, and wrote off approximately $12 million related to the carrying value of the unamortized debt issuance costs related to our Holdings Notes and approximately $4 million related to the carrying value of the unamortized discount on the issuance of the Holdings Notes. See "—Financial Condition and Liquidity" for more information.

Unrealized gain on warrants

We recognized a $17 million unrealized gain to mark–to–market the value of the warrants issued to Time Warner in connection with the Acquisition for the nine months ended June 30, 2005. In connection with the Company's Initial Common Stock Offering, we repurchased the warrants at a cost of approximately $138 million, which approximated fair value at that date.

Minority interest expense

We recognized minority interest expense of $5 million for the nine months ended June 30, 2005. This expense related to dividends on preferred stock of Holdings that was held directly by the Investor Group and was issued in connection with the initial funding of the purchase price for the Acquisition effective March 1, 2004. The preferred stock was fully redeemed in December 2004 from the proceeds of the Holdings Notes. As such, there is no comparable charge recognized during the nine months ended June 30, 2006.

Source: Warner Music Group C, 10-Q, August 03, 2006

Other Income, net

We recognized $3 million and $5 million of other income, net for the nine months ended June 30, 2006 and 2005, respectively. Other income, net relates to favorable foreign currency exchange rate movements associated with inter-company receivables and payables that are short-term in nature, and therefore required to be recognized in the statement of operations under U.S. GAAP.

Income tax expense

We provided income tax expense of $38 million for the nine months ended June 30, 2006 as compared to $46 million for the nine months ended June 30, 2005. The tax provision for the nine months ended June 30, 2006 included a discreet period item that resulted from the completion in the current period of an analysis of the allocation of our operating expenses charged to affiliates. The analysis resulted in a higher percentage of operating expenses being allocated to foreign income, thereby reducing foreign income taxes. In connection with the Acquisition we made a joint election with Time Warner under Section 338(h)(10) of the U.S. Internal Revenue Code to treat the Acquisition as an asset purchase. There was no offsetting income tax benefit on U.S. domestic tax losses recognized due to the uncertain nature of these deferred tax assets. Our income tax expense for the nine months ended June 30, 2006 and 2005 primarily relates to the tax provisions on foreign income.

Net income (loss)

Our net income increased by $187 million, to net income of $48 million for the nine months ended June 30, 2006 as compared to a net loss of $139 million for the nine months ended June 30, 2005. The increase in net income is primarily the result of the absence of certain one-time expenses which were included in the nine months ended June 30, 2005, including the $73 million payment on termination of the Management Agreement, $29 million of one-time compensation expenses and the $35 million loss on repayment of the Holdings Notes, which are more fully discussed above.

Business Segment Results

Revenue, OIBDA and operating income (loss) by business segment are as follows:

	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)
	(In millions)	
Recorded Music		
Revenue	$ 2,274	$ 2,149
OIBDA	$ 379	$ 313
Operating income	$ 258	$ 188
Music Publishing		
Revenue	$ 410	$ 470
OIBDA	$ 91	$ 99
Operating income	$ 47	$ 55
Corporate and Revenue Eliminations		
Revenue	$ (22)	$ (22)
OIBDA	$ (78)	$ (167)
Operating (loss)	$ (88)	$ (178)
Total		
Revenue	$ 2,662	$ 2,597
OIBDA	$ 392	$ 245
Operating income	$ 217	$ 65

Source: Warner Music Group C, 10-Q, August 03, 2006

Recorded Music

Recorded Music revenues increased by $125 million, or 6%, to $2.274 billion for the nine months ended June 30, 2006 from $2.149 billion for the nine months ended June 30, 2005. Excluding a $48 million unfavorable impact of foreign currency exchange rates, Recorded Music revenues increased by $173 million, or 8%, which was primarily driven by an increase in digital sales of $148 million and an increase in licensing revenue and physical sales of $25 million. Digital sales totaled $238 million, or 10% of Recorded Music revenues for the nine months ended June 30, 2006 and $90 million, or 4%, for the nine months ended June 30, 2005.

Recorded Music revenues represented 85% and 83% of consolidated revenues, prior to corporate and revenue eliminations, for the nine months ended June 30, 2006 and 2005, respectively. U.S. Recorded Music revenues were $1.115 billion and $1.001 billion, or 49% and 47% of consolidated Recorded Music Revenues for the nine months ended June 30, 2006 and 2005, respectively. International Recorded Music revenues were $1.159 billion and $1.148 billion, or 51% and 53% of consolidated Recorded Music Revenues for the nine months ended June 30, 2006 and 2005, respectively.

Recorded Music OIBDA increased by $66 million, or 21%, to $379 million for the nine months ended June 30, 2006 compared to $313 million for the nine months ended June 30, 2005. Expressed as a percentage of Recorded Music revenues, Recorded Music OIBDA was 17% and 15% for the nine months ended June 30, 2006 and 2005, respectively. Excluding a $3 million unfavorable impact of foreign currency exchange rates, OIBDA increased $69 million, or 22%, primarily as a result of the $173 million increase in revenues more fully described above, offset by (i) a $45 million increase in product costs, due primarily to the increase in physical sales and to increased sales of special edition physical products, such as CD/DVD box sets in the current period, (ii) a $27 million increase in artist and repertoire costs and licensing costs due primarily to increased royalty expense related to our increases in physical and digital sales and (iii) a $34 million increase in selling and marketing costs related to the timing of marketing costs incurred related to our product release schedule in the current period and as well as a larger number of releases that sold in excess of one million units as compared to the prior year period. General and administrative costs declined $12 million due to prior-year one-time bonuses to employees related to the Company's Initial Common Stock Offering and one-time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date amounting to $20 million, offset by the $8 million severance payment made related to the departure of the chairman of WMI in the nine months ended June 30, 2006.

Recorded Music operating income was $258 million for the nine months ended June 30, 2006 as compared to $188 million for the nine months ended June 30, 2005. Recorded Music operating income included the following components:

	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)
	(In millions)	
OIBDA	$ 379	$ 313
Depreciation and amortization	(121)	(125)
Operating income	$ 258	$ 188

The $70 million increase in Recorded Music operating income related to the $66 million increase in Recorded Music OIBDA, more fully discussed above, and a decrease in Recorded Music depreciation and amortization of $4 million.

Music Publishing

Music Publishing revenues decreased to $410 million for the nine months ended June 30, 2006 as compared to $470 million for the nine months ended June 30, 2005. Excluding a $14 million unfavorable impact of foreign

Source: Warner Music Group C, 10-Q, August 03, 2006

currency exchange rates, and prior–year revenue of $34 million of revenue from our sheet music business, which was sold in May 2005, Music Publishing revenues declined $12 million, or 3%, which was comprised of a $16 million decrease in mechanical revenue and a $14 million decline in synchronization revenue, offset by an $8 million increase in performance revenue and a $11 million increase in other revenues. Mechanical revenue declines reflect prior–year industry declines in physical record sales. Synchronization revenues declined as a result of variability in the film and television commercial markets as well as the timing of payments from key licensors of our copyrights. The increase in performance revenue reflects a change in the timing of payments received from a U.S. performing rights organization. Other revenue consists primarily of print licensing fees and royalties from other sources such as stage productions. Music Publishing revenues consisted of $179 million of mechanical revenues, $145 million of performance revenues, $59 million of synchronization revenues, $13 million of revenues from digital sales and $14 million of other revenues. Digital sales represented 3% of Music Publishing revenues for the nine months ended June 30, 2006 and 2005. Music Publishing revenues represented 15% and 18% of consolidated revenues, prior to corporate and revenue eliminations, for the nine months ended June 30, 2006 and 2005, respectively.

Music Publishing OIBDA decreased $8 million to $91 million for the nine months ended June 30, 2006 as compared to $99 million for the nine months ended June 30, 2005. Expressed as a percent of Music Publishing revenues, Music Publishing OIBDA was 22% and 21% for the nine months ended June 30, 2006 and 2005, respectively. Excluding a $1 million unfavorable impact of foreign currency exchange rates, and prior–year OIBDA of $1 million from our sheet music business, which was sold in May 2005, Music Publishing OIBDA decreased $6 million, primarily as a result of the $12 million decrease in revenue more fully discussed above, which was offset by a $6 million decrease in royalty expenses related to the decrease in revenue discussed above.

Music Publishing operating income decreased to $47 million for the nine months ended June 30, 2006 as compared to $55 million for the nine months ended June 30, 2005. Music Publishing operating income includes the following components:

	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(unaudited)	(unaudited)
	(In millions)	
OIBDA	$ 91	$ 99
Depreciation and amortization	(44)	(44)
Operating income	$ 47	$ 55

The $8 million decrease in Music Publishing operating income related to the $8 million decrease in Music Publishing OIBDA, more fully discussed above.

Corporate Expenses and Eliminations

Corporate expenses before depreciation and amortization expense decreased by $89 million to $78 million for the nine months ended June 30, 2005, compared to $167 million for the nine months ended June 30, 2004. Corporate expenses primarily decreased due to the prior–year $73 million payment on termination of Management Agreement, more fully described above, as well as the absence of management fees amounting to $6 million related to such Management Agreement. Corporate expenses for the nine months ended June 30, 2005 also included $8 million of one–time compensation expenses consisting of a one–time bonus to employees related to the Company's Initial Common Stock Offering and one–time payments to holders of restricted stock and stock options primarily to compensate them for certain amounts related to stock awards issued at prices that were below fair value at the grant date.

Source: Warner Music Group C, 10-Q, August 03, 2006

FINANCIAL CONDITION AND LIQUIDITY

Financial Condition

At June 30, 2006, we had $2.251 billion of debt, $306 million of cash and equivalents, $29 million of short-term investments (net debt of $1.916 billion, defined as total debt less cash and equivalents and short-term investments) and $80 million of shareholders' equity. This compares to $2.246 billion of debt, $288 million of cash and equivalents (net debt of $1.958 billion) and $89 million of shareholders' equity at September 30, 2005. Net debt decreased by $42 million as a result of (i) an $18 million increase in cash and equivalents, (ii) a $29 million increase in short-term investments and (iii) a $13 million reduction of debt related to our quarterly repayments of our term loans under the senior secured credit facility. The declines were offset by a $6 million impact of foreign currency exchange rates on our Sterling-denominated notes and $12 million accretion of our Holdings Discount Notes.

Short-term investments include high-quality, investment grade securities such as taxable auction rate securities as well as commercial paper and corporate bonds with maturities greater than 90 days but less than one year. We have expanded our investment portfolio in order to increase yield while maintaining safety of principal consistent with an investment policy approved by the Board of Directors.

The $9 million decrease in shareholders' equity during the nine months ended June 30, 2006 consisted of $48 million of net income for the nine months ended June 30, 2006, deferred gains on derivative financial instruments of $12 million and stock compensation of $12 million for the nine months ended June 30, 2006. These increases were primarily offset by $76 million of dividends, which was comprised of our $19.3 million dividend declared on October 3, 2005 and paid on November 23, 2005, our $19.3 million dividend declared on December 29, 2005 and paid on February 17, 2006, our $19.3 million dividend declared on March 14, 2006 and paid on May 3, 2006, and our $19.3 million dividend declared on June 7, 2006 and paid on July 27, 2006.

Cash Flows

The following table summarizes our historical cash flows. The financial data for the nine months ended June 30, 2006 and 2005 are unaudited and are derived from our interim financial statements included elsewhere herein.

	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
	(unaudited)	(unaudited)
	(In millions)	
Cash provided by (used in):		
Operating activities	$ 223	$ 172
Investing activities	(142)	(54)
Financing activities	(68)	(407)

Operating Activities

Cash provided by operations was $223 million for the nine months ended June 30, 2006 compared to $172 million for the nine months ended June 30, 2005. The $51 million increase reflects the prior-year payment of the $73 million fee as a result of the termination of the Management Agreement, higher interest payments in the prior-year related to the additional Holdings debt outstanding, prior-year cash payments of $10 million to our employees in connection with the Company's Initial Common Stock Offering and cash payments for certain of the other one-time special bonuses paid to certain holders of restricted stock and stock options and cash paid in the prior-year in relation to our restructuring plan. The current-year cash provided by operations reflects higher cash collections due to consistently higher sales, offset by higher royalty advance payments in connection with contractual obligations and the timing of releases and additional royalty payments related to the timing of releases.

Source: Warner Music Group C, 10-Q, August 03, 2006

Investing Activities

Cash used in investing activities was $142 million for the nine months ended June 30, 2006 compared to $54 million for the nine months ended June 30, 2005. The $142 million of cash used in investing activities in the nine months ended June 30, 2006 primarily reflects $63 million, net of cash acquired, paid for the completion of our acquisition of Ryko, $29 million of cash invested in auction-rate securities and other short-term investments, $18 million of capital expenditures as well as several small acquisitions in Australia, Singapore and South Africa. The $54 million of cash used in investing activities in the nine months ended June 30, 2005 primarily reflects $20 million of capital expenditures, the acquisition of an additional 30% interest in Maverick and various acquisitions of music publishing copyrights offset by $50 million of proceeds from the sale of certain assets.

Financing Activities

Cash used in financing activities was $68 million for the nine months ended June 30, 2006, a $339 million decrease as compared to $407 million for the nine months ended June 30, 2005. Cash used in financing activities for the nine months ended June 30, 2006 consisted of our quarterly repayment of debt and the payment of dividends. Cash used in financing activities for the nine months ended June 30, 2005 primarily relates to the repayment of a portion of the Holdings Notes for $574 million, quarterly term loan debt repayments of $10 million, the returns of capital paid to the Investor Group of $917 million, the $209 million redemption of subsidiary preferred stock as part of the Holdings Refinancing and $138 million paid to repurchase the three-year warrants from Time Warner. These uses of cash were offset principally by $525 million of net proceeds after stock-issuance costs from the Company's Initial Common Stock Offering, $681 million of net proceeds after debt-issuance costs from the issuance of debt as part of the Holdings Refinancing and $247 million of net proceeds after debt-issuance costs from the additional term loan borrowings under the senior secured credit facility.

Liquidity

Our primary sources of liquidity are the cash flow generated from our subsidiaries' operations, availability under the undrawn $250 million (less $2 million of outstanding letters of credit as of June 30, 2006) revolving credit portion of our senior secured credit facility and available cash and equivalents and short-term investments. These sources of liquidity are needed to fund our debt service requirements, working capital requirements, capital expenditure requirements, regular quarterly dividends and the remaining one-time costs associated with the execution of our restructuring plan. We believe that our existing sources of cash will be sufficient to support our existing operations over the next twelve months.

As of June 30, 2006, our long-term debt consisted of $1.417 billion of borrowings (including $17 million of debt that is classified as a current obligation) under the term loan portion of our senior secured credit facility, $648 million of Acquisition Corp. senior subordinated notes and $186 million of Holdings Discount Notes. There were no borrowings under the revolving portion of our senior secured credit facility as of June 30, 2006.

Senior Secured Credit Facility

The senior secured credit facility consists of a $1.417 billion outstanding term loan portion and a $250 million revolving credit portion. The term loan portion of the facility matures in February 2011. We are required to prepay outstanding term loans, subject to certain exceptions and conditions, with excess cash flow or in the event of certain asset sales and casualty and condemnation events and incurrence of debt. We are required to make minimum repayments under the term loan portion of our facility in quarterly principal amounts of approximately $4 million through November 2010, with a remaining balloon payment in February 2011. The revolving credit portion of the senior secured credit facility matures in February 2010. There are no mandatory reductions in borrowing availability for the revolving credit portion of the facility through its term.

Borrowings under both the term loan and revolving credit portion of the senior secured credit facility currently bear interest at a rate equal to an applicable margin plus, at our option, either (a) a base rate determined

Source: Warner Music Group C, 10-Q, August 03, 2006

by reference to the higher of (1) the prime rate of Bank of America, N.A. and (2) the federal funds rate plus 1/2 of 1% or (b) a LIBOR rate determined by reference to the costs of funds for deposits in the currency of such borrowing for the interest period relevant to such borrowing adjusted for certain additional costs. As of June 30, 2006, the applicable margins with respect to base rate borrowings and LIBOR borrowings were 1.25% and 2.25%, respectively, for borrowings under the revolving credit facility. The applicable margins are variable subject to changes in certain leverage ratios. For borrowings under the term loan facility, the margins with respect to the base rate borrowings and LIBOR borrowings are 1.00% and 2.00%, respectively, but will be 0.75% and 1.75%, respectively if the senior secured debt of Acquisition Corp. is rated at least BB by S&P and at least Ba2 by Moody's. As of August 2, 2006, our term loan facility was rated B+ by S&P and Ba2 by Moody's.

In addition to paying interest on outstanding principal under the senior secured credit facility, we are required to pay a commitment fee to the lenders under the revolving credit facility in respect of the unutilized commitments. As of June 30, 2006, the commitment fee rate was 0.375%. The commitment fee rate is variable subject to changes in certain of our leverage ratios. We also are required to pay customary letter of credit fees, as necessary.

The senior secured credit facility contains a number of covenants that, among other things, restrict, subject to certain exceptions, our ability and the ability of our subsidiaries to sell assets, incur additional indebtedness or issue preferred stock, repay other indebtedness, pay dividends and distributions or repurchase capital stock, create liens on assets, make investments, loans or advances, make certain acquisitions, engage in mergers or consolidations, engage in certain transactions with affiliates, amend certain material agreements, change the business conducted by us and enter into agreements that restrict dividends from subsidiaries. In addition, the senior secured credit facility requires us to maintain the following financial covenants: a maximum total leverage ratio and a minimum interest coverage ratio, both tested quarterly, and a maximum annual capital expenditures limitation.

Senior Subordinated Notes of Acquisition Corp.

Acquisition Corp. has outstanding two tranches of senior subordinated notes due 2014: $465 million principal amount of U.S. dollar–denominated notes and £100 million principal amount of Sterling–denominated notes (collectively, the "Senior Subordinated Notes"). The Senior Subordinated Notes mature on April 15, 2014. The Senior Subordinated Notes bear interest at a fixed rate of 7 3/8% per annum on the $465 million dollar notes and 8 1/8% per annum on the £100 million Sterling notes. The indenture governing the notes limits our ability and the ability of our restricted subsidiaries to incur additional indebtedness or issue certain preferred shares, to pay dividends on or make other distributions in respect of its capital stock or make other restricted payments, to make certain investments; to sell certain assets, to create liens on certain debt without securing the notes, to consolidate, merge, sell or otherwise dispose of all or substantially all of our assets, to enter into certain transactions with affiliates and to designate our subsidiaries as unrestricted subsidiaries. Subject to certain exceptions, the indenture governing the notes permits us and our restricted subsidiaries to incur additional indebtedness, including secured indebtedness, and to make certain restricted payments and investments.

Holdings Notes

In December 2004, Holdings issued the Holdings Notes. In connection with the Company's Initial Common Stock Offering, we used $517 million of proceeds from the offering along with $57 million of available cash to redeem certain of the Holdings Notes outstanding. As of June 30, 2006, Holdings had $186 million of debt on its balance sheet relating to such securities, net of issuance discounts.

The Holdings Floating Rate Notes were redeemed in full on June 15, 2005. From the issuance date through the redemption date, the notes bore interest at a quarterly floating rate based on six–month LIBOR rates plus a margin equal to 4.375%. Interest was payable quarterly in cash beginning on March 15, 2005.

The Holdings Discount Notes were issued at a discount and had an initial accreted value of $630.02 per $1,000 principal amount at maturity. Prior to December 15, 2009, no cash interest payments are required.

Source: Warner Music Group C, 10-Q, August 03, 2006

However, interest accrues on the Holdings Discount Notes in the form of an increase in the accreted value of such notes such that the accreted value of the Holdings Discount Notes will equal the principal amount at maturity on December 15, 2009. Thereafter, cash interest on the Holdings Discount Notes is payable semiannually at a fixed rate of 9.5% per annum. The Holdings Discount Notes mature on December 15, 2014. The Company redeemed 35% of the Holdings Discount Notes on June 15, 2005.

The Holdings PIK Notes were redeemed in full on June 15, 2005. From the date of issuance through the date of redemption, the notes bore interest at a semi-annual floating rate based on six-month LIBOR rates plus a margin equal to 7%. Interest was accrued in the form of additional PIK notes at the election of the Company. Such amounts were also repaid in connection with the redemption.

The terms of the indentures governing the Acquisition Corp. Senior Subordinated Notes and Holdings Discount Notes significantly restrict Acquisition Corp., Holdings and other subsidiaries from paying dividends and otherwise transferring assets to us. For example, the ability of Acquisition Corp. and Holdings to make such payments is governed by a formula based on 50% of each of their consolidated net income (which, as defined in the indentures governing such notes, excludes goodwill impairment charges and any after-tax extraordinary, unusual or nonrecurring gains and losses) accruing from June 1, 2004 and July 1, 2004, respectively. In addition, as a condition to making such payments to us based on such formula, Acquisition Corp. and Holdings must each have an adjusted EBITDA to interest expense ratio of at least 2.0 to 1 after giving effect to any such payments. Acquisition Corp. may also make a restricted payment prior to April 15, 2009 if, immediately after giving pro forma effect to such restricted payment and any indebtedness incurred to finance such restricted payment, its net indebtedness to adjusted EBITDA ratio would not exceed 3.75 to 1 and its net senior indebtedness to adjusted EBITDA ratio would not exceed 2.50 to 1. In addition, Holdings may make a restricted payment if, immediately after giving pro forma effect to such restricted payment and any indebtedness incurred to finance such restricted payment, its net indebtedness to adjusted EBITDA ratio would not exceed 4.25 to 1.0. Notwithstanding such restrictions, the indentures permit an aggregate of $45.0 million and $75.0 million of such payments to be made by Acquisition Corp. and Holdings, respectively, whether or not there is availability under the formula or the conditions to its use are met. Acquisition Corp.'s senior secured credit agreement permits Acquisition Corp. to make additional restricted payments to Holdings, the proceeds of which may be utilized by Holdings to make additional restricted payments, in an aggregate amount not to exceed $10.0 million (such amount subject to increase to $35.0 million if the leverage ratio as of the last day of the immediately preceding four fiscal quarters was less than 4.0 to 1 and to $50.0 million if the leverage ratio as of the last day of the immediately preceding four fiscal quarters was less than 3.5 to 1), and subject to further increase in an amount equal to 50% of cumulative excess cash flow that is not otherwise applied pursuant to Acquisition Corp.'s senior secured credit agreement, and, in addition, permits Acquisition Corp. to make restricted payments to Holdings, the proceeds of which may be utilized by Holdings to make additional restricted payments not to exceed $90 million in any fiscal year, provided that the proceeds of such restricted payments shall be applied solely to pay cash dividends on the Company's common stock. Furthermore, Holdings' subsidiaries will be permitted under the terms of Acquisition Corp.'s existing senior secured credit agreement, as it may be amended, and under other indebtedness, to incur additional indebtedness that may restrict or prohibit the making of distributions, the payment of dividends or the making of loans by such subsidiaries to Holdings.

Initial Common Stock Offering

In May 2005, we completed the Initial Common Stock Offering. Prior to the consummation of the Initial Common Stock Offering, we, among other things, renamed all of our outstanding shares of Class A Common Stock as common stock and authorized an approximately 1,139 for 1 split of our common stock. We contributed the net proceeds from the Initial Common Stock Offering of $517 million to Holdings as an equity capital contribution. Holdings used all of such funds and approximately $57 million of cash received through dividends from Acquisition Corp. to redeem all outstanding Holdings Floating Rate Notes, all outstanding Holdings PIK Notes and 35% of the aggregate principal amount of the outstanding Holdings Discount Notes, including redemption premiums and interest obligations through the date of redemption.

Source: Warner Music Group C, 10-Q, August 03, 2006

Dividends

We intend to pay regular quarterly dividends on our common stock outstanding in an amount not to exceed $80 million per year. Any decision to declare and pay dividends in the future will be made at the discretion of our board of directors and will depend on, among other things, our results of operations, cash requirements, financial condition, contractual restrictions and other factors our board of directors may deem relevant.

On October 3, 2005, December 29, 2005, March 14, 2006 and June 7, 2006, we declared dividends on our outstanding common stock at a rate of $0.13 per share. The dividends were paid on November 23, 2005, February 17, 2006, May 3, 2006 and July 27, 2006, respectively, except for the portion of the dividends with respect to unvested restricted stock, which will be paid at such time as such shares become vested.

During the nine months ended June 30, 2006, 2,479,501 shares of restricted stock purchased by or awarded to certain employees of the Company vested.

Covenant Compliance

Our senior secured credit facility requires us to maintain certain covenants including a Leverage Ratio and an Interest Coverage Ratio, as such terms are defined in the credit facility. The credit facility also contains covenants that, among other things, restrict our ability to incur additional debt. The occurrence of an event of default under the credit facility could result in all amounts outstanding under the facility to be immediately due and payable, which could have a material adverse impact on our results of operations, financial position and cash flow. As of June 30, 2006, we were in compliance with all covenants under the credit facility.

Our borrowing arrangements, including the Holding Notes and the Acquisition Corp. Subordinated Notes contain certain financial covenants, which limit the ability of our restricted subsidiaries as defined in the indentures governing the notes to, among other things, incur additional indebtedness, issue certain preferred shares, pay dividends, make certain investments, sell certain assets, and consolidate, merge, sell or otherwise dispose of all, or some of, our assets. In order for Acquisition Corp. and Holdings Corp. to incur additional debt or make certain restricted payments using certain exceptions provided for in the indentures governing the Acquisition Corp Subordinated Notes and the Holdings Notes, the Fixed Charge Coverage Ratio, as defined in the indentures agreements governing the notes, must exceed a 2.0 to 1.0 ratio. Fixed Charges are defined in the indentures governing the Holdings Notes and the Acquisition Corp. Subordinated Notes as consolidated interest expense excluding certain non-cash interest expense.

In order for Acquisition Corp. to make certain restricted payments, including payments to Holdings on a pro forma basis after giving effect to such payments, its Net Indebtedness to Adjusted EBITDA ratio and Net Senior Indebtedness to Adjusted EBITDA ratio, as defined in the indenture agreement governing the Acquisition Corp. Subordinated Notes, need to be lower than 3.75x and 2.5x, respectively, at the time of the restricted payment. In order for Holdings to make certain restricted payments, including payments to Warner Music Group Corp., its Net Indebtedness to Adjusted EBITDA ratio, as defined in the indenture agreement governing the Holdings Notes, needs to be lower than 4.25x at the time of the restricted payment.

Acquisition Corp. and Holdings may make additional restricted payments using certain other exceptions provided for in the indentures governing the Acquisition Corp. Subordinated Notes and Holdings Notes, respectively.

Summary

Management believes that future funds generated from our operations and available borrowing capacity will be sufficient to fund our debt service requirements, working capital requirements, capital expenditure requirements, payment of regular dividends on our common stock and the remaining one-time costs associated with the execution of the restructuring plan for the foreseeable future. However, our ability to continue to fund these items and to reduce debt may be affected by general economic, financial, competitive, legislative and regulatory factors, as well as other industry-specific factors such as the ability to control music piracy.

Source: Warner Music Group C, 10-Q, August 03, 2006

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As discussed in Note 22 to our audited consolidated financial statements for the twelve months ended September 30, 2005, the Company is exposed to market risk arising from changes in market rates and prices, including movements in foreign currency exchange rates and interest rates. As of June 30, 2006, other than as described below, there have been no material changes to the Company's exposure to market risk since September 30, 2005.

We have transactional exposure to changes in foreign currency exchange rates relative to the U.S. dollar due to the global scope of our operations. We use foreign exchange contracts, primarily to hedge the risk that unremitted or future royalties and license fees owed to our 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. We focus on managing the level of exposure to the risk of foreign current exchange rate fluctuations on our major currencies, which include the British pound sterling, euro, Japanese yen, Canadian dollar and Australian dollar. The Company did not enter into any significant foreign exchange forward contracts during the nine months ended June 30, 2006 or subsequent to June 30, 2006.

We are exposed to foreign currency exchange rate risk with respect to our £100 million principal amount of Sterling-denominated notes that were issued in April 2004. These sterling notes mature on April 15, 2014. As of June 30, 2006, the carrying value of these Sterling notes was $183 million. However, a weakening or strengthening of the U.S. dollar compared to the British Pound Sterling would not have an impact on the fair value of these Sterling notes, as these notes are completely hedged as of June 30, 2006. We did not enter into any additional hedges related to this debt subsequent to June 30,2006.

We are exposed to interest rate risk with respect to our floating rate debt. During the nine months ended June 30, 2006, we extended the terms of certain existing interest rate swap agreements. As of June 30, 2006 we had total interest rate swap agreements in place to hedge total notional amounts of $897 million. Under existing interest rate swap agreements, we agreed to receive floating-rate payments (based on three-month LIBOR rates) in exchange for fixed-rate payments. We did not enter into any additional interest rate swap agreements subsequent to June 30, 2006.

We monitor our positions with, and the credit quality of, the financial institutions that are party to any of our financial transactions. Credit risk relating to the interest rate swaps is considered low because the swaps are entered into with strong, credit-worthy counterparties, and the credit risk is confined to the net settlement of the interest over the remaining life of the swaps.

Source: Warner Music Group C, 10-Q, August 03, 2006

ITEM 4. CONTROLS AND PROCEDURES

Certification

The certifications of the principal executive officer and the principal financial officer (or persons performing similar functions) required by Rules 13a–15(e) and 15d–15(e) of the Securities Exchange Act of 1934, as amended (the "Certifications") are filed as exhibits to this report. This section of the report contains the information concerning the evaluation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a–15(e) and 15d–15(e)) ("Disclosure Controls") and changes to internal control over financial reporting (as defined in Exchange Act Rules 13a–15(f) and 15d–15(f)) ("Internal Controls") referred to in the Certifications and this information should be read in conjunction with the Certifications for a more complete understanding of the topics presented.

Introduction

The Company became subject to the periodic and other reporting requirements of the Securities Exchange Act of 1934, as amended, on May 10, 2005, the effective date of our registration statement relating to our Initial Common Stock Offering. Acquisition Corp., our wholly owned subsidiary, became subject to the periodic and other reporting requirements of the Exchange Act on February 10, 2005, the effective date of Acquisition Corp.'s registration statement relating to its exchange offer to exchange outstanding unregistered notes for freely tradeable exchange notes that were registered under the Securities Act of 1933, as amended.

SEC rules define "disclosure controls and procedures" as controls and procedures that are designed to ensure that information required to be disclosed by public companies in the reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by public companies in the reports that they file or submit under the Exchange Act is accumulated and communicated to a company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

SEC rules define "internal control over financial reporting" as a process designed by, or under the supervision of, a public company's principal executive and principal financial officers, or persons performing similar functions, and effected by our board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles, or U.S. GAAP, including those policies and procedures that: (i) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the company, (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. GAAP, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

Our management, including the principal executive officer and principal financial officer, does not expect that our Disclosure Controls or Internal Controls will prevent or detect all error and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the limitations in any and all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our company have been detected. Further, the design of any control system is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Because of these inherent limitations in a cost–effective control

Source: Warner Music Group C, 10-Q, August 03, 2006

system, misstatements due to error or fraud may occur and not be detected even when effective Disclosure Controls and Internal Controls are in place.

Internal Controls

In connection with our audit for our 2005 fiscal year-end, our outside auditors identified a material weakness in our internal controls. A material weakness, as defined by the Public Company Accounting Oversight Board, is a significant deficiency that by itself, or in combination with other significant deficiencies, results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. Specifically, our outside auditors noted that our domestic operations currently use different royalty systems, which has created certain complexities in reconciling royalty expense and payables. While we recognize that additional staff and enhancements to our current royalty systems are needed to cope with current requirements in royalty processing until a new system can be developed, we may not be able to hire and train additional staff. See also "Risk Factors—Our outside auditors have identified weaknesses in our internal controls that could affect our ability to ensure reliable financial reports."

Evaluation of Disclosure Controls and Procedures

Based on our management's evaluation (with the participation of our principal executive officer and principal financial officer), as of the end of the period covered by this report and as a result of the weakness in our internal controls described above and below, our principal executive officer and principal financial officer have concluded that our Disclosure Controls need to be improved so that they will provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act will be recorded, processed, summarized and reported within the time periods specified in SEC rules and forms. In addition, we continue to review our disclosure controls and procedures during the transition to a stand-alone business with the objective of implementing comprehensive periodic reporting standards as well as addressing the weaknesses in Internal Controls identified by our outside auditors. We will continue to devote resources to improve our controls and remedy the weakness related to our domestic royalty systems identified during the completion of the most recent audit for the 2005 fiscal year-end.

Changes in Internal Control over Financial Reporting

We are committed to maintaining high standards of internal control over financial reporting, corporate governance and public disclosure and continue to improve and refine our Internal Controls as an ongoing process and will continue to take corrective actions and implement improvements as appropriate.

There have been no changes in our Internal Controls over financial reporting or other factors during the period ended June 30, 2006 that have materially affected, or are reasonably likely to materially affect, our Internal Controls.

Institution of Internal Controls in compliance with Section 404 of Sarbanes-Oxley

As a result of our registration with the Securities and Exchange Commission, we will be required to comply with Section 404 of the Sarbanes-Oxley Act of 2002 and regulations promulgated thereunder as of September 30, 2006. We are currently performing the system and process evaluation and testing required (and any necessary remediation) in an effort to comply with management certification and auditor attestation requirements of Section 404. In the course of our ongoing evaluation, we have identified areas of our internal controls requiring improvement, and plan to design enhanced processes and controls to address these and any other issues that might be identified through this review. As a result, we expect to incur additional expenses and diversion of management's time. We cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or the impact of the same on our operations and may not be able to ensure that the process is

Source: Warner Music Group C, 10-Q, August 03, 2006

effective or that the internal controls are or will be effective in a timely manner. If we are not able to implement the requirements of Section 404 in a timely manner or with adequate compliance, our independent auditors may not be able to certify as to the effectiveness of our internal control over financial reporting and we may be subject to sanctions or investigation by regulatory authorities, such as the Securities and Exchange Commission. As a result, there could be an adverse reaction in the financial markets due to loss of confidence in the reliability of our financial statements. In addition, we may be required to incur costs in improving our internal control system and the hiring of additional personnel. Any such action could adversely affect our results. See also "Risk Factors—Our internal controls over financial reporting may not be adequate and our independent auditors may not be able to certify as to their adequacy, which could have a significant affect on our business and reputation."

Source: Warner Music Group C, 10-Q, August 03, 2006

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Radio Promotion Activities

On September 7, 2004, November 22, 2004 and March 31, 2005, the Attorney General of the State of New York served us with requests for information in connection with an industry–wide investigation of the relationship between music companies and radio stations, including the use of independent promoters and accounting for any such payments. The investigation was pursuant to New York Executive Law §63(12) and New York General Business Law §349, both of which are consumer fraud statutes. On November 22, 2005 we reached a settlement with the Attorney General in connection with this investigation. As part of such settlement, we agreed to make $5 million in charitable payments and to abide by a list of permissible and impermissible promotional activities. The Attorney General has also reached settlements with all of the other major music companies in connection with this investigation. Two independent labels have filed related antitrust suits against us alleging that our radio promotion activities are anticompetitive. *Radikal Records, Inc. v. Warner Music Group, et al.* was filed on March 21, 2006 in U.S. District Court in the Central District of California, Western Division. *TSR Records, Inc. v. Warner Music Group, et al.* was filed on March 28, 2006 in U.S. District Court in the Central District of California, Western Division. We filed a Notice of Related Case and were successful in having both of these cases consolidated. On May 23, 2006, we filed a Motion to Dismiss in both cases. Decisions on these motions are pending. The Company intends to defend against these lawsuits vigorously, but is unable to predict the outcome of these suits. Any litigation we may become involved in as a result of our settlement with the Attorney General, regardless of the merits of the claim, could be costly and divert the time and resources of management.

Pricing of Digital Music Downloads

On December 20, 2005 and February 3, 2006, the Attorney General of the State of New York served us with requests for information in the form of a subpoena duces tecum and subpoena ad testificandum in connection with an industry–wide investigation as to whether the practices of industry participants concerning the pricing of digital music downloads violate Section 1 of the Sherman Act, New York State General Business Law §§ 340 et seq., New York Executive Law §63(12), and related statutes. On February 28, 2006, the U.S. Department of Justice served us with a request for information in the form of a Civil Investigative Demand as to whether its activities relating to the pricing of digitally downloaded music violate Section 1 of the Sherman Act (15 U.S.C. Section 1). The Company intends to fully cooperate with the Attorney General's and Department of Justice's industry–wide inquiries. Subsequent to the announcements of the above governmental investigations, a total of twenty–seven putative class action lawsuits concerning the pricing of digital music downloads have been filed. We have yet to be served in some of the cases, but we expect they will all be consolidated into one case. The lawsuits are all based on the same general subject matter as the Attorney General's request for information alleging conspiracy among record companies to fix prices for downloads and, according to some of the complaints, protect allegedly inflated prices for compact discs. The complaints generally seek unspecified compensatory, statutory and treble damages. We intend to defend against these lawsuits vigorously, but are unable to predict the outcome of these suits. Any litigation we may become involved in as a result of the inquiries of the Attorney General and Department of Justice, regardless of the merits of the claim, could be costly and divert the time and resources of management.

Other Matters

In addition to the matters discussed above, we are involved in other litigation arising in the normal course of our business. Management does not believe that any legal proceedings pending against us will have, individually, or in the aggregate, a material adverse effect on our business. However, we cannot predict with certainty the outcome of any litigation or the potential for future litigation. Regardless of the outcome, litigation can have an adverse impact on us, including our brand value, because of defense costs, diversion of management resources and other factors.

Source: Warner Music Group C, 10-Q, August 03, 2006

ITEM 1A. RISK FACTORS

You should carefully consider the following risks and other information in this report before making an investment decision with respect to shares of our common stock. Any of the following risks could materially and adversely affect our business, financial condition or results of operations.

Risks Related to our Business

Increased costs associated with corporate governance compliance may significantly affect our results of operations.

Prior to our acquisition by the Investor Group in 2004, we were a business division of Time Warner. In addition we completed our initial public offering in May 2005. Accordingly, we have limited experience operating as an independent public company implementing our own corporate governance practices. We expect the continued evaluation and implementation of corporate governance and securities disclosure and compliance practices in order to comply with these requirements will increase our legal compliance and financial reporting costs. In addition, they could make it more difficult for us to attract and retain qualified members of our board of directors, or qualified executive officers. Finally, director and officer liability insurance for public companies like us has become more difficult and more expensive to obtain, and we may be required to accept reduced coverage or incur higher costs to obtain coverage that is satisfactory to us and our officers or directors. We continue to evaluate and monitor regulatory developments and cannot estimate the timing or magnitude or additional costs we may incur as a result.

Our internal controls over financial reporting may not be adequate and our independent auditors may not be able to certify as to their adequacy, which could have a significant and adverse effect on our business and reputation.

We are evaluating our internal controls over financial reporting in order to allow management to report on, and our independent auditors to attest to, our internal controls over financial reporting, as required by Section 404 of the Sarbanes–Oxley Act of 2002 and rules and regulations of the SEC thereunder, which we refer to as Section 404. Section 404 requires a reporting company such as ours to, among other things, annually review and disclose its internal controls over financial reporting, and evaluate and disclose changes in its internal controls over financial reporting quarterly. We will be required to comply with Section 404 as of September 30, 2006. We are currently performing the system and process evaluation and testing required (and any necessary remediation) in an effort to comply with management certification and auditor attestation requirements of Section 404. In the course of our ongoing evaluation, we have identified areas of our internal controls requiring improvement, and plan to design enhanced processes and controls to address these and any other issues that might be identified through this review. As a result, we expect to incur additional expenses and diversion of management's time. We cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or the impact of the same on our operations and may not be able to ensure that the process is effective or that the internal controls are or will be effective in a timely manner. If we are not able to implement the requirements of Section 404 in a timely manner or with adequate compliance, our independent auditors may not be able to certify as to the effectiveness of our internal control over financial reporting and we may be subject to sanctions or investigation by regulatory authorities, such as the Securities and Exchange Commission. As a result, there could be an adverse reaction in the financial markets due to a loss of confidence in the reliability of our financial statements. In addition, we may be required to incur costs in improving our internal control system and the hiring of additional personnel. Any such action could adversely affect our results.

Our outside auditors have identified weaknesses in our internal controls that could affect our ability to ensure reliable financial reports.

In addition to our evaluation of internal controls under Section 404 of the Sarbanes–Oxley Act and any areas requiring improvement that we identify as part of that process, in connection with our most recent audit, our outside auditors identified a material weakness related to our domestic royalty controls. A material weakness, as

Source: Warner Music Group C, 10-Q, August 03, 2006

defined by the Public Company Accounting Oversight Board, is a significant deficiency that by itself, or in combination with other significant deficiencies, results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

Our outside auditors noted that our domestic operations currently use different royalty systems, which has created certain complexities in reconciling royalty expense and payables. While we recognize that additional staff and enhancements to our current royalty systems are needed to cope with current requirements in royalty processing until a new system can be developed, we may not be able to hire and train additional staff. While we have begun to take actions to address the issues surrounding our royalty systems, including hiring outside resources to assist our internal personnel with royalties accounting and entering into a joint venture with Universal Music Group, Exigen Group and Lightspeed Venture Partners to build a new uniform royalty system for all U.S. operations, additional measures will be necessary and these measures along with other measures we expect to take to improve our internal controls may not be sufficient to address the issues identified by our outside auditors or ensure that our internal controls are effective. If we are unable to provide reliable financial reports our business and prospects could suffer material adverse effects and our share price could be adversely affected.

The recorded music industry has been declining and may continue to decline, which may adversely affect our prospects and our results of operations.

Illegal downloading of music from the Internet, CD-R piracy, industrial piracy, economic recession, bankruptcies of record wholesalers and retailers and growing competition for consumer discretionary spending and retail shelf space may all be contributing to a declining recorded music industry. Additionally, the period of growth in recorded music sales driven by the introduction and penetration of the CD format has ended. The value of worldwide sales (recorded music, excluding sales of digital tracks), as reported by the International Federation of the Phonographic Industry (IFPI) at fixed 2004 exchange rates, fell as the music industry witnessed a decline of 1.6% from 1999 to 2000, 1.3% from 2000 to 2001, 6.7% from 2001 to 2002, 7.4% from 2002 to 2003, 1.3% from 2003 to 2004 and 3.0% from 2004 to 2005. As of July 30, 2006, year-to-date U.S. recorded music sales (excluding sales of digital tracks) are down approximately 5.5% year-over-year. However, new formats for selling recorded music product have been created, including the legal downloading of digital music using the Internet and DVD-Audio formats and the distribution of music on mobile devices, and revenue streams from these new markets are beginning to emerge. As reported by the International Federation of the Phonographic Industry (IFPI), sales of music via the internet and mobile phones generated sales of $1.1 billion for record companies in 2005, up from $380 million in the prior-year and sales of music through new avenues such as digital tracks are beginning to offset the declines seen in prior-years. However, it is too soon to determine if the industry has stabilized or the impact of sales of music through new channels might have on the industry and the recorded music industry performance may continue to negatively impact our operating results. A declining recorded music industry is likely to lead to reduced levels of revenue and operating income generated by our Recorded Music business. Additionally, a declining recorded music industry is also likely to have a negative impact on our Music Publishing business, which generates a significant portion of its revenues from mechanical royalties, primarily from the sale of music in CD and other recorded music formats.

There may be downward pressure on our pricing and our profit margins.

There are a variety of factors which could cause us to reduce our prices and erode our profit margins. They are, among others, increased price competition among record companies resulting from the Universal and Sony BMG recorded music duopoly, price competition from the sale of motion pictures in DVD-Video format and videogames, the negotiating leverage of mass merchandisers, big box retailers and distributors of digital music, the increased costs of doing business with mass merchandisers and big box retailers as a result of complying with operating procedures that are unique to their needs, the adoption by record companies of initially lower-margin formats such as DVD-Audio and any changes in costs associated with new digital formats. See "Risk Factors—We may be materially and adversely affected by the formation of Sony BMG Music Entertainment."

Source: Warner Music Group C, 10-Q, August 03, 2006

Our prospects and financial results may be adversely affected if we fail to identify, sign and retain artists and songwriters and by the existence or absence of superstar releases and by local economic conditions in the countries in which we operate.

We are dependent on identifying, signing and retaining artists with long-term potential, whose debut albums are well received on release, whose subsequent albums are anticipated by consumers and whose music will continue to generate sales as part of our catalog for years to come. The competition among record companies for such talent is intense. Competition among record companies to sell records is also intense and the marketing expenditures necessary to compete have increased as well. We are also dependent on signing and retaining songwriters who will write the hit songs of today and the classics of tomorrow under terms that are economically attractive to us. Our competitive position is dependent on our continuing ability to attract and develop talent whose work can achieve a high degree of public acceptance. Our financial results may be adversely affected if we are unable to identify, sign and retain such artists and songwriters under terms that are economically attractive to us. Our financial results may also be affected by the existence or absence of superstar artist releases during a particular period. Some music industry observers believe that the number of superstar acts with long-term appeal, both in terms of catalog sales and future releases, has declined in recent years. Additionally, our financial results are generally affected by the general economic and retail environment of the countries in which we operate, as well as the appeal of our recorded music catalog and our music publishing library.

We may have difficulty addressing the threats to our business associated with home copying and Internet downloading.

The combined effect of the decreasing cost of electronic and computer equipment and related technology such as CD burners and the conversion of music into digital formats have made it easier for consumers to create unauthorized copies of our recordings in the form of, for example, CDs and MP3 files. An estimated 20 billion songs were illegally swapped or downloaded worldwide in 2005, according to IFPI. A substantial portion of our revenue comes from the sale of audio products that are potentially subject to unauthorized consumer copying and widespread dissemination on the Internet without an economic return to us. We are working to control this problem through litigation, by lobbying governments for new, stronger copyright protection laws and more stringent enforcement of current laws and by establishing legitimate new media business models. We cannot give any assurances that such measures will be effective. If we fail to obtain appropriate relief through the judicial process or the complete enforcement of judicial decisions issued in our favor (or if judicial decisions are not in our favor), if we are unsuccessful in our efforts to lobby governments to enact and enforce stronger legal penalties for copyright infringement or if we fail to develop effective means of protecting our intellectual property (whether copyrights or other rights such as patents, trademarks and trade secrets) or entertainment-related products or services, our results of operations, financial position and prospects may suffer.

Organized industrial piracy may lead to decreased sales.

The global organized commercial pirate trade is a significant threat to the music industry. Worldwide, industrial pirated music (which encompasses unauthorized physical copies manufactured for sale but does not include Internet downloads or home CD burning) is estimated to have generated over $4.5 billion in revenues in 2005, according to IFPI. IFPI estimates that 1.2 billion pirated units were manufactured in 2005. According to IFPI estimates, approximately 37% of all music CDs sold worldwide in 2005 were pirated. Unauthorized copies and piracy contributed to the decrease in the volume of legitimate sales and put pressure on the price of legitimate sales. They have had, and may continue to have, an adverse effect on our business.

Our involvement in intellectual property litigation could adversely affect our business.

Our business is highly dependent upon intellectual property, a field that has encountered increasing litigation in recent years. If we are alleged to infringe the intellectual property rights of a third party, any litigation to defend the claim could be costly and would divert the time and resources of management, regardless

Source: Warner Music Group C, 10-Q, August 03, 2006

of the merits of the claim. There can be no assurance that we would prevail in any such litigation. If we were to lose a litigation relating to intellectual property, we could be forced to pay monetary damages and to cease the sale of certain products or the use of certain technology. Any of the foregoing may adversely affect our business.

Due to the nature of our business, our results of operations and cash flows may fluctuate significantly from period to period.

Our net sales, operating income and profitability, like those of other companies in the music business, are largely affected by the number and quality of albums that we release, our release schedule, and, more importantly, the consumer demand for these releases. We also make advance payments to recording artists and songwriters, which impact our operating cash flows. The timing of album releases and advance payments is largely based on business and other considerations and is made without regard to the timing of the release of our financial results. We report results of operations quarterly and our results of operations and cash flows in any reporting period may be materially affected by the timing of releases and advance payments, which may result in significant fluctuations from period to period.

Our operating results fluctuate on a seasonal and quarterly basis, and, in the event we do not generate sufficient net sales in our first fiscal quarter, we may not be able to meet our debt service and other obligations.

Our business is seasonal. For the fiscal year ended September 30, 2005, we derived approximately 83% of our revenues from our Recorded Music business. In the recorded music business, purchases are heavily weighted towards the last three months of the calendar year, which represent our first quarter under our September 30 fiscal year. Historically, we have realized approximately 35% of recorded music net sales worldwide during the last three months of the calendar year, making those three months (i.e., our new first fiscal quarter) material to our full-year performance. We realized 32% of recorded music calendar year net sales during the last three months of calendar 2005 and 2004. This sales seasonality affects our operating cash flow from quarter to quarter. We cannot assure you that our recorded music net sales for the last three months of any calendar year will continue to be sufficient to meet our obligations or that they will be higher than such net sales for our other quarters. In the event that we do not derive sufficient recorded music net sales in such last three months, we may not be able to meet our debt service requirements, working capital requirements, capital expenditure requirements, payment of regular dividends on our common stock and other obligations. As digital revenue increases as a percentage of our total revenue, this may affect the overall seasonality of our business. For example, sales of MP3 players or gift cards to purchase digital music sold in the holiday season tend to result in sales of digital music in subsequent periods. However, seasonality with respect to the sale of music in new formats, such as digital, are still developing.

We may be unable to compete successfully in the highly competitive markets in which we operate and we may suffer reduced profits as a result.

The industry in which we operate is highly competitive, is based on consumer preferences and is rapidly changing. Additionally, the music industry requires substantial human and capital resources. We compete with other recorded music companies and music publishers to identify and sign new recording artists and songwriters who subsequently achieve long-term success and to renew agreements with established artists and songwriters. In addition, our competitors may from time to time reduce their prices in an effort to expand market share and introduce new services, or improve the quality of their products or services. We may lose business if we are unable to sign successful artists or songwriters or to match the prices or the quality of products and services, offered by our competitors. Our Music Publishing business competes not only with other music publishing companies, but also with songwriters who publish their own works. Our Recorded Music business is to a large extent dependent on technological developments, including access to and selection and viability of new technologies, and is subject to potential pressure from competitors as a result of their technological developments. For example, our Recorded Music business may be adversely affected by technological

Source: Warner Music Group C, 10-Q, August 03, 2006

developments that facilitate the piracy of music, such as Internet peer-to-peer file-sharing and CD-R activity; by its inability to enforce our intellectual property rights in digital environments; and by its failure to develop a successful business model applicable to a digital online environment, including such channels of distribution as satellite radio. It also faces competition from other forms of entertainment and leisure activities, such as cable and satellite television, pre-recorded films on videocassettes and DVD, the Internet and computer and videogames.

Our business operations in some countries subject us to trends, developments or other events in foreign countries which may affect us adversely.

We are a global company with strong local presences, which have become increasingly important as the popularity of music originating from a country's own language and culture has increased in recent years. Our mix of national and international recording artists and songwriters provides a significant degree of diversification for our music portfolio. However, our creative content does not necessarily enjoy universal appeal. As a result, our results can be affected not only by general industry trends, but also by trends, developments or other events in individual countries, including:

- limited legal protection and enforcement of intellectual property rights;
- restrictions on the repatriation of capital;
- differences and unexpected changes in regulatory environment, including environmental, health and safety, local planning, zoning and labor laws, rules and regulations;
- varying tax regimes which could adversely affect our results of operations or cash flows, including regulations relating to transfer pricing and withholding taxes on remittances and other payments by subsidiaries and joint ventures;
- exposure to different legal standards and enforcement mechanisms and the associated cost of compliance;
- difficulties in attracting and retaining qualified management and employees or rationalizing our workforce;
- tariffs, duties, export controls and other trade barriers;
- longer accounts receivable settlement cycles and difficulties in collecting accounts receivable;
- recessionary trends, inflation and instability of the financial markets;
- higher interest rates; and
- political instability.

We may not be able to insure or hedge against these risks, and we may not be able to ensure compliance with all of the applicable regulations without incurring additional costs. Furthermore, financing may not be available in countries with less than investment-grade sovereign credit ratings. As a result, it may be difficult to create or maintain profit-making operations in developing countries.

In addition, our results can be affected by trends, developments and other events in individual countries. There can be no assurance that in the future other country-specific trends, developments or other events will not have such a significant adverse effect on our business, results of operations or financial condition.

Our business may be adversely affected by competitive market conditions and we may not be able to execute our business strategy.

We intend to increase revenues and cash flow through a business strategy which requires us to, among other things, continue to maximize the value of our music assets, significantly reduce costs to maximize flexibility and

Source: Warner Music Group C, 10-Q, August 03, 2006

adjust to new realities of the market, continue to act to contain digital piracy and capitalize on digital distribution and emerging technologies.

Each of these initiatives requires sustained management focus, organization and coordination over significant periods of time. Each of these initiatives also requires success in building relationships with third parties and in anticipating and keeping up with technological developments and consumer preferences. The results of the strategy and the success of our implementation of this strategy will not be known for some time in the future. If we are unable to implement the strategy successfully or properly react to changes in market conditions, our financial condition, results of operations and cash flows could be adversely affected.

Our ability to operate effectively could be impaired if we fail to attract and retain our executive officers.

Our success depends, in part, upon the continuing contributions of our executive officers. Although we have employment agreements with our executive officers, there is no guarantee that they will not leave. The loss of the services of any of our executive officers or the failure to attract other executive officers could have a material adverse effect on our business or our business prospects.

Legitimate channels for digital distribution of our creative content are a recent development, and their impact on our business is unclear and may be adverse.

We have positioned ourselves to take advantage of the Internet and wireless technology as a sales distribution channel and believe that the development of legitimate channels for digital music distribution holds promise for us in the future. However, legitimate channels for digital distribution are a recent development and we cannot predict their impact on our business. In digital formats, certain costs associated with physical products such as manufacturing, distribution, inventory and return costs do not apply. While there are some digital-specific variable costs and infrastructure investments necessary to produce, market and sell music in digital formats, we believe it is reasonable to expect that we will generally derive a higher contribution margin from digital versus physical sales. However, we cannot assure you that we will generally continue to achieve higher margins from digital sales. Any legitimate digital distribution channel that does develop may result in lower or less profitable sales for us than comparable physical sales. In addition, the transition to greater sales through digital channels introduces uncertainty regarding the potential impact of the "unbundling" of the album on our business. While recent studies have indicated that consumers spend more on music in general when they begin to purchase music in digital form than previously, it remains unclear how consumer behavior will change when faced with the prospect of purchasing only their favorite tracks from a given album rather than the entire album. In addition, if piracy continues unabated and legitimate digital distribution channels fail to gain consumer acceptance, our results of operations could be harmed.

A significant portion of our music publishing revenues is subject to rate regulation either by government entities or by local third-party collection societies throughout the world and rates on other income streams may be set by arbitration proceedings, which may limit our profitability.

Mechanical royalties and performance royalties are the two largest sources of income to our Music Publishing business and mechanical royalties are a significant expense to our Recorded Music business. In the U.S., mechanical rates are set pursuant to industry negotiations contemplated by the U.S. Copyright Act and performance rates are set by performing rights societies and subject to challenge by performing rights licensees. Outside the U.S., mechanical and performance rates are typically negotiated on an industry-wide basis. The mechanical and performance rates set pursuant to such processes may adversely affect us by limiting our ability to increase the profitability of our Music Publishing business. If the mechanical rates are set too high it may also adversely affect us by limiting our ability to increase the profitability of our Recorded Music business. In addition, rates our Recorded Music business receives in the U.S. for, among other sources of income and potential income, the statutory license for eligible non-subscription services to perform sound recordings publicly

Source: Warner Music Group C, 10-Q, August 03, 2006

by means of digital audio transmissions ("webcasting"), the statutory license to make ephemeral recordings of sound recordings for use of sound recordings and the statutory license for use of our content on satellite radio are set by an arbitration process under the U.S. Copyright Act unless rates are determined through voluntary negotiations. If the rates for these and other income sources are set too low through this process, it could have a material adverse impact on our Recorded Music business or our business prospects.

Unfavorable currency exchange rate fluctuations could adversely affect our results of operations.

The reporting currency for our financial statements is the U.S. dollar. We have substantial assets, liabilities, revenues and costs denominated in currencies other than U.S. dollars. To prepare our consolidated financial statements, we must translate those assets, liabilities, revenues and expenses into U.S. dollars at then-applicable exchange rates. Consequently, increases and decreases in the value of the U.S. dollar versus other currencies will affect the amount of these items in our consolidated financial statements, even if their value has not changed in their original currency. These translations could result in significant changes to our results of operations from period to period. For the fiscal year ended September 30, 2005, approximately 52% of our revenues related to operations in foreign territories. For the nine months ended June 30, 2006, approximately 52% of our revenues related to operations in foreign territories. From time to time, we enter into foreign exchange contracts to hedge the risk of unfavorable foreign currency exchange rate movements. As of June 30, 2006, we have hedged our material foreign currency exposures related to royalty payments remitted between our foreign affiliates and our U.S. affiliates for the balance of the fiscal year.

We may not have full control and ability to direct the operations we conduct through joint ventures.

We currently have interests in a number of joint ventures and may in the future enter into further joint ventures as a means of conducting our business. In addition, we structure certain of our relationships with recording artists and songwriters as joint ventures. We may not be able to fully control the operations and the assets of our joint ventures, and we may not be able to make major decisions or may not be able to take timely actions with respect to our joint ventures unless our joint venture partners agree.

The enactment of legislation limiting the terms by which an individual can be bound under a "personal services" contract could impair our ability to retain the services of key artists.

California Labor Code Section 2855 ("Section 2855") limits the duration of time any individual can be bound under a contract for "personal services" to a maximum of seven years. In 1987, Subsection (b) was added, which provides a limited exception to Section 2855 for recording contracts, creating a damages remedy for record companies. Legislation was introduced in California to repeal Subsection (b) and then withdrawn. Legislation was introduced in New York to create a statute similar to Section 2855, which did not advance. There is no assurance that New York, California or any other state will not reintroduce or introduce similar legislation in the future. In fact, legislation similar to Section 2855 has been introduced in the New York Assembly. The repeal of Subsection (b) of Section 2855 and/or the passage of legislation similar to Section 2855 by other states could materially affect our results of operations and financial position.

We face a potential loss of catalog if it is determined that recording artists have a right to recapture rights in their recordings under the U.S. Copyright Act.

The U.S. Copyright Act provides authors (or their heirs) a right to terminate licenses or assignments of rights in their copyrighted works. This right does not apply to works that are "works made for hire". Since the effective date of U.S. copyrightability for sound recordings (February 15, 1972), virtually all of our agreements with recording artists provide that such recording artists render services under an employment-for-hire relationship. A termination right exists under the U.S. Copyright Act for musical compositions that are not "works made for hire". If any of our commercially available recordings were determined not to be "works made

Source: Warner Music Group C, 10-Q, August 03, 2006

for hire", then the recording artists (or their heirs) could have the right to terminate the rights they granted to us, generally during a five-year period starting at the end of 35 years from the date of a post-1977 license or assignment (or, in the case of a pre-1978 grant in a pre-1978 recording, generally during a five-year period starting either at the end of 56 years from the date of copyright or on January 1, 1978, whichever is later). A termination of rights could have an adverse effect on our Recorded Music business. From time to time, authors (or their heirs) can terminate our rights in musical compositions. However, we believe the effect of those terminations is already reflected in the financial results of our Music Publishing business.

If we acquire or invest in other businesses, we will face certain risks inherent in such transactions.

We may acquire, make investments in, or enter into strategic alliances or joint ventures with, companies engaged in businesses that are similar or complementary to ours. If we make such acquisitions or investments or enter into strategic alliances, we will face certain risks inherent in such transactions. For example, gaining regulatory approval for significant acquisitions or investments could be a lengthy process and there can be no assurance of a successful outcome. We could face difficulties in managing and integrating newly acquired operations. Additionally, such transactions would divert management resources and may result in the loss of artists or songwriters from our rosters. We cannot assure you that if we make any future acquisitions, investments, strategic alliances or joint ventures that they will be completed in a timely manner, that they will be structured or financed in a way that will enhance our credit-worthiness and allow for continued payment of regular dividends or that they will meet our strategic objectives or otherwise be successful. Failure to effectively manage any of these transactions could result in material increases in costs or reductions in expected revenues, or both. See also "Management's Discussion and Analysis of Financial Condition and Results of Operations—Overview—Recent Developments."

We are controlled by entities that may have conflicts of interest with us.

The Investor Group controls a majority of our capital stock on a fully diluted basis. In addition, representatives of the Investor Group occupy substantially all of the seats on our board of directors and pursuant to a stockholders agreement, will have the right to appoint all of the independent directors to our board. As a result, the Investor Group has the ability to control our policies and operations, including the appointment of management, the entering into of mergers, acquisitions, sales of assets, divestitures and other extraordinary transactions, future issuances of our common stock or other securities, the payments of dividends, if any, on our common stock, the incurrence of debt by us and the amendment of our certificate of incorporation and bylaws. The Investor Group will have the ability to prevent any transaction that requires the approval of our board of directors or the stockholders regardless of whether or not other members of our board of directors or stockholders believe that any such transaction is in their own best interests. For example, the Investor Group could cause us to make acquisitions that increase our indebtedness or to sell revenue-generating assets. Additionally, the Investor Group are in the business of making investments in companies and may from time to time acquire and hold interests in businesses that compete directly or indirectly with us. The Investor Group may also pursue acquisition opportunities that may be complementary to our business, and, as a result, those acquisition opportunities may not be available to us. So long as the Investor Group continues to hold a majority of our outstanding common stock the Investor Group will be entitled to nominate a majority of our board of directors, and will have the ability to effectively control the vote in any election of directors. In addition, so long as the Investor Group continues to own a significant amount of our equity, even if such amount is less than 50%, they will continue to be able to strongly influence or effectively control our decisions.

Our reliance on one company for the manufacturing, packaging and physical distribution of our products in North America and Europe could have an adverse impact on our ability to meet our manufacturing, packaging and physical distribution requirements.

Cinram is currently our exclusive supplier of manufacturing, packaging and physical distribution services in North America and most of Europe. Accordingly, our continued ability to meet our manufacturing, packaging

Source: Warner Music Group C, 10-Q, August 03, 2006

and physical distribution requirements in those territories depends largely on Cinram's continued successful operation in accordance with the service level requirements mandated by us in our service agreements. If, for any reason, Cinram were to fail to meet contractually required service levels, we would have difficulty satisfying our commitments to our wholesale and retail customers, which could have an adverse impact on our revenues. Even though our agreements with Cinram give us a right to terminate based upon failure to meet mandated service levels, and there are several capable substitute suppliers, it might be difficult for us to switch to substitute suppliers for any such services, particularly in the short-term, and the delay and transition time associated with finding substitute suppliers could itself have an adverse impact on our revenues. In addition, our agreements with Cinram begin to expire in 2006. If we are unable to negotiate renewals of these agreements we would have to switch to substitute suppliers. Further, pricing negotiated with Cinram in future agreements may be less favorable than the existing agreements.

We may be materially and adversely affected by the formation of Sony BMG Music Entertainment.

In August 2004, Sony Music Entertainment ("Sony") and Bertelsmann Music Group ("BMG") merged their recorded music businesses to form Sony BMG Music Entertainment ("Sony BMG"). As a result, the recorded music market now consists of four major players (Universal, Sony BMG, EMI Recorded Music ("EMI") and us) rather than five (Universal, Sony, BMG, EMI and us). Prior to the formation of Sony BMG, there was one disproportionately large major, Universal, with approximately 25% market share and four other majors relatively equal in size with market shares ranging between 11% and 14%. Now there are two majors with 2004 global market shares over 25%, Universal and Sony BMG, and two significantly smaller majors, EMI and us, each with less than 15%. IFPI is in the process of gathering 2005 market data, but final data is not yet available. There is a threat that the change in the competitive landscape caused by the new Universal and Sony BMG duopoly could drive up the costs of artist signings and the costs of marketing and promoting records to our detriment. See also "Management's Discussion and Analysis of Financial Condition and Results of Operations—Overview—Recent Developments".

Risks Related to our Leverage

Our substantial leverage on a consolidated basis could adversely affect our ability to raise additional capital to fund our operations, limit our ability to react to changes in the economy or our industry and prevent us from meeting our obligations under our indebtedness.

We are highly leveraged. As of June 30, 2006, our total consolidated indebtedness was $2.251 billion. We have an additional $250 million available for borrowing under the revolving portion of our senior secured credit facility (less $2 million of current letters of credit).

Our high degree of leverage could have important consequences for you, including:

- making it more difficult for us and our subsidiaries to make payments on indebtedness;
- increasing our vulnerability to general economic and industry conditions;
- requiring a substantial portion of cash flow from operations to be dedicated to the payment of principal and interest on indebtedness, therefore reducing our ability to use our cash flow to fund our operations, capital expenditures and future business opportunities;
- exposing us to the risk of increased interest rates as certain of the borrowings of our subsidiaries, including borrowings under our senior secured credit facility, will be at variable rates of interest;
- limiting our ability and the ability of our subsidiaries to obtain additional financing for working capital, capital expenditures, product development, debt service requirements, acquisitions and general corporate or other purposes; and
- limiting our ability to adjust to changing market conditions and placing us at a competitive disadvantage compared to our competitors who are less highly leveraged.

Source: Warner Music Group C, 10-Q, August 03, 2006

We and our subsidiaries may be able to incur substantial additional indebtedness in the future, subject to the restrictions contained in our senior secured credit facility and the indentures relating to our outstanding notes. If new indebtedness is added to our current debt levels, the related risks that we and our subsidiaries now face could intensify.

We may not be able to generate sufficient cash to service all of our indebtedness, and may be forced to take other actions to satisfy our obligations under our indebtedness, which may not be successful.

Our ability to make scheduled payments on or to refinance our debt obligations depends on our financial condition and operating performance, which is subject to prevailing economic and competitive conditions and to certain financial, business and other factors beyond our control. We cannot assure you that we will maintain a level of cash flows from operating activities sufficient to permit us to pay the principal, premium, if any, and interest on our indebtedness, including the notes.

If our cash flows and capital resources are insufficient to fund our debt service obligations, we may be forced to reduce or delay investments in recording artists, and songwriters capital expenditures, or to sell assets, seek additional capital or restructure or refinance our indebtedness. These alternative measures may not be successful and may not permit us to meet our scheduled debt service obligations. In the absence of such operating results and resources, we could face substantial liquidity problems and might be required to dispose of material assets or operations to meet our debt service and other obligations. Our senior secured credit facility and the indenture governing our outstanding notes restrict our ability to dispose of assets and use the proceeds from dispositions. We may not be able to consummate those dispositions or to obtain the proceeds which we could realize from them and these proceeds may not be adequate to meet any debt service obligations then due.

Holdings also will be relying on Acquisition Corp. and its subsidiaries to make payments on the Holdings Notes. If Acquisition Corp. does not dividend funds to Holdings in an amount sufficient to make such payments, Holdings may default under the indenture governing the Holdings Notes, which would result in all such notes becoming due and payable. Because Acquisition Corp.'s debt agreements have covenants that limit its ability to make payments to Holdings, Holdings may not have access to funds in an amount sufficient to service its indebtedness.

Our debt agreements contain restrictions that limit our flexibility in operating our business.

Our senior secured credit agreement and the indentures governing our outstanding notes contain various covenants that limit our ability to engage in specified types of transactions. These covenants limit the ability of our restricted subsidiaries to, among other things:

- incur additional indebtedness or issue certain preferred shares;
- pay dividends on or make distributions in respect of our capital stock or make other restricted payments;
- make certain investments;
- sell certain assets;
- create liens on certain indebtedness without securing the notes;
- consolidate, merge, sell or otherwise dispose of all or substantially all of our assets;
- enter into certain transactions with our affiliates; and
- designate our subsidiaries as unrestricted subsidiaries.

In addition, under our senior secured credit agreement, our subsidiaries are required to satisfy and maintain specified financial ratios and other financial condition tests. Their ability to meet those financial ratios and tests

Source: Warner Music Group C, 10-Q, August 03, 2006

can be affected by events beyond our control, and they may not be able to meet those ratios and tests. A breach of any of these covenants could result in a default under our senior secured credit agreement. Upon the occurrence of an event of default under our senior secured credit agreement, the lenders could elect to declare all amounts outstanding under our senior secured credit agreement to be immediately due and payable and terminate all commitments to extend further credit. If we were unable to repay those amounts, the lenders under our senior secured credit agreement could proceed against the collateral granted to them to secure that indebtedness. We have pledged a significant portion of our assets as collateral under our senior secured credit agreement. If the lenders under our senior secured credit agreement accelerate the repayment of borrowings, we may not have sufficient assets to repay our senior secured credit agreement, as well as any unsecured indebtedness.

Risks Related to our Common Stock

We are a "controlled company" within the meaning of the New York Stock Exchange rules and, as a result, will qualify for, and intend to rely on, exemptions from certain corporate governance requirements.

The Investor Group controls a majority of our outstanding common stock. As a result, we are a "controlled company" within the meaning of the New York Stock Exchange corporate governance standards. Under the New York Stock Exchange rules, a company of which more than 50% of the voting power is held by an individual, a group, or another company is a "controlled company" and may elect not to comply with certain New York Stock Exchange corporate governance requirements, as applicable, including (1) the requirement that a majority of the board of directors consist of independent directors, (2) the requirement that we have a nominating/corporate governance committee that is composed entirely of independent directors with a written charter addressing the committee's purpose and responsibilities and (3) the requirement that we have a compensation committee that is composed entirely of independent directors with a written charter addressing the committee's purpose and responsibilities. We are and intend to continue to utilize these exemptions while we are a controlled company. As a result, we will not have a majority of independent directors nor will our nominating and corporate governance committee, which also serves as our executive committee, and compensation committee consist entirely of independent directors. Accordingly, you will not have the same protections afforded to stockholders of companies that are subject to all of the New York Stock Exchange corporate governance requirements.

Future sales of our shares could depress the market price of our common stock.

The market price of our common stock could decline as a result of sales of a large number of shares of common stock in the market or the perception that such sales could occur. These sales, or the possibility that these sales may occur, also might make it more difficult for us to sell equity securities in the future at a time and at a price that we deem appropriate. As of June 30, 2006 we had approximately 148.5 million shares of common stock outstanding. Approximately 107.5 million shares are held by the Investor Group and are eligible for resale from time to time, subject to contractual and Securities Act restrictions. The Investor Group has the ability to cause us to register the resale of their shares and certain other holders of our common stock, including members of our management, will be able to participate in such registration. In addition we have registered approximately 8.3 million shares of restricted common stock and approximately 8.4 million shares underlying options issued and that may be issued in the future pursuant to our benefit plans and arrangements on registration statements on Form S-8 and such shares may be sold as provided therein.

The market price of our common stock may be volatile, which could cause the value of your investment to decline.

Securities markets worldwide experience significant price and volume fluctuations. This market volatility, as well as general economic, market or potential conditions, could reduce the market price of our common stock in spite of our operating performance. In addition, our operating results could be below the expectations of securities analysts and investors, and in response, the market price of our common stock could decrease significantly. As a result, the market price of our common stock could decline below price at which you purchase

Source: Warner Music Group C, 10-Q, August 03, 2006

it. You may be unable to resell your shares of our common stock at or above such price. Among other factors that could affect our stock price are:

- actual or anticipated variations in operating results;
- changes in financial estimates by research analysts;
- actual or anticipated changes in economic, political or market conditions, such as recessions or international currency fluctuations;
- actual or anticipated changes in the regulatory environment affecting the music industry;
- changes in the retailing environment;
- changes in the market valuations of other music industry peers; and
- announcements by us or our competitors of significant acquisitions, strategic partnerships, divestitures, joint ventures or other strategic initiatives.

See "Risk Factors—Due to the nature of our business, our results of operations and cash flows may fluctuate significantly from period to period." In the past, following periods of volatility in the market price of a company's securities, stockholders have often instituted class action securities litigation against those companies. Such litigation, if instituted, could result in substantial costs and a diversion of management attention and resources, which could significantly harm our profitability and reputation.

Provisions in our Charter and amended and restated bylaws and Delaware law may discourage a takeover attempt.

Provisions contained in our Charter and amended and restated bylaws ("Bylaws") and Delaware law could make it more difficult for a third party to acquire us, even if doing so might be beneficial to our stockholders. Provisions of our Charter and Bylaws impose various procedural and other requirements, which could make it more difficult for shareholders to effect certain corporate actions. For example, our Charter authorizes our board of directors to determine the rights, preferences, privileges and restrictions of unissued series of preferred stock, without any vote or action by our shareholders. Thus, our board of directors can authorize and issue shares of preferred stock with voting or conversion rights that could adversely affect the voting or other rights of holders of our common stock. These rights may have the effect of delaying or deterring a change of control of our company. These provisions could limit the price that certain investors might be willing to pay in the future for shares of our common stock.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Item 2 is not applicable and has been omitted.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Item 3 is not applicable and has been omitted.

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

Item 4 is not applicable and has been omitted.

ITEM 5. OTHER INFORMATION

Item 5 is not applicable and has been omitted.

Source: Warner Music Group C, 10-Q, August 03, 2006

ITEM 6. EXHIBITS

3.1	Amended and Restated Certificate of Incorporation of Warner Music Group Corp. (1)
3.2	Amended and Restated Bylaws of Warner Music Group Corp. (1)
10.1	Sixth Supplemental Indenture, dated as of June 30, 2006, to the Indenture dated April 8, 2004, as amended, among WMG Acquisition Corp., the additional subsidiary guarantors party thereto and Wells Fargo Bank, National Association, as Trustee. (2)
31.1	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended*
31.2	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-15(a) of the Securities Exchange Act, as amended*
32.1	Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**
32.2	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**

* Filed herewith.

** Pursuant to SEC Release No. 33-8212, this certification will be treated as "accompanying" this Quarterly Report on Form 10-Q and not "filed" as part of such report for purposes of Section 18 of the Securities Exchange Act, as amended, or otherwise subject the liability of Section 18 of the Securities Exchange Act, as amended, and this certification will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act, as amended, except to the extent that the registrant specifically incorporates it by reference.

(1) Incorporated by reference to Warner Music Group Corp.'s Form 10-Q for the period ended March 31, 2005.

(2) Incorporated by reference to Warner Music Group Corp.'s Current Report on Form 8-K filed on June 30, 2006.

Source: Warner Music Group C, 10-Q, August 03, 2006

SIGNATURES

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

August 3, 2006

WARNER MUSIC GROUP CORP.

By: /s/ EDGAR BRONFMAN, JR.

Name: Edgar Bronfman, Jr.
Title: Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)

By: /s/ MICHAEL D. FLEISHER

Name: Michael D. Fleisher
Title: Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)

Source: Warner Music Group C, 10-Q, August 03, 2006

Exhibit 31.1

CHIEF EXECUTIVE OFFICER CERTIFICATION

I, Edgar Bronfman, Jr., Chief Executive Officer and Chairman of the Board of Directors of Warner Music Group Corp., certify that:

1. I have reviewed this quarterly report on Form 10–Q of Warner Music Group Corp. (the "Registrant");

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this quarterly report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a–15(e) and 15d–15(e)) for the Registrant and we have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared; and

b) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Dated: August 3, 2006

/s/ EDGAR BRONFMAN, JR.

Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)

Source: Warner Music Group C, 10–Q, August 03, 2006

Exhibit 31.2

CHIEF FINANCIAL OFFICER CERTIFICATION

I, Michael D. Fleisher, Chief Financial Officer of Warner Music Group Corp., certify that:

1. I have reviewed this quarterly report on Form 10-Q of Warner Music Group Corp. (the "Registrant");

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this quarterly report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the Registrant and we have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared; and

b) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

c) Disclosed in this report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

Dated: August 3, 2006

/s/ MICHAEL D. FLEISHER

Chief Financial Officer (Principal Financial and Accounting Officer)

Source: Warner Music Group C, 10-Q, August 03, 2006

Exhibit 32.1

Certification of the Chief Executive Officer
Pursuant to 18 U.S.C. Section 1350,
As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report of Warner Music Group Corp. (the "Company") on Form 10-Q for the period ended June 30, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Edgar Bronfman, Jr., Chief Executive Officer of Warner Music Group Corp., certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 3, 2006

/S/ EDGAR BRONFMAN, JR.
Edgar Bronfman, Jr.
Chief Executive Officer

Source: Warner Music Group C, 10-Q, August 03, 2006

Exhibit 32.2

Certification of the Chief Financial Officer
Pursuant to 18 U.S.C. Section 1350,
As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Quarterly Report of Warner Music Group Corp. (the "Company") on Form 10-Q for the period ended June 30, 2006 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Michael D. Fleisher, Chief Financial Officer of Warner Music Group Corp., certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 3, 2006

/S/ MICHAEL D. FLEISHER
Michael D. Fleisher
Chief Financial Officer

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EXHIBIT CO 0946

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Sunday, November 26, 2006, 4:53PM ET - U.S. Markets closed. Dow ↓ 0.38% Nasdaq ↓ 0.23%

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Warner Music Group Inc. (WMG)

On Nov 24: 26.87 ↑ 0.12 (0.

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Warner Music Group Inc.
75 Rockefeller Plaza
New York, NY 10019
United States - Map
Phone: 212-275-2000
Fax: 212-757-3985
Web Site: http://www.wmg.com

DETAILS

Index Membership:	N/A
Sector:	Services
Industry:	General Entertainment
Full Time Employees:	4,000

BUSINESS SUMMARY

Warner Music Group, Inc., through its subsidiaries, offers recorded music and music publishing services worldwide. Its recorded music operations consist of the discovery and development of artists and related marketing and distribution of recorded music produced by such artists. The company also markets its music catalog through compilations and reissuances of previously released music and video titles, as well as licenses tracks to/from third parties for various uses, including film and television soundtracks. It markets, sells, and licenses recorded music in various physical formats, such as compact discs, cassettes, LPs, and digital versatile discs; and digital formats, including downloads and ringtones. The company's music publishing business involves the ownership and acquisition rights to approximately one million musical compositions, including various pop hits, American standards, folk songs and motion picture, and theatrical compositions. The company markets and distributes music

ADVERTISEMENT

CORPORATE GOVERNANCE

Warner Music Group Inc.'s Corporate Governance Quotient (CGQ®) as of 1-Nov-06 is better than 18.8% of Russell 3000 companies and 38.2% of Media companies.

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KEY EXECUTIVES

	Pay	Exercised
Mr. Edgar M. Bronfman Jr., 51 Chairman, Chief Exec. Officer and Member of Exec., Governance & Nominating Committee	$ 7.25M	$ 0
Mr. Lyor Cohen , 46 Chairman of U S Recorded Music, Chief Exec. Officer of U S Recorded Music of U S Recorded Music	$ 6.00M	$ 0

products to retailers and wholesale distributors. Warner Music Group was founded in 1929 and is headquartered in New York City.

Key Statistics

COMPANY WEBSITES

- Home Page

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HOTJOBS JOB POSTINGS

- Royalty Analyst
- WCM Administrative Assistant
- WEA - Administrative AssistantCatalog Sales & Market Development

More job openings...
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Mr. Michael D. Fleisher, 41 Chief Financial Officer, Principal Accounting Officer and Exec. VP	$ 2.05M	$ 0
Mr. Richard Blackstono, 46 Chairman of Warner/Chappell Music Inc. and Chief Exec. Officer of Warner/Chappell Music Inc	N/A	N/A
Mr. Craig Kallman, Chairman and Chief Exec. Officer of Atlantic Records Group	N/A	N/A

Dollar amounts are as of 31-Dec-05 and compensation values are for the last fiscal year ending on that date. "Pay" is salary, bonuses, etc. "Exercised" is the value of options exercised during the fiscal year.

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EXHIBIT CO 0947

Warner Music Group

News

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Warner Music Group Corp. Reports Fiscal Third Quarter Results for the Period Ended June 30, 2006

08/03/06

Revenue increases 11% to $822 million with double-digit domestic and international gains; Digital revenue grows 109% to $92 million or 11% of total revenue

- Total revenue of $822 million for the third quarter 2006 increased 11% from the prior-year quarter.
- Digital revenue was $92 million or 11% of total revenue in the quarter, up 109% from $44 million in the same quarter last year.
- Operating income rose to $28 million in the third quarter compared to a loss of $92 million in the prior-year quarter. Adjusted to exclude non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below), operating income rose 155% from $11 million.
- Operating income before depreciation and amortization (OIBDA) improved to $86 million from a loss of $33 million in the prior-year quarter. Adjusted to exclude non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below), OIBDA grew 23% from $70 million.
- Net loss of $0.10 per diluted share in the quarter improved from a net loss of $1.41 per diluted share in the same quarter last year. Adjusted to exclude non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below), the company's net loss per diluted share for the third quarter of fiscal 2005 was $0.34.

Warner Music Group Corp. (NYSE: WMG) today announced its financial results for the three-month period ended June 30, 2006.

"Continued execution on our strategy delivered balanced double-digit revenue growth both domestically and internationally, produced significant margin and market share gains and sustained our leadership position in digital," said Edgar Bronfman, Jr., Warner Music Group's Chairman and CEO. "We've amassed strong fundamental business momentum, outperforming the industry. Our artists' and labels' remarkable performance continues, including the success of our independent label initiatives. Additionally, we've continued to innovate in digital, with pioneering mobile partnerships in China and South Korea and novel product offerings such as SMS tones in Germany. While we're pleased with the results to date, our goal remains continuous growth in shareholder value through the transformation of Warner Music into the premier music-based content company."

Michael Fleisher, Warner Music Group's Executive Vice President and CFO, added: "We continue to believe that our twelve-month performance is the best indication of the progress we are making in our mission to be a music-based content company. Looking at the last twelve months, Warner Music Group's worldwide revenue was up 5% year over year, outpacing the industry."

Third Quarter Results

For the third quarter of fiscal 2006, revenue increased by 11% to $822 million from $742 million in the same quarter of fiscal 2005. Domestic revenue rose 11%, while international revenue grew 11% on both an as-reported

and currency-adjusted basis. Revenue growth in Recorded Music was partially offset by modest declines in Music Publishing.

Digital revenue more than doubled from the prior-year quarter to $92 million. Similar to last quarter, Warner Music Group had a larger digital presence in the U.S. than outside the U.S., with approximately 74% of the company's digital revenue coming from the U.S. and the remaining 26% coming from outside the U.S.

Operating income rose to $28 million in the third quarter, a margin of 3.4%, compared to a loss of $92 million in the prior-year quarter. Adjusted to exclude non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below), operating income for the quarter rose to $28 million from $11 million in the prior-year quarter and operating margin expanded by 1.9 percentage points.

OIBDA in the quarter improved to $86 million from a loss of $33 million in the prior-year quarter. Adjusted to exclude non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below), OIBDA for the quarter grew to $86 million from $70 million in the prior-year quarter and OIBDA margin improved by 1.1 percentage points to 10.5%. The company's OIBDA margin expansion reflects successful cost management in the quarter and the benefit of a shift to higher-margin digital revenue.

Net loss was $14 million or $0.10 per diluted share for the quarter. Net loss in our third quarter of fiscal 2005 was $1.41 per diluted share. Adjusted to exclude non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below), the prior-year quarter had a net loss of $44 million or $0.34 per diluted share.

As of June 30, 2006, the company had a cash balance of $306 million, short-term investments of $29 million, total long-term debt of $2.25 billion and net debt (total long-term debt minus cash and short-term investments) of approximately $1.92 billion.

For the quarter, net cash provided by operating activities was $18 million. Free cash flow (calculated by taking cash flow from operations less capital expenditures and cash paid for investments) amounted to ($33) million, including $63 million in net cash outflow related to the acquisition of Ryko Corporation (which represents the $67.5 million purchase price, net of cash purchased as part of the business). Prior-year free cash flow amounted to ($113) million in the comparable 2005 fiscal quarter and included the payment of certain non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below) and $50 million in cash received from the sale of certain assets.

Unlevered after-tax cash flow, defined as free cash flow excluding cash interest paid and non-recurring management fees (see Non-Recurring Items below) was $14 million, which included $63 million in net cash outflow related to the acquisition of Ryko Corporation (see below for calculation of Non-GAAP free cash flow and unlevered after-tax cash flow).

Below is the business segment discussion for the quarter.

Recorded Music

Revenue for the company's Recorded Music business increased 15% to $678 million, and 16% on a constant-currency basis. Both domestic and international markets contributed to this growth. Recorded Music digital revenue of $88 million surged 132% over the prior-year quarter and represented 13% of total Recorded Music revenue. Digital growth is reflective of the company's continued digital innovation along with the success of new releases.

Recorded Music revenue increases reflect the success of both established and developing artists, as well as

significant carryover sales. Major sellers in the quarter included titles from Red Hot Chili Peppers, James Blunt, T.I., Gnarls Barkley and Tim McGraw. Domestic Recorded Music revenue rose 19% in the quarter to $347 million from the prior-year quarter, while international Recorded Music revenue increased 12% from the prior-year quarter to $331 million. This international revenue growth was primarily driven by strong gains in Europe led by the United Kingdom and double-digit gains in the Asia/Pacific region.

Recorded Music operating income totaled $52 million in the quarter, a margin of 7.7%, up from $6 million in the prior-year quarter. Adjusted to exclude non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below), Recorded Music operating income doubled from $26 million and Recorded Music operating margin improved 3.3 percentage points from the comparable prior-year period.

Recorded Music OIBDA grew to $92 million for the quarter, compared to $47 million in the prior-year quarter. Adjusted to exclude non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items below), Recorded Music OIBDA grew 37% from $67 million driven by increased revenue, higher-margin digital sales and successful management of costs and Recorded Music OIBDA margins expanded by 2.2 percentage points to 13.6%.

Music Publishing

Music Publishing revenue decreased by 7% to $150 million compared to the same quarter in the prior year, but was down 2% from the prior-year quarter on a constant-currency basis and excluding $8 million of prior-year revenue from the company's sheet music business sold in May 2005. Digital revenue from Music Publishing amounted to $4 million, which represents 3% of total Music Publishing revenue for the quarter.

Declines in synchronization revenue of 36% and mechanical revenue of 6% were partially offset by a 16% increase in performance revenue. Mechanical revenue declines reflect a prior-year industry reduction in physical record sales. Synchronization revenue fell as a result of variability in market demand as well as the timing of cash payments received. The increase in performance revenue reflects a change in the timing of payments received from a domestic performing rights organization.

Music Publishing operating income was $9 million in the quarter, a margin of 6.0%, down 31% from $13 million in the prior-year quarter. Music Publishing OIBDA was $23 million in the quarter, down 18% from $28 million in the prior-year quarter. Operating income and OIBDA were down due to lower revenue and a pick-up in investments to drive long-term growth. Turning the Music Publishing business around remains a top management priority.

Non-Recurring Items

The company's operating results for the third quarter of fiscal 2005 contained non-recurring, IPO-related items including a $73 million fee to terminate a management contract, $1 million of management fees paid to the company's Investor Group, certain cash payments to employees totaling $19 million related to the issuance of stock awards below fair market value and payment of a $10 million bonus to employees, as previously disclosed. Net income and earnings per share also included a charge of $35 million resulting from the redemption of debt issued by the company's subsidiary, WMG Holdings Corp. These non-recurring items had related tax expense of $3 million.

Recorded Music operating results for the third quarter of fiscal 2005 contained non-recurring charges of $8 million for IPO-related cash bonuses and $12 million for bonuses related to stock awards. Music Publishing operating results for the third quarter of fiscal 2005 contained a non-recurring charge of $1 million for IPO-related cash bonuses.

FAS 123 Expenses
FAS 123 expenses, which represent stock compensation expenses, amounted to $4 million for the quarter ended June 30, 2006 and $9 million for the quarter ended June 30, 2005. Recorded Music FAS 123 expenses amounted to $3 million and $6 million for the quarters ended June 30, 2006 and 2005, respectively. Music Publishing FAS 123 expenses amounted to about $1 million for the quarter ended June 30, 2006 and $1 million for the quarter ended June 30, 2005.

Financial details for the company's third fiscal quarter 2006 can be found in the Form 10-Q filed today with the Securities and Exchange Commission.

This morning, management will be hosting a conference call to discuss the results at 10:00 A.M. EDT. The call will be webcast on www.wmg.com [http://www.wmg.com/].

About Warner Music Group
Warner Music Group became the only stand-alone music company to be publicly traded in the United States in May 2005. With its broad roster of new stars and legendary artists, Warner Music Group is home to a collection of the best-known record labels in the music industry including Asylum, Atlantic, Bad Boy, Cordless, East West, Elektra, Lava, Maverick, Nonesuch, Perfect Game, Reprise, Rhino, Rykodisc, Sire, Warner Bros. and Word. Warner Music International, a leading company in national and international repertoire, operates through numerous international affiliates and licensees in more than 50 countries. Warner Music Group also includes Warner/Chappell Music, one of the world's leading music publishers.

"Safe Harbor" Statement under Private Securities Litigation Reform Act of 1995:
This communication includes forward-looking statements that reflect the current views of Warner Music Group about future events and financial performance. Words such as "estimates," "expects," "anticipates," "projects," "plans," "intends," "believes," "forecasts" and variations of such words or similar expressions that predict or indicate future events or trends, or that do not relate to historical matters, identify forward-looking statements. All forward-looking statements are made as of today, and we disclaim any duty to update such statements. Our expectations, beliefs and projections are expressed in good faith and we believe there is a reasonable basis for them. However, there can be no assurance that management's expectations, beliefs and projections will result or be achieved. Investors should not rely on forward-looking statements because they are subject to a variety of risks, uncertainties, and other factors that could cause actual results to differ materially from our expectations. Please refer to our Form 10-K and Form 10-Q concerning factors that could cause actual results to differ materially from those described in our forward-looking statements.

Figure 1. Warner Music Group Corp. - Consolidated Statement of Operations, Three and Nine Months Ended 6/30/06 versus 6/30/05 (dollars in millions, except per share amounts)

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)	% Change	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)	% Change
Revenues:	$822	$742	11%	$2,662	$2,597	3%
Costs and expenses:						
Cost of revenues	(446)	(398)	(12%)	(1,384)	(1,377)	(1%)
Selling, general and administrative expenses	(301)	(318)	5%	(918)	(942)	3%
Amortization of intangible assets	(43)	(47)	(2%)	(143)	(140)	(2%)
Loss on termination of management agreement	-	(73)	100%	-	(73)	100%
Total costs and expenses	($794)	($834)	5%	($2,445)	($2,532)	3%
Operating income (loss)	$28	($92)	130%	$217	$65	234%
Interest expense, net	(45)	(50)	10%	(135)	(140)	4%
Net investment-related gains	-	1	-	-	1	-
Equity in gains (losses) of equity method investees	-	-	-	1	(1)	200%
Unrealized gain on warrants	-	-	-	-	17	-
Loss on repayment of Holdings Notes	-	(35)	-	-	(35)	-
Minority interest expense	-	-	-	-	(5)	-
Other income, net	1	1	-	3	6	(50%)
Net (loss) income before income taxes	($16)	($175)	91%	$86	($93)	192%
Income tax benefit (expense)	2	(4)	150%	(38)	(46)	17%
Net (loss) income	($14)	($179)	92%	$48	($139)	135%
Net income (loss) per share:						
Basic	($0.10)	($1.41)	93%	$0.34	($1.22)	128%
Diluted (a)	($0.10)	($1.41)	93%	$0.32	($1.22)	126%
Weighted average shares outstanding:						
Basic	143.7	127.0	13%	142.3	114.1	25%
Diluted (b)	143.7	127.0	13%	150.8	114.1	32%

(a) Diluted net loss per share for the nine months ended June 30, 2005 reflects an add-back of net income for the unrealized gain on warrants as a result of the assumed exercise of the warrants in the calculation.

(b) Diluted shares for the three months ended June 30, 2006, the three months ended June 30, 2005 and the nine months ended June 30, 2005 would include an add-back of 7.5, 9.8, 10.0 million shares, respectively, related to the assumed vesting of restricted stock and assumed exercise of stock options if they were anti-dilutive.

Figure 2. Warner Music Group Corp. -Consolidated Balance Sheets as of 6/30/06 and 9/30/05 (dollars in millions)

	June 30, 2006 (unaudited)	Sept 30, 2005 (audited)	% Change
Assets:			
Current Assets			
Cash & cash equivalents	$306	$288	6%
Short-term investments	29	-	100%
Accounts receivable, less allowances of $205 and $218	524	637	(18%)
Inventories	50	52	(4%)
Royalty advances (to be recouped w/in 1 year)	209	190	10%
Deferred tax assets	40	36	11%
Other current assets	47	39	21%
Total Current Assets	$1,205	$1,242	(3.0%)
Royalty advances (to be recouped after 1 year)	209	190	10%
Investments	24	21	14%
Property, plant & equipment, net	144	157	(8%)
Goodwill	946	869	9%
Intangible assets subject to amortization, net	1,746	1,815	(4%)
Intangible assets not subject to amortization	100	100	-
Other assets	109	104	5%
Total Assets	$4,483	$4,498	(0%)
Liabilities & Shareholders' Equity:			
Current Liabilities			
Accounts payable	$202	$247	(18%)
Accrued royalties	1,146	1,057	8%
Taxes & other withholdings	34	23	48%
Current portion of long-term debt	17	17	-
Dividend payable	22	-	100%
Other current liabilities	336	404	(17%)
Total current liabilities	$1,757	$1,748	1%
Long-term debt	$2,234	$2,229	-
Dividends payable	3	5	(40%)
Deferred tax liabilities, net	193	201	(4%)
Other noncurrent liabilities	216	226	(4%)
Total Liabilities	$4,403	$4,409	(0%)
Common stock	-	-	-
Additional paid-in capital	560	548	2%
Accumulated deficit	(509)	(480)	(6%)
Accumulated other comprehensive income	29	21	38%
Total Shareholders' Equity	$80	$89	(10%)
Total Liabilities & Shareholders' Equity	$4,483	$4,498	(0%)

Figure 3. Warner Music Group Corp.-- Summarized Statement of Cash Flows, Three Months and Nine Months Ended 6/30/06 versus 6/30/05 (dollars in millions)

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)	% Change	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)	% Change
Net cash provided by (used in) operating activities	$18	($120)		$223	$172	
Net cash (used in) provided by investing activities	(51)	7		(142)	(54)	
Net cash used in financing activities	(23)	(65)		(68)	(407)	
Effect of foreign currency exchange rates on cash	3	(4)		5	(1)	
Net increase (decrease) in cash	($53)	($182)	71%	$18	($290)	106%

Supplemental Disclosures Regarding Non-GAAP Financial Information

OIBDA

We evaluate our operating performance based on several factors, including our primary financial measure of operating income (loss) before non-cash depreciation of tangible assets and non-cash amortization of intangible assets (which we refer to as OIBDA). We consider OIBDA to be an important indicator of the operational strengths and performance of our businesses, and believe the presentation of OIBDA helps improve the ability to understand the company's operating performance and evaluate our performance in comparison to comparable periods. However, a limitation of the use of OIBDA as a performance measure is that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenue in our businesses. Accordingly, OIBDA should be considered in addition to, not as a substitute for, operating income (loss), net income (loss) and other measures of financial performance reported in accordance with accounting principles generally accepted in the U.S.

Figure 4. Warner Music Group Corp. -- Reconciliation of OIBDA to Net Income, Three and Nine Months Ended 6/30/06 versus 6/30/05 (dollars in millions)

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)	% Change	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)	% Change
OIBDA	$86	($33)	361%	$392	$245	60%
Depreciation expense	(10)	(12)	17%	(32)	(40)	20%
Amortization expense	(48)	(47)	(2%)	(143)	(140)	(2%)
Operating income (loss)	$28	($92)	130%	$217	$65	234%
Interest expense, net	(45)	(50)	10%	(135)	(140)	4%
Net investment-related gains	-	1	-	-	1	-
Equity in gains (losses) of equity-method investees	-	-	-	1	(1)	200%
Unrealized gain on warrants	-	-	-	-	17	-
Loss on repayment of Holdings Notes	-	(35)	-	-	(35)	-
Minority interest expense	-	-	-	-	(5)	-
Other income, net	1	1	-	3	6	(40%)
Income (loss) before income taxes	($16)	($175)	91%	$86	($93)	192%
Income tax benefit (expense)	2	(4)	150%	(38)	(40)	17%
Net (loss) income	($14)	($179)	92%	$48	($133)	136%
OIBDA Margin	10.5%	(4.4%)		14.7%	9.4%	
Operating Income Margin	3.4%	(12.4%)		8.2%	2.5%	

Adjusted Results

As previously disclosed, the prior year contained a number of non-recurring charges that occurred concurrently with or in connection with our initial public offering. Such charges relate to specific IPO-related one-time events and do not reflect ongoing operations of the business. Therefore, the company is also presenting results excluding these items. We consider these adjusted results to be an important

indicator of the operational strengths and performance of our businesses, including the ability to provide free cash flow to service debt. However, a limitation of the use of these adjusted amounts as performance measures is that they do not reflect the charges noted and, therefore, do not necessarily represent funds available for discretionary use, and are not necessarily measures of the company's ability to fund its cash needs. Accordingly, these adjusted amounts should be considered in addition to, not as a substitute for, operating income (loss), net income (loss), EPS and other measures of financial performance reported in accordance with accounting principles generally accepted in the U.S.

Figure 5. Warner Music Group Corp.-- Reconciliation of GAAP Operating Income to Non-GAAP Adjusted OIBDA, for the Three and Nine Months ended 6/30/06 versus 6/30/05 (dollars in millions)

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)	% Change	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)	% Change
Total WMG Operating Income (Loss) - GAAP	$28	($92)	130%	$217	$65	234%
Depreciation and Amortization	69	59	(2%)	175	180	(3%)
Total WMG OIBDA	$96	(33)	361%	$392	$245	60%
IPO-related cash bonus	-	10	-	-	10	-
Bonus related to stock awards	-	19	-	-	19	-
Loss on termination of management agreement	-	73	-	-	73	-
Management fees	-	1	-	-	6	-
Total WMG OIBDA Excluding Non-Recurring Charges	$96	$70	23%	$392	$353	11%
Recorded Music Operating Income (Loss) - GAAP	$52	$6	767%	$258	$188	37%
Depreciation and Amortization	40	41	(2%)	121	125	(3%)
Recorded Music OIBDA	$92	$47	96%	$379	$313	21%
IPO-related cash bonus	-	8	-	-	8	-
Bonus related to stock awards	-	12	-	-	12	-
Recorded Music OIBDA Excluding Non-Recurring Charges	$92	$67	37%	$379	$333	14%
Music Publishing Operating Income (Loss) - GAAP	$9	$13	(31%)	$47	$55	(15%)
Depreciation and Amortization	14	15	(7%)	44	44	-
Music Publishing OIBDA	$23	$28	(18%)	$91	$99	(9%)
IPO-related cash bonus	-	1	-	-	1	-
Music Publishing OIBDA Excluding Non-Recurring Charges	$23	$29	(21%)	$91	$100	(9%)

Figure 6. Warner Music Group Corp.—Reconciliation of GAAP Operating Income to Non-GAAP Operating Income for the Three and Nine Months ended 6/30/06 versus 6/30/05 (dollars in millions)

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)	% Change	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)	% Change
Total WMG Operating Income (Loss) - GAAP	$28	($92)	130%	$217	$65	234%
IPO-related cash bonus	-	10	-	-	10	-
Bonus related to stock awards	-	19	-	-	19	-
Loss on termination of management agreement	-	73	-	-	73	-
Management fees	-	1	-	-	6	-
Total WMG Operating Income Excluding Non-Recurring Charges	$28	$11	155%	$217	$173	25%
Recorded Music Operating Income - GAAP	$52	$6	767%	$258	$188	37%
IPO-related cash bonus	-	8	-	-	8	-
Bonus related to stock awards	-	12	-	-	12	-
Recorded Music Operating Income Excluding Non-Recurring Charges	$52	$26	100%	$258	$208	24%
Music Publishing Operating Income - GAAP	$9	$13	(31%)	$47	$55	(15%)
IPO-related cash bonus	-	1	-	-	1	-
Music Publishing Operating Income Excluding Non-Recurring Charges	$9	$14	(36%)	$47	$56	(16%)

Figure 7. Warner Music Group Corp. -- Reconciliation of GAAP to Non-GAAP Net Income (Loss) and Earnings Per Share for the Three and Nine Months ended 6/30/06 versus 6/30/05 (dollars in millions, except per share amounts)

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)
Net income (loss):				
Net (loss) income - GAAP	($14)	($179)	$48	($139)
Loss on termination of management fee	-	73	-	73
Loss on repayment of debt	-	35	-	35
IPO-related cash bonus	-	10	-	10
Bonus related to stock awards	-	19	-	19
Management fees	-	1	-	6
Tax effect on non-recurring items	-	(3)	-	(3)
Net (loss) income - Excluding Non-Recurring Charges	($14)	($44)	$48	$1
Earnings Per Share:				
EPS - GAAP	($0.10)	($1.41)	$0.32	($1.22)
Loss on termination of management fee	-	0.58	-	0.64
Loss on repayment of debt	-	0.28	-	0.31
IPO-related cash bonus	-	0.08	-	0.09
Bonus related to stock awards	-	0.15	-	0.17
Management fees	-	0.01	-	0.05
Tax effect on non-recurring items	-	(0.02)	-	(0.03)
Diluted EPS - Excluding Non-Recurring Charges	($0.10)	$0.34	$0.32	$0.01

Constant Currency

As exchange rates are an important factor in understanding period to period comparisons, we believe the presentation of results on a constant-currency basis in addition to reported results helps improve the ability to understand the company's operating results and evaluate our performance in comparison to prior periods. Constant-currency information compares results between periods as if exchange rates had remained constant period-over-period. We use results on a constant-currency basis as one measure to evaluate our performance. However, a limitation of the use of the constant-currency results as a performance measure is that it does not reflect the $4 million unfavorable impact of exchange rates on both our Total and Recorded Music revenue in the three months ended June 30, 2006 compared to the comparable prior-year quarter and the $62 million, $48 million and $14 million unfavorable impact of exchange rates on our Total, Recorded Music and Music Publishing revenue, respectively, in the nine months ended June 30, 2006 compared to the comparable period in the prior year (see Figure 9). Further, it does not reflect the $1 million impact of unfavorable exchange rates on both Total and Recorded Music operating income (see Figure 8 and 5 to calculate the impact). In addition, it does not reflect the $4 million unfavorable impact of exchange rates on our total international revenue for the three months ended June 30, 2005 (see Figure 9) or the $55 million unfavorable impact of exchange rates on our revenue for the last twelve months (see Figure 11). These results should be considered in addition to, not as a substitute for, results reported in accordance with accounting principles generally accepted in the U.S. Results on a constant-currency basis, as we present them, may not be comparable to similarly titled measures used by other companies and is not a measure of performance presented in accordance with accounting principles generally accepted in the U.S.

Figure 8. Warner Music Group Corp.– Reconciliation of GAAP Operating Income to Non-GAAP Adjusted OIBDA, Constant Currency for the Three and Nine Months ended 6/30/06 versus 6/30/05 (dollars in millions)

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)	% Change	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)	% Change
Total WMG Operating Income (Loss) - GAAP	$28	($93)	130%	$217	$59	274%
Depreciation and Amortization	58	59	(2%)	175	180	(3%)
Total WMG OIBDA	86	(34)	353%	392	239	65%
IPO-related cash bonus	-	10	-	-	10	-
Bonus related to stock awards	-	19	-	-	19	-
Loss on termination of management agreement	-	73	-	-	73	-
Management fees	-	1	-	-	6	-
Total WMG OIBDA Excluding Non-Recurring Charges	$86	$69	25%	$392	$346	13%
Recorded Music Operating Income (Loss) - GAAP	$52	$5	940%	$258	$185	39%
Depreciation and Amortization	40	41	(2%)	121	125	(3%)
Recorded Music OIBDA	92	46	100%	379	310	22%
IPO-related cash bonus	-	8	-	-	8	-
Bonus related to stock awards	-	12	-	-	12	-
Recorded Music OIBDA Excluding Non-Recurring Charges	$92	$66	39%	$379	$330	15%
Music Publishing Operating Income (Loss) - GAAP	$9	$13	(31%)	$47	$54	(13%)
Depreciation and Amortization	14	15	(7%)	44	44	-
Music Publishing OIBDA	23	28	(18%)	91	98	(7%)
IPO-related cash bonus	-	1	-	-	1	-
Music Publishing OIBDA Excluding Non-Recurring Charges	$23	$29	(21%)	$91	$99	(8%)

Figure 9. Warner Music Group Corp.-- Revenue by Geography, Three and Nine Months Ended 6/30/06 versus 6/30/05 As Reported and Constant Currency (dollars in millions)

	Three Months Ended June 30, 2006 As reported (unaudited)	Three Months Ended June 30, 2005 As reported (unaudited)	Three Months Ended June 30, 2005 Constant $ (unaudited)	Nine Months Ended June 30, 2006 As reported (unaudited)	Nine Months Ended June 30, 2005 As reported (unaudited)	Nine Months Ended June 30, 2005 Constant $ (unaudited)
Revenue by Geography:						
US revenue	$406	$367	$367	$1,282	$1,217	$1,217
Recorded Music	347	292	292	1,115	1,001	1,001
Music Publishing (a)	59	75	75	167	216	216
International revenue	$422	$382	$378	$1,402	$1,402	$1,340
Recorded Music	331	296	292	1,159	1,148	1,100
Music Publishing (a)	91	86	86	243	254	240
Intersegment eliminations	($6)	($7)	($7)	($22)	($22)	($22)
	$822	$742	$738	$2,662	$2,597	$2,535
Revenue by Segment:						
Recorded Music	$678	$588	$584	$2,274	$2,149	$2,101
Music Publishing	150	161	161	410	470	456
Intersegment eliminations	(6)	(7)	(7)	(22)	(22)	(22)
Total Revenue	$822	$742	$738	$2,662	$2,597	$2,535

(a) The sheetmusic business, which was sold in May 2005, contributed to Music Publishing revenues for the three and nine months ended June 30, 2005, as follows:

	3 Months Ended			9 Months Ended		
	Including sheet music business	Sheetmusic business	Excluding sheet music business	Including sheet music business	Sheetmusic business	Excluding sheet music business
Revenue	$161	$8	$153	$470	$34	$436

Free Cash Flow

Free cash flow reflects our cash flow provided by operating activities less capital expenditures and cash paid or received for investments. We use free cash flow, among other measures, to evaluate our operating performance. Management believes free cash flow provides investors with an important

perspective on the cash available to service debt, make strategic acquisitions and investments, fund ongoing operations and working capital needs and pay ongoing regular quarterly dividends. As a result, free cash flow is a significant measure of our ability to generate long-term value. It is useful for investors to know whether this ability is being enhanced or degraded as a result of our operating performance. We believe the presentation of free cash flow is relevant and useful for investors because it allows investors to view performance in a manner similar to the method used by management. In addition, free cash flow is also a primary measure used externally by our investors and analysts for purposes of valuation and comparing the operating performance of our company to other companies in our industry.

As free cash flow is not a measure of performance calculated in accordance with GAAP, free cash flow should not be considered in isolation of, or as a substitute for, net income (loss) as an indicator of operating performance or cash flow provided by operating activities as a measure of liquidity. Free cash flow, as we calculate it, may not be comparable to similarly titled measures employed by other companies. In addition, free cash flow does not necessarily represent funds available for discretionary use and is not necessarily a measure of our ability to fund our cash needs. As free cash flow deducts capital expenditures and cash paid or received for investments from "cash flow provided by operating activities" (the most directly comparable GAAP financial measure), users of this information should consider the types of events and transactions that are not reflected. We provide below a reconciliation of free cash flow to the most directly comparable amount reported under GAAP - - "cash flow provided by operating activities."

Free cash flow includes cash paid for interest and certain non-recurring payments. We also review our cash flow adjusted for these items, a measure we call unlevered after-tax cash flow. Management believes this measure provides investors with an additional important perspective on our cash generation ability. We consider unlevered after-tax cash flow excluding certain non-recurring items to be an important indicator of the performance of our businesses and believe the presentation is relevant and useful for investors because it allows investors to view performance in a manner similar to the method used by management. A limitation of the use of this measure is that it does not reflect the charges noted and, therefore, does not necessarily represent funds available for discretionary use, and is not necessarily a measure of the company's ability to fund its cash needs. Accordingly, this measure should be considered in addition to, not as a substitute for, net cash flow provided by operating activities and other measures of liquidity reported in accordance with accounting principles generally accepted in the U.S.

Figure 10. Warner Music Group Corp. – Calculation of Free Cash Flow. Three Months and Nine Months Ended 6/30/06 versus 6/30/05 (dollars in millions)

	Three Months Ended June 30, 2006 (unaudited)	Three Months Ended June 30, 2005 (unaudited)	Nine Months Ended June 30, 2006 (unaudited)	Nine Months Ended June 30, 2005 (unaudited)
Net cash flow provided by operating activities	$18	($120)	$223	$172
Less: Capital expenditures	6	6	18	20
Less: Cash paid (received) for investments	45	(13)	124	34
Free cash flow (a)	($33)	($113)	$81	$118

(a) - Free cash flow includes cash paid for interest and certain non-recurring cash payments as follows (in millions):

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Nine Months Ended June 30, 2006	Nine Months Ended June 30, 2005
Free cash flow	($33)	($113)	$81	$118
Plus: Cash paid for interest	47	63	118	129
Plus: Cash paid for management fees	-	1	-	6
Unlevered after-tax cash flow	$14	($49)	$199	$253

Unlevered after-tax cash flow for the three and nine months ended June 30, 2005 included the payment of certain non-recurring items related to the company's IPO in 2005 (see Non-Recurring Items above) including $73 million paid to terminate the management agreement, $10 million paid for IPO-related cash bonuses and $10 million paid for bonuses related to stock awards. Adjusted to exclude non-recurring items related to the company's IPO in 2005, unlevered after-tax cash flow was $53 million and $355 million for the three and nine months ended June 30, 2005.

Twelve-Month Results

We believe that, especially given the rhythm of the music release schedule and associated marketing and promotional expenses, quarterly variations of results are normal in our businesses. As a result, in addition to viewing our performance for current periods, we evaluate our operating performance on a full-year basis. We manage our business based on twelve-month results and consider twelve-month performance to be an important indicator of the performance of our businesses and believe the presentation of twelve-month results help improve the ability to understand the company's operating performance and evaluate our performance in comparison to prior periods. These twelve-month results should be considered in addition to, not as a substitute for, revenue and other measures of financial performance reported in accordance with accounting principles generally accepted in the U.S. In addition, the twelve-month periods presented below are not accounting periods under SEC rules or accounting principles generally accepted in the U.S. Our twelve months ended June 30, 2006 unaudited revenue was derived from our unaudited financial statements for each of the three-month periods ended June 30, 2006, March 31, 2006, December 31, 2005 and September 30, 2005. Our twelve months ended June 30, 2005 unaudited revenue was derived from our unaudited financial statements for each of the three-month periods ended June 30, 2005, March 31, 2005, December 31, 2004 and September 30, 2004.

Figure 11. Warner Music Group Corp. --Last Twelve Months ("LTM") Revenues (dollars in millions)

	LTM 6/30/06[a] (unaudited)	LTM 6/30/05 (unaudited)	% Change
Q4 2005 / Q4 2004	$905	$798	13%
Q1 2005 / Q1 2004	1,044	1,088	(4%)
Q2 2006 / Q2 2005	796	767	4%
Q3 2006/ Q3 2005	822	742	11%
Last Twelve Months Revenues	$3,567	$3,395	5%
Impact of foreign currency exchange rates	-	(55)	-
Last Twelve Months Revenue - Constant Currency	$3,567	$3,340	7%

(a) - Full fiscal year revenue for the fiscal year ended September 30, 2005 was $3,502.

Source: Warner Music Group

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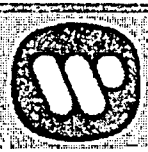
Please note that while you are reviewing any information on this website, the information is posted as of the dates listed. The Company has no obligation to update the information in the e-mail alerts or otherwise from this website, which speak as of their respective dates.

EXHIBIT CO 0948



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Warner Music Group Corp. Reports Fiscal Second Quarter Results for the Period Ended March 31, 2006

Revenue Increases 4% to $796 Million; Digital Revenue Grows 157% to $90 Million or 11% of Total Revenue

NEW YORK, NY, May 05, 2006 – Warner Music Group Corp. (NYSE: WMG)

- Total revenue of $796 million for the second quarter 2006 increased 4% from the prior-year quarter and was up 10%, excluding the impact of exchange rates and the sheet music business sold in May 2005.
- Digital revenue was $90 million, climbing to 11% of total revenue in the quarter, up 30% sequentially from the first quarter 2006 and up 157% from $35 million in the same quarter last year.
- Operating income rose 67% over the second quarter last year to $45 million in the quarter, driving a 2.1 percentage point improvement in operating income margin to 5.7%.
- Operating income before depreciation and amortization (OIBDA) in the quarter rose 18% over the second quarter last year to $104 million, leading to a 1.6 percentage point expansion in OIBDA margin to 13.1%.
- Net loss of ($0.05) per diluted share in the quarter increased from a net loss of ($0.28) per diluted share in the same quarter last year.

Warner Music Group Corp. (NYSE: WMG) today announced its financial results for the three-month period ended March 31, 2006.

"One year since our IPO, Warner Music has grown revenue, outperforming the market and gaining

significant margin and market share," said Edgar Bronfman, Jr., Warner Music Group's Chairman and CEO. "Through its strategy for profitable growth, this team has led the industry in the digital space, enhanced its competitiveness in the independent arena and gained share in the highest-growth market segments. Our artists and labels have had a remarkable year – including both innovative efforts with established artists and development of new artists."

Michael Fleisher, Warner Music Group's Executive Vice President and CFO, added: "We continue to believe that our twelve-month performance is the best indication of the progress we are making in our mission to be a music-based content company. Over the latest twelve months, Warner Music Group's worldwide revenue was up 3% year-over-year, outpacing the industry."

Second Quarter Results

For the second quarter of fiscal 2006, revenue increased by 4% to $796 million from $767 million in the same quarter of fiscal 2005. Domestic revenue rose 15% while international revenue fell 6%, but rose 2% on a currency-adjusted basis. On a constant-currency basis and excluding the sheet music business(1), quarterly revenue rose 10% from the same quarter in the prior year.

Digital revenue nearly tripled from the prior-year quarter to $90 million. Similar to last quarter, Warner Music Group continues to have a larger digital presence in the U.S. than outside the U.S., with approximately 70% of the company's digital revenue originating from the U.S. and the remaining 30% coming from outside the U.S.

Operating income for the quarter rose by $18 million to $45 million, a 67% improvement when compared to the prior-year quarter.

OIBDA for the quarter rose by $16 million to $104 million from $88 million last year, driving margin improvement of 1.6 percentage points to 13.1%. This quarter's OIBDA includes $2 million in FAS 123 charges and a previously announced $8 million severance charge relating to an executive departure. The prior year quarter included $7 million in FAS 123 charges.

Reported net loss was ($7) million or ($0.05) per diluted share for the quarter, compared to net income of $4 million or ($0.28) per diluted share in the comparable prior-year period. Net income for the March 31, 2005 quarter included a $39 million unrealized gain to mark-to-market the warrants issued to Time Warner as part of the original purchase price of the acquisition. The warrants were repurchased in May 2005.

The company also reported a cash balance of $359 million, short-term investments of $61 million, total long-term debt of $2.2 billion and net debt (total long-term debt minus cash and short-term investments) of approximately $1.8 billion, as of March 31, 2006.

For the quarter, free cash flow (calculated by taking cash flow from operations less capital expenditures and cash paid for investments) amounted to $162 million, compared to $193 million in the comparable fiscal 2005 quarter. Unlevered after-tax cash flow (defined as free cash flow excluding cash interest paid and non-recurring management fees) was $186 million, compared to $220 million in the comparable fiscal 2005 quarter (see below for calculation of Non-GAAP Free Cash Flow and unlevered after-tax cash flow).

For the six months ended March 31, 2006, unlevered after-tax cash flow was $246 million, compared to $302 million in the prior-year comparable period. This gives Warner Music Group an 80% conversion rate for the first six months of the 2006 fiscal year (calculated by taking unlevered after-tax cash flow and dividing by OIBDA).

Below is the business segment discussion for the quarter.

Recorded Music

Revenue for the company's Recorded Music business increased 9% to $676 million, and 13% on a constant currency basis. Both domestic and international markets (on a constant-currency basis) contributed to this growth. Recorded Music digital revenue of $86 million represented 13% of total Recorded Music revenue and grew 177% from the prior-year quarter. Digital growth is reflective of the company's continued digital innovation along with the success of several key new releases.

Recorded Music revenue increases reflect the success of both established and developing artists, as well as significant carryover sales. Major sellers in the quarter included titles from James Blunt, T.I., Madonna, Sean Paul and Juvenile. Domestic Recorded Music revenue fueled the quarter, adding 22% to $361 million from the prior-year quarter, while international Recorded Music revenue increased 4%, excluding $21 million attributable to the negative impact of exchange rates. This international revenue growth in the quarter was primarily driven by Europe led by the United Kingdom and Italy and strong double-digit gains in the Asia/Pacific region.

Recorded Music operating income climbed 33% to $40 million in the quarter over the prior-year's quarter, yielding an operating margin of 5.9%, up 1.1 percentage points from the comparable prior-year

period.

Recorded Music OIBDA grew 13% to $81 million for the quarter, compared to $72 million in the prior-year comparable period as a result of increased revenue and a more profitable product mix, including higher-margin digital sales. This drove a 0.4 percentage point expansion in OIBDA margins to 12.0%, as compared to the same quarter last year.

Music Publishing

Music Publishing revenue decreased 16% compared to the same quarter in the prior year to $129 million in the quarter, but was down only 3% from the prior-year quarter on a constant currency basis and excluding $11 million of prior-year revenue from the sold sheet music business. Digital revenue from Music Publishing amounted to $4 million, which represents 3% of total Music Publishing revenue for the quarter.

Declines in both mechanical revenue of 12% and synchronization revenue of 9% were partially offset by an increase in performance revenue. Mechanical revenue declines reflect prior-year industry declines in physical record sales. Synchronization and performance revenue variances reflect timing issues rather than business growth or decline.

Music Publishing operating income was $32 million and OIBDA was $47 million in the quarter, both flat from the prior-year quarter.

FAS 123 Expenses

FAS 123 expenses, which represent stock compensation expenses, amounted to $2 million for the quarter ended March 31, 2006 and $7 million for the quarter ended March 31, 2005.

Financial details for the company's second fiscal quarter 2006 can be found in the Form 10-Q filed today with the Securities and Exchange Commission.

This morning, management will be hosting a conference call to discuss the results at 8:30 A.M. EST. The call will be webcast on www.wmg.com.

About Warner Music Group

Warner Music Group became the only stand-alone music company to be publicly traded in the United States in May 2005. With its broad roster of new stars and legendary artists, Warner Music Group is home to a collection of the best-known record labels in the music industry including Asylum, Atlantic, Bad Boy, Cordless, East West, Elektra, Lava, Maverick, Nonesuch, Perfect Game, Reprise, Rhino, Sire, Warner Bros. and Word. Warner Music International, a leading company in national and international repertoire, operates through numerous international affiliates and licensees in more than 50 countries. Warner Music Group also includes Warner/Chappell Music, one of the world's leading music publishers.

"Safe Harbor" Statement under Private Securities Litigation Reform Act of 1995:

This communication includes forward-looking statements that reflect the current views of Warner Music Group about future events and financial performance. Words such as "estimates," "expects," "anticipates," "projects," "plans," "intends," "believes," "forecasts" and variations of such words or similar expressions that predict or indicate future events or trends, or that do not relate to historical matters, identify forward-looking statements. All forward-looking statements are made as of today, and we disclaim any duty to update such statements. Our expectations, beliefs and projections are expressed in good faith and we believe there is a reasonable basis for them. However, there can be no assurance that management's expectations, beliefs and projections will result or be achieved. Investors should not rely on forward-looking statements because they are subject to a variety of risks, uncertainties, and other factors that could cause actual results to differ materially from our expectations. Please refer to our Form 10-K and Form 10-Q concerning factors that could cause actual results to differ materially from those described in our forward-looking statements.

(1) The sheet music business, which we sold in May 2005, contributed $11 million to Music Publishing revenue in the second quarter of fiscal 2005, and was immaterial to our profit measures in that quarter.

Figure 1. Warner Music Group Corp. -- Consolidated Statement of Operations, Three and Six Months Ended 3/31/06 versus 3/31/05 (dollars in millions, except per share amounts)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005	% Change	Six Months Ended March 31, 2006	Six Months Ended March 31, 2005	% Change

	(unaudited)	(unaudited)		(unaudited)	(unaudited)	
Revenues:	$ 796	$ 767	4%	$ 1,840	$ 1,855	(1%)
Costs and expenses:						
Cost of revenues	(409)	(400)	2%	(939)	(981)	(4%)
Selling, general and administrative expenses	(294)	(293)	-	(617)	(624)	(1%)
Amortization of intangible assets	(48)	(47)	2%	(95)	(93)	2%
Total costs and expenses	$ (751)	$ (740)	1%	$ (1,651)	$ (1,698)	(3%)
Operating income	$ 45	$ 27	67%	$ 189	$ 157	20%
Interest expense, net	(45)	(52)	(13%)	(90)	(90)	-
Equity in gains (losses) of equity-method investees	1	-	-	1	(1)	-
Unrealized gain on warrants	-	39	-	-	17	-
Minority interest expense	-	-	-	-	(5)	-
Other income, net	2	-	-	2	4	(50%)
Net income before income taxes	$ 3	$ 14	(79%)	$ 102	$ 82	24%
Income tax expense	(10)	(10)	0%	(40)	(42)	(5%)
Net (loss) income	$ (7)	$ 4	(275%)	$ 62	$ 40	55%
Net income (loss) per share:						
Basic	($ 0.05)	$ 0.04	(233%)	$ 0.44	$ 0.37	18%

Diluted (a)	($ 0.05)	$ (0.28)	(83%)	$ 0.41	$ 0.19	114%
Weighted averages shares outstanding:						
Basic	141.9	107.7	32%	141.7	107.6	32%
Diluted (b)	141.9	123.5	15%	150.6	119.6	26%

(a) Diluted net loss per share for the three months and six months ended March 31, 2005 reflects an add-back to net income for the unrealized gain on warrants as a result of the assumed exercise of the warrants in the calculation.

(b) Diluted shares for the three months ended March 31, 2006 would include an additional 8.9 million shares related to the assumed vesting of restricted stock and assumed exercise of stock options if they were anti-dilutive.

Figure 2. Warner Music Group Corp. -- Consolidated Balance Sheets as of 3/31/06 and 9/30/05 (dollars in millions)

	March 31, 2006	Sept 30, 2005	% Change
	(unaudited)	(audited)	
Assets:			
Current Assets			
Cash & cash equivalents	$ 359	$ 288	25%
Short-term investments	61	-	-
Accounts receivable, less allowances of $230 and $218	530	637	(17%)
Inventories	44	52	(15%)
Royalty advances (to be recouped w/in 1 year)	196	190	3%
Deferred tax assets	32	36	(11%)
Other current assets	56	39	44%
Total Current Assets	$ 1,278	$ 1,242	3%
Royalty advances (to be recouped after 1 year)	196	190	3%
Investments	24	21	14%
Property, plant & equipment, net	147	157	(6%)

Goodwill	876	869	1%
Intangible assets subject to amortization, net	1,737	1,815	(4%)
Intangible assets not subject to amortization	100	100	-
Other assets	106	104	2%
Total Assets	$ 4,464	$ 4,498	(1%)
Liabilities & Shareholders' Equity:			
Current Liabilities			
Accounts payable	$ 211	$ 247	(15%)
Accrued royalties	1,088	1,057	3%
Taxes & other withholdings	43	23	87%
Current portion of long-term debt	17	17	-
Dividend payable	20	-	-
Other current liabilities	327	404	(19%)
Total current liabilities	$ 1,706	$ 1,748	(2%)
Long-term debt	$ 2,226	$ 2,229	-
Dividends payable	6	5	20%
Deferred tax liabilities, net	192	201	(4%)
Other noncurrent liabilities	225	226	-
Total Liabilities	$ 4,355	$ 4,409	(1%)
Common stock	-	-	-
Additional paid-in capital	556	548	1%
Accumulated deficit	(475)	(480)	(1%)
Accumulated other comprehensive income	28	21	33%
Total Shareholders' Equity	$ 109	$ 89	22%
Total Liabilities & Shareholders' Equity	$ 4,464	$ 4,498	(1%)

Figure 3. Warner Music Group Corp. -- Summarized Statement of Cash Flows,

Three Months and Six Months Ended 3/31/06 versus 3/31/05 (dollars in millions)

	Three Months Ended March 31, 2006 (unaudited)	Three Months Ended March 31, 2005 (unaudited)	% Change	Six Months Ended March 31, 2006 (unaudited)	Six Months Ended March 31, 2005 (unaudited)	% Change
Net cash provided by operating activities	$ 176	$ 229	(23%)	$ 205	$ 292	(30%)
Net cash used in investing activities	(75)	(36)	108%	(91)	(61)	49%
Net cash used in financing activities	(23)	(46)	(50%)	(45)	(342)	(87%)
Effect of foreign currency exchange rates on cash	3	(6)	(150%)	2	3	(33%)
Net increase (decrease) in cash	$ 81	$ 141	(43%)	$ 71	$ (108)	(166%)

Supplemental Disclosures Regarding Non-GAAP Financial Information

OIBDA

We evaluate our operating performance based on several factors, including our primary financial measure of operating income (loss) before non-cash depreciation of tangible assets and non-cash amortization of intangible assets (which we refer to as OIBDA). We consider OIBDA to be an important indicator of the operational strengths and performance of our businesses, and believe the presentation of OIBDA helps improve the ability to understand the company's operating performance and evaluate our performance in comparison to comparable periods. However, a limitation of the use of OIBDA as a performance measure is that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenue in our businesses. Accordingly, OIBDA should be

considered in addition to, not as a substitute for, operating income (loss), net income (loss) and other measures of financial performance reported in accordance with accounting principles generally accepted in the U.S.

Figure 4. Warner Music Group Corp. -- Reconciliation of OIBDA to Net Income, Three and Six Months Ended 3/31/06 versus 3/31/05 (dollars in millions)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005	% Change	Six Months Ended March 31, 2006	Six Months Ended March 31, 2005	% Change
	(unaudited)	(unaudited)		(unaudited)	(unaudited)	
OIBDA	$ 104	$ 88	18%	$ 306	$ 278	10%
Depreciation expense	(11)	(14)	(21%)	(22)	(28)	(21%)
Amortization expense	(48)	(47)	2%	(95)	(93)	2%
Operating income	$ 45	$ 27	67%	$ 189	$ 157	20%
Interest expense, net	(45)	(52)	(13%)	(90)	(90)	-
Equity in gains (losses) of equity-method investees	1	-	-	1	(1)	-
Unrealized gain on warrants	-	39	-	-	17	-
Minority interest expense	-	-	-	-	(5)	-
Other income, net	2	-	-	2	4	(50%)
Income before income taxes	$ 3	$ 14	(79%)	$ 102	$ 82	24%
Income tax expense	(10)	(10)	0%	(40)	(42)	(5%)
Net (loss) income	$ (7)	$ 4	(275%)	$ 62	$ 40	55%
OIBDA Margin	13.1%	11.5%		16.6%	15.0%	
Operating Income Margin	5.7%	3.5%		10.3%	8.5%	

Figure 5. Warner Music Group Corp. -- Statement of Operations by Segment, Revenue by Geography, Three and Six Months Ended 3/31/06 versus 3/31/05 (dollars in millions)

	Three Months Ended March 31, 2006 (unaudited)	Three Months Ended March 31, 2005 (unaudited)	% Change	Six Months Ended March 31, 2006 (unaudited)	Six Months Ended March 31, 2005 (unaudited)	% Change
Recorded Music:						
Revenue	$ 676	$ 621	9%	$ 1,596	$ 1,561	2%
OIBDA	81	72	13%	287	266	8%
Depreciation and amortization	41	42	(2%)	81	84	(4%)
Operating Income	$ 40	$ 30	33%	$ 206	$ 182	13%
Music Publishing (a):						
Revenue	$ 129	$ 154	(16%)	$ 260	$ 309	(16%)
OIBDA	47	47	-	68	71	(4%)
Depreciation and amortization	15	15	-	30	29	3%
Operating Income	$ 32	$ 32	-	$ 38	$ 42	(10%)
Total:						
Revenue	$ 796	$ 767	4%	$ 1,840	$ 1,855	(1%)
OIBDA	104	88	18%	306	278	10%
Depreciation and amortization	59	61	(3%)	117	121	(3%)
Operating Income	$ 45	$ 27	67%	$ 189	$ 157	20%

Revenue by Geography:						
US revenue (b)	$ 417	$ 363	15%	$ 876	$ 850	3%
Recorded Music	361	296	22%	768	709	8%
Music Publishing	56	67	(16%)	108	141	(23%)
International revenue	379	404	(6%)	964	1,005	(4%)
Recorded Music	315	325	(3%)	828	852	(3%)
Music Publishing	64	79	(19%)	136	153	(11%)
	$ 796	$ 767	4%	$ 1,840	$ 1,855	(1%)

(a) The sheet music business, which was sold in May 2005, contributed to Music Publishing revenues for the three and six months ended March 31, 2005, as follows:

	3 Months Ended			6 Months Ended		
	Including sheet music business	Sheet music business	Excluding sheet music business	Including sheet music business	Sheet music business	Excluding sheet music business
Revenue	$ 154	11	$ 143	$ 309	26	$ 283
OIBDA	47	(1)	48	71	-	71
Operating Income	32	(1)	33	42	-	42

(b) Excluding prior year revenue from the sheet music business, US Revenue grew by $65 million or 18%, and $52 million or 6%, for the three months and six months ended March 31, 2006, respectively, as compared to the prior year periods.

Constant Currency

As exchange rates are an important factor in understanding period to period comparisons, we believe the presentation of results on a constant currency basis in addition to reported results helps improve the ability to understand the company's operating results and evaluate our performance in comparison to prior periods. Constant currency information compares results between periods as if exchange rates had remained constant period-over-period. We use results on a constant currency basis as one measure to evaluate our performance. However, a limitation of the use of the constant currency results

as a performance measure is that it does not reflect the $31 million, $21 million and $10 million unfavorable impact of exchange rates on our Total, Recorded Music and Music Publishing revenue, respectively, in the three months ended March 31, 2006 compared to the comparable prior year quarter and the $58 million, $44 million and $14 million unfavorable impact of exchange rates on our Total, Recorded Music and Music Publishing revenue, respectively, in the six months ended March 31, 2006 compared to the comparable period in the prior year. Further, it does not reflect the $31 million unfavorable impact of exchange rates on our total international revenue for the three months ended March 31, 2005 or the $31 million unfavorable impact of exchange rates on our revenue for the last twelve months (see Figure 8). These amounts are calculated by comparing our actual results in Figures 1 and 5 with the constant currency amounts in this Figure 6. For example, Revenue for the three months ended March 31, 2005 were $767 million as set forth in Figure 1, compared to $736 million on a constant currency basis as set forth in Figure 6, for a difference of $31 million. These results should be considered in addition to, not as a substitute for, results reported in accordance with accounting principles generally accepted in the U.S. Results on a constant currency basis, as we present them, may not be comparable to similarly titled measures used by other companies and is not a measure of performance presented in accordance with accounting principles generally accepted in the U.S.

Figure 6. Warner Music Group Corp. -- Constant Currency Information - Segment Statement of Operations, Revenue by Geography, on a Non-GAAP Constant Currency Basis and Excluding the Sheet Music Business for the Three and Six Months Ended 3/31/06 versus 3/31/05 (dollars in millions)

	Three Months Ended March 31, 2006 (unaudited)	Three Months Ended March 31, 2005 (unaudited)	% Change	Six Months Ended March 31, 2006 (unaudited)	Six Months Ended March 31, 2005 (unaudited)	% Change
Segment Statement of Operations						
Recorded Music:						
Revenue	$ 676	$ 600	13%	$ 1,596	$ 1,517	5%
OIBDA	81	75	8%	287	263	9%

Depreciation and amortization	41	42	(2%)	81	84	(4%)
Operating Income	$ 40	$ 33	21%	$ 206	$ 179	15%
Music Publishing:						
Revenue	$ 129	$ 144	(10%)	$ 260	$ 295	(12%)
OIBDA	47	44	7%	68	68	-
Depreciation and amortization	15	17	(12%)	30	31	(3%)
Operating Income	$ 32	$ 27	19%	$ 38	$ 37	3%
Total:						
Revenue	$ 796	$ 736	8%	$ 1,840	$ 1,797	2%
OIBDA	104	87	20%	306	272	13%
Depreciation and amortization	59	61	(3%)	117	121	(3%)
Operating Income	$ 45	$ 26	73%	$ 189	$ 151	25%
Sheet Music Business:						
Revenue	$ 0	$ 11	-	$ 0	$ 26	-
OIBDA	-	(1)	-	-	-	-
Depreciation and amortization	-	-	-	-	-	-
Operating Income	$ 0	$ (1)	-	$ 0	$ 0	-
Total excluding Sheet Music Business:						
Revenue	$ 796	$ 725	10%	$ 1,840	$ 1,771	4%
OIBDA	104	88	18%	306	272	13%
Depreciation and amortization	59	61	(3%)	117	121	(3%)

Operating Income	$ 45	$ 27	67%	$ 189	$ 151	25%
Revenue by Geography:						
US revenue	$ 417	$ 363	15%	$ 876	$ 850	3%
Recorded Music	361	296	22%	768	709	8%
Music Publishing	56	67	(16%)	108	141	(23%)
International revenue	$ 379	373	2%	964	947	2%
Recorded Music	315	302	4%	828	806	3%
Music Publishing	64	71	(10%)	136	141	(4%)
Total revenue	$ 796	$ 736	8%	$ 1,840	$ 1,797	2%

Free Cash Flow

Free cash flow reflects our cash flow provided by operating activities less capital expenditures and cash paid or received for investments. We use free cash flow, among other measures, to evaluate our operating performance. Management believes free cash flow provides investors with an important perspective on the cash available to service debt, make strategic acquisitions and investments, fund ongoing operations and working capital needs and pay ongoing regular quarterly dividends. As a result, free cash flow is a significant measure of our ability to generate long-term value. It is useful for investors to know whether this ability is being enhanced or degraded as a result of our operating performance. We believe the presentation of free cash flow is relevant and useful for investors because it allows investors to view performance in a manner similar to the method used by management. In addition, free cash flow is also a primary measure used externally by our investors and analysts for purposes of valuation and comparing the operating performance of our company to other companies in our industry.

As free cash flow is not a measure of performance calculated in accordance with GAAP, free cash flow should not be considered in isolation of, or as a substitute for, net income (loss) as an indicator of operating performance or cash flow provided by operating activities as a measure of liquidity. Free cash flow, as we calculate it, may not be comparable to similarly titled measures employed by other companies. In addition, free cash flow does not necessarily represent funds available for discretionary use and is not necessarily a measure of our ability to fund our cash needs. As free cash flow deducts capital expenditures and cash paid or received for investments from cash flow provided by operating activities, the most directly comparable GAAP financial measure, users of this information should

consider the types of events and transactions that are not reflected. We provide below a reconciliation of free cash flow to the most directly comparable amount reported under GAAP, cash flow provided by operating activities.

Free cash flow includes cash paid for interest and certain non-recurring payments. We also review our cash flow adjusted for these items, a measure we call unlevered after-tax cash flow. Management believes this measure provides investors with an additional important perspective on our cash generation ability. We consider unlevered after-tax cash flow excluding certain non-recurring items to be an important indicator of the performance of our businesses and believe the presentation is relevant and useful for investors because it allows investors to view performance in a manner similar to the method used by management. A limitation of the use of this measure is that it does not reflect the charges noted and, therefore, does not necessarily represent funds available for discretionary use, and is not necessarily a measure of the company's ability to fund its cash needs. Accordingly, this measure should be considered in addition to, not as a substitute for, net cash flow provided by operating activities and other measures of liquidity reported in accordance with accounting principles generally accepted in the U.S.

Figure 7. Warner Music Group Corp. -- Calculation of Free Cash Flow, Three Months and Six Months Ended 3/31/06 versus 3/31/05 (dollars in millions)

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005	Six Months Ended March 31, 2006	Six Months Ended March 31, 2005
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Net cash flow provided by operating activities	$ 176	$ 229	$ 205	$ 292
Less: Capital expenditures	7	8	12	14
Less: Cash paid for investments	7	28	18	47
Free cash flow (a)	$ 162	$ 193	$ 175	$ 231

(a) - Free cash flow includes cash paid for interest and certain non-recurring cash payments as follows (in millions):

	Three Months Ended March 31, 2006	Three Months Ended March 31, 2005	Six Months Ended March 31, 2006	Six Months Ended March 31, 2005
Free cash flow	$ 162	$ 193	$ 175	$ 231
Plus: Cash paid for interest	24	24	71	66
Plus: Cash paid for management fees	-	3	-	5
Unlevered after-tax cash flow	$ 186	$ 220	$ 246	$ 302

Twelve-Month Results

We believe that, especially given the rhythm of the music release schedule and associated marketing and promotional expenses, quarterly variations of results are normal in our businesses. As a result, in addition to viewing our performance for current periods, we evaluate our operating performance on a full-year basis. We manage our business based on twelve-month results and consider twelve-month performance to be an important indicator of the performance of our businesses and believe the presentation of twelve-month results help improve the ability to understand the company's operating performance and evaluate our performance in comparison to prior periods. These twelve-month results should be considered in addition to, not as a substitute for, revenue and other measures of financial performance reported in accordance with accounting principles generally accepted in the U.S. In addition, the twelve-month periods presented below are not accounting periods under SEC rules or accounting principles generally accepted in the U.S. Our twelve months ended March 31, 2006 unaudited revenue was derived from our unaudited financial statements for each of the three-month periods ended March 31, 2006, December 31, 2005, September 30, 2005 and June 30, 2005. Our twelve months ended March 31, 2005 unaudited revenue was derived from our unaudited financial statements for each of the three-month periods ended March 31, 2005, December 31, 2004,

September 30, 2004 and June 30, 2004.

Figure 8. Warner Music Group Corp. -- Last Twelve Months ("LTM") Revenues
(dollars in millions)

	LTM 3/31/06(a)	LTM 3/31/05	% Change
	(unaudited)	(unaudited)	
Q3 2005 / Q3 2004	$ 742	$ 726	2%
Q4 2005 / Q4 2004	905	798	13%
Q1 2006 / Q1 2005	1,044	1,088	(4%)
Q2 2006 / Q2 2005	796	767	4%
Last Twelve Months Revenues	$ 3,487	$ 3,379	3%
Impact of foreign currency exchange rates	-	(31)	-
Last Twelve Months Revenue - Constant Currency	$ 3,487	$ 3,348	4%

(a) - Full fiscal year revenue for the fiscal year ended September 30, 2005 was $3,502.

To download the charts in the above press release, please **Click Here.**

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EXHIBIT CO 0949

Warner Music Group

News

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Warner Music Group Corp. Reports Fiscal First Quarter Results for the Period Ended December 31, 2005

02/14/06

Digital revenue increases 176% to $69 million;
Net income grows 92% to $69 million or $0.46 per diluted share

- Total revenue of $1,044 million for the first quarter 2006 declined 4% year-over-year and was flat year-over-year excluding the impact of exchange rates and the sheet music business sold in May 2005.
- Digital revenue was $69 million climbing to 7% of total revenue in the quarter, up 30% sequentially from the fourth quarter 2005 and 176% from $25 million in the same quarter last year.
- Operating income rose 11% year-over-year to $144 million in the quarter driving a 1.9 percentage point improvement in operating income margin to 13.8%.
- Operating income before depreciation and amortization (OIBDA) in the quarter improved 6% year-over-year to $202 million leading to a 1.8 percentage point expansion in OIBDA margin to 19.3%.
- Net income nearly doubled to $69 million in the quarter from $36 million in the same quarter last year, driving earnings up 47% to $0.46 per diluted share.

Warner Music Group Corp. (NYSE: WMG) today announced its first quarter financial results for the three-month period ended December 31, 2005.

"This report demonstrates that we are transforming our vision into results. Warner Music Group is building on its strong 2005 performance creating sustained growth of shareholder value," said Edgar Bronfman, Jr., Warner Music Group's Chairman and CEO. "Our intense focus on and investment in the digital music business yielded dramatic growth in digital revenue, which was a major contributor to gains in total worldwide Recorded Music performance on a constant-currency basis. Our disciplined approach to profitable growth led to improved OIBDA and margins. In addition, a series of successful releases and A&R achievements also strengthened our competitive position - as reflected by Warner Bros. Records' achieving the top-ranked label of the year for the first time in nine years."

Michael Fleisher, Warner Music Group's Executive Vice President and CFO, added: "We believe that our twelve-month performance is the best indication of the progress we are making in our mission to be a music-based content company. Over the latest twelve months, Warner Music Group's worldwide revenue was up 3% year-over-year outpacing the industry."

First Quarter Results
For the first quarter of fiscal 2006, revenue declined by 4% to $1,044 million from $1,088 million in the same quarter of fiscal 2005, primarily due to exchange rate fluctuations and the contribution from the

sheet music business sold in May 2005. The sheet music business contributed $15 million to Music Publishing revenues and $1 million to each of OIBDA, Operating Income and Net Income in the first quarter of fiscal 2005. On a constant-currency basis (excluding a $27 million unfavorable impact of exchange rates) and excluding the sheet music business, quarterly revenue dipped 0.2% year-over-year. While reported revenue from both domestic and international markets each slipped 3% excluding the sheet music business in the prior year, international revenue actually rose by 1.9% on a constant-currency basis.

Operating income for the quarter rose by $14 million to $144 million from $130 million in the prior year. On a constant-dollar basis, the company's operating income improved by 15% from the comparable fiscal 2005 quarter.

OIBDA for the quarter rose by $12 million to $202 million from $190 million last year, driving margin improvement of 1.8 percentage points to 19.3%.

Reported net income was $69 million or $0.46 per diluted share for the quarter compared to $36 million or $0.31 per diluted share in the comparable prior-year period.

The company also reported a cash balance of $278 million, total long-term debt of $2.2 billion and net debt (total long-term debt minus cash) of approximately $2.0 billion, as of December 31, 2005.

For the quarter, free cash flow (calculated by taking cash flow from operations less capital expenditures and cash paid for investments) amounted to $13 million compared to $38 million in the comparable fiscal 2005 quarter. Unlevered after-tax cash flow (defined as free cash flow less cash interest paid and non-recurring management fees) was $60 million compared to $83 million in the comparable fiscal 2005 quarter (see below for calculation of Non-GAAP Free Cash Flow).

The current quarter operating cash flow was negatively affected as compared to the same quarter last year by the shift of employee annual bonus payments from the second fiscal quarter to the first fiscal quarter, given the change in the fiscal year-end from November 30 to September 30.

Below is the business segment discussion for the quarter.

Recorded Music

Revenue for the company's Recorded Music business decreased 2% to $920 million. Digital Recorded Music revenue of $64 million represented 7% of total Recorded Music revenue and grew 36% sequentially from the fourth quarter of fiscal 2005. Major sellers in the quarter included product from Madonna, Enya, James Blunt, Green Day and Notorious B.I.G.

While domestic Recorded Music revenue was largely flat, declining 1.5% to $407 million year-over-year, international Recorded Music revenue grew by 1.8%, excluding $23 million attributable to the negative impact of exchange rates. This year-over-year international revenue growth was primarily driven by growth in Europe in the quarter led by the United Kingdom and strong double-digit gains in the Asia/Pacific region, slightly offset by modest declines in Latin America.

Recorded Music operating income climbed 9% to $166 million in the quarter over the prior year, yielding an operating margin of 18.0%, up 1.8 percentage points from the comparable prior-year period.

Recorded Music OIBDA grew 6% to $206 million for the quarter compared to $194 million in the prior-year comparable period as a result of a more profitable product mix, including higher-margin digital

sales. This drove a 1.8 percentage point expansion in OIBDA margins to 22.4% as compared to the same quarter last year.

Music Publishing
Music Publishing revenue decreased 15% compared to the same quarter in the prior year to $131 million in the quarter and was down only 4% year-over-year on a constant-currency basis excluding a $4 million unfavorable impact of exchange rates and the impact of the sheet music business. Digital revenue from Music Publishing amounted to $5 million which represents 4% of total Music Publishing revenue for the quarter.

Declines in both mechanical revenue and performance revenue of 6% were partially offset by growth in digital and other revenue sources. Performance revenue and mechanical revenue results reflect radio airplay and declines in prior period record sales. Synchronization revenue, consisting of movie, video game and advertisement deals as well as sales in newer formats, particularly of ringtones, was flat.

Music Publishing operating income was $6 million in the quarter compared to $10 million in the prior-year quarter ($9 million excluding the sheet music business). Music Publishing OIBDA was $21 million for the quarter, compared to $24 million in the same quarter of fiscal 2005 ($23 million excluding the sheet music business).

FAS 123 Expenses
FAS 123 expenses, which represent stock compensation expenses, amounted to $6 million for the quarter ended December 31, 2005 and $2 million for the quarter ended December 31, 2004. Recorded Music FAS 123 expenses amounted to $3 million and $2 million, for the quarters ended December 31, 2005 and 2004, respectively. Music Publishing FAS 123 expenses amounted to $1 million for the quarter ended December 31, 2005. Corporate FAS 123 expenses amounted to $2 million for the quarter ended December 31, 2005.

Financial details for the company□s first fiscal quarter 2006 can be found in the Form 10-Q filed today with the Securities and Exchange Commission.

This morning, management will be hosting a conference call to discuss the results at 8:30 A.M. EST. The call will be webcast on **www.wmg.com** [http://www.wmg.com/].

About Warner Music Group
Warner Music Group became the only stand-alone music company to be publicly traded in the United States in May 2005. With its broad roster of new stars and legendary artists, Warner Music Group is home to a collection of the best-known record labels in the music industry including Asylum, Atlantic, Bad Boy, Cordless, East West, Elektra, Lava, Maverick, Nonesuch, Reprise, Rhino, Sire, Warner Bros. and Word. Warner Music International, a leading company in national and international repertoire, operates through numerous international affiliates and licensees in more than 50 countries. Warner Music Group also includes Warner/Chappell Music, one of the world's leading music publishers, with a catalog of more than one million copyrights worldwide.

"Safe Harbor" Statement under Private Securities Litigation Reform Act of 1995:
This communication includes forward-looking statements that reflect the current views of Warner Music Group about future events and financial performance. Words such as "estimates," "expects," "anticipates," "projects," "plans," "intends," "believes," "forecasts" and variations of such words or similar expressions that predict or indicate future events or trends, or that do not relate to historical

matters, identify forward-looking statements. All forward-looking statements are made as of today, and we disclaim any duty to update such statements. Our expectations, beliefs and projections are expressed in good faith and we believe there is a reasonable basis for them. However, there can be no assurance that management's expectations, beliefs and projections will result or be achieved. Investors should not rely on forward-looking statements because they are subject to a variety of risks, uncertainties, and other factors that could cause actual results to differ materially from our expectations. Please refer to our Form 10-K and Form 10-Q concerning factors that could cause actual results to differ materially from those described in our forward-looking statements.

Figure 1: Warner Music Group Corp. - Consolidated Statement of Operations, Three Months Ended 12/31/05 versus 12/31/04
(dollars in millions, except per share amounts)

	Three Months Ended Dec.31 2005	Three Months Ended Dec.31, 2004	% Change
	(unaudited)	(unaudited)	
Revenues:	$1,044	$1,093	(4%)
Costs and Expenses:			
Cost of revenues	(530)	(581)	(9%)
Selling, general and administrative expenses	(323)	(331)	(2%)
Amortization of intangible assets	(17)	(16)	2%
Total Costs and Expenses	(870)	(928)	(6%)
Operating income	$174	$130	11%
Interest expense, net	(15)	(33)	13%
Equity in losses of equity-method investees	-	(1)	-
Unrealized loss on warrants	-	(22)	-
Minority interest expense	-	(9)	-
Other income, net	-	2	-
Net income before income taxes	$159	$68	45%
Income tax expense	(90)	(32)	(65)
Net income	$69	$36	92%
Earnings Per Share:			
Basic	$0.49	$0.33	48%
Diluted	$0.45	$0.31	47%
Weighted Average Shares Outstanding:			
Basic	141.4	107.5	32%
Diluted	153.5	115.3	31%

Figure 2: Warner Music Group Corp. - Consolidated Balance Sheets as of 12/31/05 and

Figure 2. Warner Music Group Corp. -Consolidated Balance Sheets as of 12/31/05 and 9/30/05 (dollars in millions)

	Dec. 31, 2005 (unaudited)	Sept 30, 2005 (audited)	% Change
Assets:			
Current Assets:			
Cash & cash equivalents	$278	$233	19%
Accounts receivable, less allowances of $275 and $213	749	637	13%
Inventories	53	52	2%
Royalty advances (to be recouped within 1 year)	205	190	8%
Deferred tax assets	36	36	-
Other current assets	35	39	(10%)
Total Current Assets	$1,356	$1,242	9%
Royalty advances (to be recouped after 1 year)	205	190	8%
Investments	22	21	5%
Property, plant & equipment, net	151	157	(4%)
Goodwill	869	869	-
Intangible assets subject to amortization, net	1,788	1,815	(1%)
Intangible assets not subject to amortization	100	100	-
Other assets	104	104	-
Total Assets	$4,575	$4,458	3%
Liabilities & Shareholders' Equity:			
Current Liabilities:			
Accounts payable	$215	$247	(13%)
Accrued royalties	1,185	1,057	12%
Taxes & other withholdings	49	23	113%
Current portion of long-term debt	17	17	-
Dividend payable	20	-	-
Other current liabilities	339	401	(15%)
Total current liabilities	$1,825	$1,745	5%
Long-term debt	$2,224	$2,229	-
Advances payable	6	5	20%
Deferred tax liabilities, net	193	201	(4%)
Other noncurrent liabilities	216	225	(4%)
Total Liabilities	$4,444	$4,405	1%
Common stock	-	-	-
Additional paid-in capital	554	548	1%
Retained earnings (deficit)	(447)	(450)	(1%)
Accumulated other comprehensive income	26	21	24%
Total Shareholders' Equity	$131	$119	10%
Total Liabilities & Shareholders' Equity	$4,575	$4,458	3%

9/30/05 (dollars in millions)

Figure 3: Warner Music Group Corp. - Summarized Statement of Cash Flows, Three Months Ended 12/31/05 versus 12/31/04 (dollars in millions)

	Three Months Ended Dec. 31, 2005 (unaudited)	Three Months Ended Dec. 31, 2004 (unaudited)	% Change
Net cash provided by operating activities	$29	$63	(54%)
Net cash used in investing activities	(15)	(25)	(36%)
Net cash used in financing activities	(22)	(256)	(93%)
Effect of foreign currency exchange rates on cash	(1)	9	(111%)
Net decrease in cash	($10)	($249)	(96%)

Supplemental Disclosures Regarding Non-GAAP Financial Information

OIBDA

We evaluate our operating performance based on several factors, including our primary financial measure of operating income (loss) before non-cash depreciation of tangible assets and non-cash amortization of intangible assets (which we refer to as OIBDA). We consider OIBDA to be an important indicator of the operational strengths and performance of our businesses, and believe the presentation of OIBDA helps improve the ability to understand the company's operating performance and evaluate our performance in comparison to comparable periods. However, a limitation of the use of OIBDA as a performance measure is that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in our businesses. Accordingly, OIBDA should be considered in addition to, not as a substitute for, operating income (loss), net income (loss) and other

measures of financial performance reported in accordance with accounting principles generally accepted in the U.S.

Figure 4: Warner Music Group Corp. - Reconciliation of OIBDA to Net Income, Three Months Ended 12/31/05 versus 12/31/04 (dollars in millions)

	Three Months Ended Dec. 31, 2005 (unaudited)	Three Months Ended Dec. 31, 2004 (unaudited)	% Change
OIBDA	$202	$190	6%
Depreciation expense	(11)	(14)	(21%)
Amortization expense	(47)	(46)	2%
Operating income	$144	$130	11%
Interest expense, net	(45)	(33)	18%
Equity in losses of equity-method investees	-	(1)	-
Unrealized loss on warrants	-	(22)	-
Minority interest expense	-	(5)	-
Other income, net	-	1	-
Income before income taxes	$99	$68	46%
Income tax expense	(30)	(32)	(6%)
Net income	$69	$36	92%
OIBDA Margin	19.3%	17.5%	
Operating Income Margin	13.8%	11.9%	

Figure 5: Warner Music Group Corp. - Statement of Operations by Segment, Three Months Ended 12/31/05 versus 12/31/04 (dollars in millions)

	Three Months Ended Dec. 31, 2005 (unaudited)	Three Months Ended Dec. 31, 2004 (unaudited)	% Change
Recorded Music:			
Revenue	$920	$940	(2%)
OIBDA	206	194	6%
Depreciation and amortization	40	42	(5%)
Operating income	$166	$152	9%
Music Publishing (a):			
Revenue	$131	$155	(15%)
OIBDA	21	24	(13%)
Depreciation and amortization	15	14	7%
Operating income	$6	$10	(40%)
Total:			
Revenue	$1,044	$1,058	(4%)
OIBDA	202	190	6%
Depreciation and amortization	58	60	(3%)
Operating income	$144	$130	11%

(a) The sheet music business, which was sold in May 2005, contributed $18 million to Music Publishing revenues and $1 million to Music Publishing OIBDA and Operating income in the three months ended December 31, 2004, as follows:

	Including sheet music business	Sheet music business	Excluding sheet music business
Revenue	133	15	140
OIBDA	24	1	23
Operating income	10	1	9

Constant Currency

As exchange rates are an important factor in understanding period to period comparisons, we believe the presentation of results on a constant currency basis in addition to reported results helps improve the ability to understand the company's operating results and evaluate our performance in comparison to prior periods. Constant currency information compares results between periods as if exchange rates had remained constant period-over-period. We use results on a constant currency basis as one measure to evaluate our performance. However, a limitation of the use of the constant currency results as a performance measure is that it does not reflect the $27 million, $23 million and $4 million unfavorable impact of exchange rates on our Total, Recorded Music and Music Publishing results, respectively, in the three months ended December 31, 2005 compared to the comparable prior year quarter. These

results should be considered in addition to, not as a substitute for, results reported in accordance with accounting principles generally accepted in the U.S. Results on a constant currency basis, as we present them, may not be comparable to similarly titled measures used by other companies and is not a measure of performance presented in accordance with accounting principles generally accepted in the U.S.

Figure 6: Warner Music Group Corp. - Constant Currency Information - Consolidated Statement of Operations and Segment Statement of Operations on a Non-GAAP Constant Currency Basis for the Three Months Ended 12/31/05 versus 12/31/04 (dollars in millions, except per share amounts)

	Three Months Ended Dec. 31 2005 (unaudited)	Three Months Ended Dec. 31, 2004 (unaudited)	% Change
Consolidated Statement of Operations			
Revenues:	$1,044	$1,061	(2%)
Costs and Expenses:			
Cost of revenues	(530)	(566)	(6%)
Selling, general and administrative expenses	(323)	(324)	-
Amortization of intangible assets	(17)	(16)	2%
Total Costs and Expenses	(900)	(936)	(4%)
Operating income	$144	$125	15%
Interest expense, net	(45)	(35)	13%
Equity in losses of equity-method investees	-	(1)	-
Unrealized loss on warrants	-	(22)	-
Minority interest expense	-	(5)	-
Other income, net	-	1	-
Net income before income taxes	$99	$63	57%
Income tax expense	(37)	(32)	(6%)
Net income	$62	$31	123%
Segment Statement of Operations			
Recorded Music:			
Revenue	$920	$917	-
OIBDA	206	189	9%
Depreciation and amortization	40	42	(3%)
Operating income	$166	147	13%
Music Publishing:			
Revenue	$131	$151	(13%)
OIBDA	21	24	(13%)
Depreciation and amortization	15	14	7%
Operating income	35	$10	(10%)
Total:			
Revenue	$1,044	$1,061	(2%)
OIBDA	202	185	9%
Depreciation and amortization	58	60	(3%)
Operating income	$144	$125	15%

Free Cash Flow

Free cash flow reflects our cash flow provided by operating activities less capital expenditures and cash paid or received for investments. We use free cash flow, among other measures, to evaluate our operating performance. Management believes free cash flow provides investors with an important perspective on the cash available to service debt, make strategic acquisitions and investments, fund ongoing operations and working capital needs and pay ongoing regular quarterly dividends. As a result, free cash flow is a significant measure of our ability to generate long-term value. It is useful for investors to know whether this ability is being enhanced or degraded as a result of our operating performance. We believe the presentation of free cash flow is relevant and useful for investors because it allows investors to view performance in a manner similar to the method used by management. In addition, free cash flow is also a primary measure used externally by our investors and analysts for purposes of valuation and comparing the operating performance of our company to other companies in our industry.

As free cash flow is not a measure of performance calculated in accordance with GAAP, free cash flow should not be considered in isolation of, or as a substitute for, net income (loss) as an indicator of operating performance or cash flow provided by operating activities as a measure of liquidity. Free cash flow, as we calculate it, may not be comparable to similarly titled measures employed by other companies. In addition, free cash flow does not necessarily represent funds available for discretionary use and is not necessarily a measure of our ability to fund our cash needs. As free cash flow deducts capital expenditures and cash paid or received for investments from cash flow provided by operating activities, the most directly comparable GAAP financial measure, users of this information should consider the types of events and transactions that are not reflected. We provide below a reconciliation of free cash flow to the most directly comparable amount reported under GAAP, cash flow provided by operating activities.

Free cash flow includes cash paid for interest and certain non-recurring payments. We also review our cash flow adjusted for these items, a measure we call unlevered after-tax cash flow. Management believes this measure provides investors with an additional important perspective on our cash generation ability. We consider unlevered after-tax cash flow excluding certain non-recurring items to be an important indicator of the performance of our businesses and believe the presentation is relevant and useful for investors because it allows investors to view performance in a manner similar to the method used by management. A limitation of the use of this measure is that it does not reflect the charges noted and, therefore, does not necessarily represent funds available for discretionary use, and is not necessarily a measure of the company□s ability to fund its cash needs. Accordingly, this measure should be considered in addition to, not as a substitute for, net cash flow provided by operating activities and other measures of liquidity reported in accordance with accounting principles generally accepted in the U.S.

Figure 7: Warner Music Group Corp. - Calculation of Free Cash Flow, Three Months Ended 12/31/05 versus 12/31/04 (dollars in millions)

	Three Months Ended Dec. 31, 2005 (unaudited)	Three Months Ended Dec. 31, 2004 (unaudited)
Net cash flow provided by operating activities	$29	$63
Less: Capital expenditures	5	6
Less: Cash paid (received) for investments	11	19
Free cash flow (a)	$13	$38

(a) - Free cash flow includes cash paid for interest and certain non-recurring cash payments as follows (in millions):

	Three Months Ended Dec. 31, 2005	Three Months Ended Dec. 31, 2004
Free cash flow	$13	$38
Plus: Cash paid for interest	47	42
Plus: Cash paid for management fees	-	3
Unlevered after-tax cash flow	$60	$83

Twelve-Month Result

We believe that, especially given the rhythm of the music release schedule and associated marketing and promotional expenses, quarterly variations of results are normal in our businesses. As a result, in addition to viewing our performance for current periods, we evaluate our operating performance on a full-year basis. We manage our business based on twelve-month results and consider twelve-month

performance to be an important indicator of the performance of our businesses and believe the presentation of twelve-month results help improve the ability to understand the company's operating performance and evaluate our performance in comparison to prior periods. These twelve-month results should be considered in addition to, not as a substitute for, revenue and other measures of financial performance reported in accordance with accounting principles generally accepted in the U.S. In addition, the twelve-month periods presented below are not accounting periods under SEC rules or accounting principles generally accepted in the U.S. Our twelve months ended December 31, 2005 unaudited revenues were derived from our unaudited financial statements for each of the three-month periods ended December 31, 2005, September 30, 2005, June 30, 2005 and March 31, 2005. Our twelve months ended December 31, 2004 unaudited revenues were derived from our unaudited financial statements for each of the three-month periods ended December 31, 2004, September 30, 2004, June 30, 2004 and March 31, 2004. The three-month period ended March 31, 2004 represents the combination of the two months ended February 29, 2004 of our predecessor company and the one-month ended March 31, 2004 of our successor company.

Figure 8: Warner Music Group Corp. - Last Twelve Months ("LTM") Revenues (dollars in millions)

	LTM 12/31/05[a] (unaudited)	LTM 12/31/04 (unaudited)	% Change
Q2 2005 / Q2 2004[b]	$757	$735	4%
Q3 2005 / Q3 2004	742	726	2%
Q4 2005 / Q4 2004	903	793	13%
Q1 2006 / Q1 2005	1,041	1,053	(1%)
Last Twelve Months Revenues	$3,443	$3,347	3%

(a) - The quarter ended March 31, 2004 reflects the combination of the two months ended February 29, 2004 of the predecessor company and the one month ended March 31, 2004 of the successor company.

(b) - Fiscal year revenue for the fiscal year ended September 30, 2005 was $3,522.

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Please note that while you are reviewing any information on this website, the information is posted as of the dates listed. The Company has no obligation to update the information in the e-mail alerts or otherwise from this website, which speak as of their respective dates.

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Warner Music Group Corp. Reports Full Year and Fourth Quarter Results for the Period Ended September 30, 2005

Revenue Increases by 13% for the Quarter and by 2% for the Full Year

- Total revenue grew 13% year-over-year to $905 million for the fourth quarter 2005, driven by strong growth in Recorded Music.
- Digital revenue represented 6% of total revenue in the fourth quarter 2005 and rose to $53 million, up 20% sequentially from the third quarter.
- Operating income increased to $19 million for the quarter, as compared to $3 million in the fourth quarter of 2004. Excluding the previously announced Lava restructuring costs, certain other non-recurring items and FAS 123 expenses in 2005 as well as certain non-recurring costs in 2004 (see Non-Recurring Items below), adjusted operating income increased 85% to $61 million.
- Operating income before depreciation and amortization (OIBDA) for the fourth quarter 2005 rose 24% year-over-year to $77 million. Excluding non- recurring items and FAS 123 expenses (see Non-Recurring Items below), adjusted OIBDA grew 29% to $119 million.
- Net losses for the quarter amounted to ($0.21) per share as compared to net losses of ($1.27) per share in 2004. However, excluding non- recurring items and FAS 123 expenses (see Non-Recurring Items below), adjusted earnings were $0.08 per diluted share, a major improvement from last year's adjusted net losses of ($1.01) per share.

Warner Music Group Corp. (NYSE: WMG) today announced its full-year and fourth-quarter financial results for the period ended September 30, 2005.

"This report demonstrates that Warner Music Group is translating its vision and marketplace

momentum into results," said Edgar Bronfman, Jr., Warner Music Group's Chairman and CEO. "Our focus on the digital music business has yielded dramatic growth in digital revenue. Not only did annual digital revenue rise more than four-fold year-over-year to represent 6% of our fourth-quarter revenue, but we are also proud to report that for our 2005 fiscal year the absolute growth in digital revenue outpaced the absolute decline in physical revenue for our U.S. Recorded Music business."

"As we complete our first fiscal year as a publicly traded company, we remain committed to delivering value to our artists, consumers and our shareholders as we lead the transformation of the music industry."

Michael Fleisher, Warner Music Group's Executive Vice President and CFO, added: "In addition to our solid revenue and OIBDA growth, we generated strong cash flow for the quarter and fiscal year. Net cash provided by operating activities for the year was $205 million. We also focus on unlevered after-tax cash flow as an important measure of our cash-generating ability. For the fiscal year we converted 84% of adjusted OIBDA into unlevered after-tax cash flow excluding non-recurring IPO-related items. Our ability to convert OIBDA into unlevered after-tax cash flow benefits from disciplined control of capital expenditures and our valuable amortization tax deduction of about $100 million annually, which together with our interest expense deduction completely offsets our taxable income in the U.S."

Fourth Quarter Results

For the fourth quarter 2005, revenue climbed 13% to $905 million from $798 million in 2004, driven primarily by a strong fourth-quarter release schedule and continued growth in digital. On a constant-currency basis, quarterly revenue grew 12%. Domestic revenue grew 17% while international markets advanced 11% or 9% on a constant-currency basis.

Operating income for the quarter rose by $16 million to $19 million from $3 million in the prior year. Excluding non-recurring items and FAS 123 expenses (see Non-Recurring Items below), the company's adjusted operating income improved by 85% to $61 million from $33 million in the comparable 2004 quarter.

OIBDA for the quarter rose 24% to $77 million from $62 million last year. Excluding non-recurring items and FAS 123 expenses (see Non-Recurring Items below), the company's adjusted OIBDA improved 29% year-over-year to $119 million from $92 million, driving margin improvement of 1.6 percentage points to 13.1%.

Reported net losses were $30 million or ($0.21) per share for the quarter. Net losses in the fourth quarter of 2004 were $137 million or ($1.27) per share. Excluding non-recurring items and FAS 123 expenses (see Non-Recurring Items below), adjusted net income for the fourth quarter 2005 was $12 million or $0.08 per diluted share, compared to adjusted net losses of $109 million or ($1.01) per share for the comparable quarter in 2004.

The company also reported a cash balance of $288 million, total long-term debt of $2.2 billion and net debt (total long-term debt minus cash) of $1.9 billion, as of September 30, 2005.

For the quarter, the company's business segment performance was as follows:

Recorded Music

Revenue for the company's Recorded Music business increased 17% to $775 million. Digital Recorded Music revenue of $47 million represented 6% of total Recorded Music revenue and grew 24% sequentially from the third quarter. Major sellers in the quarter were James Blunt, Faith Hill, Green Day, Eric Clapton, Sean Paul, Disturbed, Staind and Craig David.

Recorded Music operating income climbed to $27 million from $2 million last year. Excluding non-recurring items and FAS 123 expenses (see Non-Recurring Items below), adjusted operating income increased by $43 million to $63 million yielding a margin of 8.1%, up 5.1 percentage points from 3.0% in the comparable prior-year period.

Recorded Music OIBDA grew 60% to $67 million for the quarter compared to $42 million in last year's comparable period. Excluding non-recurring items and FAS 123 expenses (see Non-Recurring Items below), quarterly Recorded Music adjusted OIBDA increased 72% to $103 million from $60 million in last year's comparable quarter as cost-savings initiatives and higher-margin digital sales contributed to results. Recorded Music adjusted OIBDA margin rose 4.2 percentage points to 13.3% as compared to the same quarter last year.

Music Publishing

Music Publishing revenue decreased 2% to $137 million compared to last year's comparable period. However, last year's comparable quarter included $9 million of revenue from the Sheet Music business divested on May 31, 2005. Excluding this amount from last year's fourth quarter Music Publishing revenue to compare revenue on a continuing operations basis, Music Publishing revenue

rose by 5%. Digital revenue from Music Publishing of $6 million represented 4% of total Music Publishing revenue.

Synchronization and performance revenue increased while mechanical revenue was relatively flat with the prior year. Movie, video game and advertisement deals as well as continued increases in sales in newer formats, particularly of ringtones, drove higher synchronization revenue. Performance revenue increases reflect both improved chart activity and the timing of Music Publishing A&R investments. Mechanical revenue results are reflective of the state of the recorded music industry.

Music Publishing operating income was $27 million in the quarter compared to $31 million in the prior-year quarter. Music Publishing OIBDA was $42 million for the quarter, compared to $44 million in the prior-year quarter. Music Publishing OIBDA margin was 30.7%, relatively flat with the comparable prior-year period.

Full Year Results

For the full year 2005, Warner Music Group revenue increased 2% to $3.5 billion from $3.4 billion in the prior year. On a constant-currency basis, total revenue fell 1%. Total revenue was split 48% and 52% between domestic and international territories, respectively, on a constant-currency basis. Total digital revenue increased more than four-fold to $157 million and was split 73% domestic and 27% international, showing the more advanced state of the domestic digital industry.

Warner Music Group's reported operating income of $84 million reflected solid growth by both Recorded Music and Music Publishing.

OIBDA for the year amounted to $322 million compared to $333 million last year. However, excluding non-recurring items and FAS 123 expenses (see Non-Recurring Items below), adjusted OIBDA rose 31% to $491 million from $374 million last year, contributing to a 3.1 percentage point margin improvement to 14.0%, as results benefited from cost savings and higher margins on digital sales.

Reported net losses were $169 million or ($1.40) per share, compared to net losses of $1.4 billion reported last year. Excluding non-recurring items and FAS 123 expenses (see Non-Recurring Items below), adjusted net income was $32 million, or $0.25 per diluted share, compared to adjusted net losses of $295 million last year.

For the full fiscal year, the company's business segment performance was as follows:

Recorded Music

Recorded Music revenue improved 2% to $2.9 billion, led by robust digital sales and a broad slate of successful releases. Digital Recorded Music revenue of $137 million represented 5% of total Recorded Music revenue. Domestic Recorded Music digital revenue amounted to $105 million or 7% of total domestic Recorded Music revenue. Major sellers for the year were Green Day, Linkin Park/Jay-Z, Michael Buble, James Blunt, Simple Plan, Ray Charles, Rob Thomas and Faith Hill.

Recorded Music operating income was $215 million for the year and when adjusted for non-recurring items and FAS 123 expenses (see Non-Recurring Items below), more than doubled to $283 million compared to $110 million last year, yielding an adjusted operating margin of 9.7%, up 5.8 percentage points from 3.9% in the comparable prior-year period.

Recorded Music OIBDA improved 43% to $380 million for the year from $266 million last year. Excluding non-recurring items and FAS 123 expenses (see Non-Recurring Items below), adjusted OIBDA rose 54% to $448 million. Recorded Music adjusted OIBDA margin rose 5.1 percentage points to 15.3% resulting from cost management, prior-period restructuring efforts and higher margins on digital sales.

Music Publishing

Music Publishing revenue advanced by 1% to $607 million compared to last year's comparable period. 2004 revenue included $49 million and 2005 revenue included $35 million from the Sheet Music business divested on May 31, 2005. Excluding these amounts from both periods, revenue advanced 4%.

Digital revenue from Music Publishing of $20 million represented 3% of total Music Publishing revenue. Increases in synchronization revenue were largely offset by declines in mechanical and performance revenue. Movie, video game and advertisement deals as well as DVDs drove higher synchronization revenue. Declines in mechanical and performance revenue reflect prior-year recorded music industry declines and the timing of Music Publishing A&R investments.

Music Publishing operating income increased 11% to $82 million for the year, yielding an operating margin of 13.5%, up 1.2 percentage points year-over-year. Music Publishing OIBDA was $141 million, down 2% from $144 million last year, leading to a margin decline of 0.7 percentage points to 23.2%.

Non-Recurring Items

In the fourth quarter of 2005, non-recurring items included a previously announced restructuring charge of $7 million for the integration of the Lava label into The Atlantic Records Group, which included severance and contract terminations related to the integration of operations, as well as other non-recurring charges of $24 million specifically related to the departure of one of the executives of Atlantic and the expensing of certain other amounts. Approximately $20 million of these charges were non-cash. In addition, Warner Music Group took a $4 million charge in the fourth quarter for the $5 million settlement of a government investigation into radio promotion practices by New York State Attorney General, Eliot Spitzer, which is detailed in the 10-K. The remaining $1 million of this settlement was accrued for in the third fiscal quarter.

For the year ended September 30, 2005, non-recurring, IPO-related items included the $73 million fee to terminate the management contract with the Investor Group, $6 million of management fees paid to the Investor Group under the management contract prior to the termination, certain cash payments to employees totaling $29 million related to the issuance of stock awards below fair market value and payment of an IPO cash bonus to employees, as well as $35 million resulting from the payment of redemption premiums and other charges in connection with the previously announced redemption of debt issued by the subsidiary, WMG Holdings Corp. All of these charges were previously reported in the third quarter 2005 results.

The non-recurring items had a related tax benefit of $3 million for the 2005 fiscal year and had no effect during the quarter.

Non-recurring items in 2004 included a $1.0 billion impairment of goodwill and intangibles charge primarily reflecting the declines in the valuation of music-related assets. This charge was taken by Time Warner in preparation for the sale of its music division to the Investor Group. In addition, Warner Music Group incurred $34 million in restructuring charges, which included $20 million associated with the implementation of a cost-savings incentive compensation plan designed to reduce operating costs, $6 million from headcount reductions and $8 million from prior company restructuring charges for reductions in headcount and termination of leases. Finally, 2004 non-recurring items included $6 million in management fees paid to the Investor Group and a $6 million loss on repayment of debt.

The non-recurring items had a related tax benefit of $2 million for both our 2004 fiscal year and the fourth quarter of 2004.

See also Supplemental Disclosures Regarding Non-GAAP Financial Information, Adjusted Results in Figures 4, 5, and 6 below.

FAS 123 Expenses

FAS 123 expenses for the year 2005 amounted to $25 million and to $7 million for the quarter ending September 30, 2005. FAS 123 expenses for both the year 2004 and the quarter ended September 30, 2004 amounted to $1 million.

Financial details for the full fiscal year can be found in the company's current Form 10-K, filed today with the Securities and Exchange Commission.

This morning, management will be hosting a conference call to discuss the results at 8:30 A.M. EST. The call will be webcast on www.wmg.com.

About Warner Music Group

Warner Music Group became the only stand-alone music company to be publicly traded in the United States in May 2005. With its broad roster of new stars and legendary artists, Warner Music Group is home to a collection of the best-known record labels in the music industry including Asylum, Atlantic, Bad Boy, Cordless, East West, Elektra, Lava, Maverick, Nonesuch, Reprise, Rhino, Sire, Warner Bros. and Word. Warner Music International, a leading company in national and international repertoire operates through numerous international affiliates and licensees in more than 50 countries. Warner Music Group also includes Warner/Chappell Music, one of the world's leading music publishers, with a catalog of more than one million copyrights worldwide.

"Safe Harbor" Statement under Private Securities Litigation Reform Act of 1995:

This communication includes forward-looking statements that reflect the current views of Warner Music Group about future events and financial performance. Words such as "estimates," "expects," "anticipates," "projects," "plans," "intends," "believes," "forecasts" and variations of such words or similar expressions that predict or indicate future events or trends, or that do not relate to historical matters, identify forward-looking statements. Our expectations, beliefs and projections are expressed in good faith and we believe there is a reasonable basis for them. However, there can be no assurance that management's expectations, beliefs and projections will result or be achieved. Investors should not rely on forward-looking statements because they are subject to a variety of risks,

uncertainties, and other factors that could cause actual results to differ materially from our expectations.

Figure 1. Warner Music Group Corp. - Consolidated Statement of Operations, Three Months and Twelve Months Ended 9/30/05 versus 9/30/04 (dollars in millions except per share amounts)

	Three Months Ended Sept 30, 2005	Three Months Ended Sept 30, 2004	Twelve Months Ended Sept 30, 2005	Twelve Months Ended Sept 30, 2004(a)
	(unaudited)	(unaudited)	(audited)	(unaudited)
Revenues:	$905	$798	$3,502	$3,437
Costs and Expenses:				
Cost of revenues	(473)	(421)	(1,850)	(1,850)
Selling, general and administrative expenses	(359)	(304)	(1,301)	(1,287)
Amortization of intangible assets	(47)	(44)	(187)	(201)
Loss on termination of management agreement	-	-	(73)	-
Impairment of goodwill and other intangible assets	-	-	-	(1,019)
Restructuring costs	(7)	(26)	(7)	(34)
Total Costs and Expenses	($886)	($795)	($3,418)	($4,391)
Operating Income	$19	$3	$84	($954)
Interest expense, net	(42)	(35)	(182)	(82)
Net investment-related gains (losses)	-	-	1	(9)
Loss on repayment of debt	-	-	(35)	(6)

Equity in losses of equity-method investees	-	(2)	(1)	(13)
Deal-related transaction costs	-	-	-	(63)
Unrealized (loss) gain on warrants	-	(73)	17	(120)
Minority interest expense	-	(5)	(5)	(14)
Other income (expense), net	2	(4)	7	(11)
Loss before income taxes	($21)	($116)	($114)	($1,272)
Income tax expense	(9)	(21)	(55)	(150)
Net Loss	($30)	($137)	($169)	($1,422)
Earnings Per Share:				
Basic and Diluted	($0.21)	($1.27)	($1.40)	
Weighted Averages Shares Outstanding:				
Basic	141,208,577	107,544,923	120,910,235	
Diluted	150,492,386	113,670,396	129,355,871	

(a) - The twelve-month period ended September 30, 2004 is the combination of the five months ended February 29, 2004 of the predecessor company and the seven months ended September 30, 2004 of the successor company.

Figure 2. Warner Music Group Corp. - Statement of Operations by Segment, Three Months and Twelve Months Ended 9/30/05 versus 9/30/04
(dollars in millions)

	Three Months Ended Sept 30, 2005	Three Months Ended Sept 30, 2004	Twelve Months Ended Sept 30, 2005	Twelve Months Ended Sept 30, 2004(a)
	(unaudited)	(unaudited)	(audited)	(unaudited)
Recorded Music:				
Revenue	$775	$662	$2,924	$2,859
OIBDA	$67	$42	$380	$266

Depreciation and amortization	(40)	(40)	(165)	(181)
Impairment of goodwill and other intangible assets	-	-	-	(1,019)
Operating Income	$27	$2	$215	($934)
Music Publishing:				
Revenue	$137	$140	$607	$601
OIBDA	$42	$44	$141	$144
Depreciation and amortization	(15)	(13)	(59)	(70)
Operating Income	$27	$31	$82	$74
Total:				
Revenue	$905	$798	$3,502	$3,437
OIBDA	$77	$62	$322	$333
Depreciation and amortization	(58)	(59)	(238)	(268)
Impairment of goodwill and other intangible assets	-	-	-	(1,019)
Operating Income	$19	$3	$84	($954)

(a) - The twelve-month period ended September 30, 2004 is the combination of the five months ended February 29, 2004 of the predecessor company and the seven months ended September 30, 2004 of the successor company.

Supplemental Disclosures Regarding Non-GAAP Financial Information

OIBDA

We evaluate our operating performance based on several factors, including our primary financial

measure of operating income (loss) before non-cash depreciation of tangible assets, non-cash amortization of intangible assets and non-cash impairment charges to reduce the carrying value of goodwill and other intangible assets (which we refer to as OIBDA). We consider OIBDA to be an important indicator of the operational strengths and performance of our businesses, and believe the adjusted results help improve the ability to understand the company's operating performance and evaluate our performance in comparison to comparable periods. However, a limitation of the use of OIBDA as a performance measure is that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in our businesses. Accordingly, OIBDA should be considered in addition to, not as a substitute for, operating income (loss), net income (loss) and other measures of financial performance reported in accordance with accounting principles generally accepted in the U.S.

Figure 3. Warner Music Group Corp. - Reconciliation of OIBDA to Net Loss, Three Months and Twelve Months Ended 9/30/05 versus 9/30/04
(dollars in millions)

	Three Months Ended Sept 30, 2005	Three Months Ended Sept 30, 2004	Twelve Months Ended Sept 30, 2005	Twelve Months Ended Sept 30, 2004(a)
	(unaudited)	(unaudited)	(audited)	(unaudited)
OIBDA	$77	$62	$322	$333
Depreciation expense	(11)	(15)	(51)	(67)
Amortization expense	(47)	(44)	(187)	(201)
Impairment of goodwill and other intangible assets	-	-	-	(1,019)
Operating income (loss)	$19	$3	$84	($954)
Interest expense	(42)	(35)	(182)	(82)
Net investment-related gains (losses)	-	-	1	(9)
Equity in losses of equity-method investees	-	(2)	(1)	(13)
Deal-related transaction				

costs	-	-	-	(63)
Loss on repayment of Holdings Notes	-	-	(35)	-
Loss on repayment of bridge loan	-	-	-	(6)
Unrealized (loss) gain on warrants	-	(73)	17	(120)
Minority interest expense	-	(5)	(5)	(14)
Other income (expense), net	2	(4)	7	(11)
Loss before income taxes	($21)	($116)	($114)	($1,272)
Income tax expense	(9)	(21)	(55)	(150)
Net Loss	($30)	($137)	($169)	($1,422)

(a) - The twelve-month period ended September 30, 2004 is the combination of the five months ended February 29, 2004 of the predecessor company and the seven months ended September 30, 2004 of the successor company.

Adjusted Results

As previously disclosed, the current year contained a number of non-recurring charges that occurred concurrently with or in connection with our initial public offering. Such charges relate to specific IPO-related one-time events and do not reflect on-going operations of the business. In addition, the fourth quarter contained non-recurring charges in connection with our integration of the Lava label into the Atlantic Records Group and our settlement of the Spitzer investigation. The prior year also contained non-recurring items. Therefore, the company is also presenting results excluding these items and FAS 123 expenses. We consider these adjusted results to be an important indicator of the operational strengths and performance of our businesses, including the ability to provide cash flows to service debt. However, a limitation of the use of these adjusted amounts as performance measures is that they do not reflect the charges noted and, therefore, do not necessarily represent funds available for discretionary use, and are not necessarily measures of the company's ability to fund its cash needs. Accordingly, these adjusted amounts should be considered in addition to, not as a substitute for, operating income (loss), net income (loss), EPS and other measures of financial performance reported in accordance with accounting principles generally accepted in the U.S.

Figure 4. Warner Music Group Corp. - Reconciliation of GAAP Operating Income to Non-GAAP Adjusted OIBDA, Three Months and Twelve Months Ended 9/30/05 versus 9/30/04 (dollars in millions)

	Three Months Ended Sept 30, 2005	Three Months Ended Sept 30, 2004	Twelve Months Ended Sept 30, 2005	Twelve Months Ended Sept 30, 2004(a)
	(unaudited)	(unaudited)	(audited)	(unaudited)
Total WMG Operating Income (Loss) - GAAP	$19	$3	$84	($954)
Depreciation and amortization	58	59	238	268
Impairment of goodwill and intangible assets	-	-	-	1,019
Total WMG OIBDA	$77	$62	$322	$333
Non-recurring severance and other	24	-	24	-
Legal settlement	4	-	5	-
Restructuring costs	7	26	7	34
Loss on termination of management agreement	-	-	73	-
IPO-related cash bonus	-	-	10	-
Bonus related to stock awards	-	-	19	-
Management fees	-	3	6	6
Total WMG OIBDA Excluding Non-Recurring Charges	$112	$91	$466	$373
FAS 123 expense	7	1	25	1
Total WMG Adjusted OIBDA	$119	$92	$491	$374

Recorded Music Operating Income (Loss) - GAAP	$27	$2	$215	($934)
Depreciation and amortization	40	40	165	181
Impairment of goodwill and intangible assets	-	-	-	1,019
Recorded Music OIBDA	$67	$42	$380	$266
Non-recurring severance and other	24	-	24	-
Restructuring costs	7	17	7	24
IPO-related cash bonus	-	-	8	-
Bonus related to stock awards	-	-	12	-
Recorded Music OIBDA Excluding Non-Recurring Charges	$98	$59	$431	$290
FAS 123 expense	5	1	17	1
Recorded Music Adjusted OIBDA	$103	$60	$448	$291
Music Publishing Operating Income (Loss) - GAAP	$27	$31	$82	$74
Depreciation and amortization	15	13	59	70
Music Publishing OIBDA	$42	$44	$141	$144
Restructuring costs	-	1	-	1
IPO-related cash bonus	-	-	1	-
Music Publishing OIBDA Excluding Non-Recurring Charges	$42	$45	$142	$145
FAS 123 expense	1	-	3	-

Music Publishing Adjusted OIBDA	$43	$45	$145	$145

(a) - The twelve-month period ended September 30, 2004 is the combination of the five months ended February 29, 2004 of the predecessor company and the seven months ended September 30, 2004 of the successor company.

Figure 5. Warner Music Group Corp. - Reconciliation of GAAP Operating Income to Non-GAAP Operating Income, Three Months and Twelve Months Ended 9/30/05 versus 9/30/04 (dollars in millions)

	Three Months Ended Sept 30, 2005	Three Months Ended Sept 30, 2004	Twelve Months Ended Sept 30, 2005	Twelve Months Ended Sept 30, 2004(a)
	(unaudited)	(unaudited)	(audited)	(unaudited)
Total WMG Operating Income (Loss) - GAAP	$19	$3	$84	($954)
Non-recurring severance and other	24	-	24	-
Legal settlement	4	-	5	-
Restructuring costs	7	26	7	34
Loss on termination of management agreement	-	-	73	-
IPO-related cash bonus	-	-	10	-
Impairment of goodwill and intangible assets	-	-	-	1,019
Bonus related to stock awards	-	-	19	-
Management fees	-	3	6	6
Total WMG Operating Income Excluding Non-Recurring Charges	$54	$32	$228	$105

FAS 123 expense	7	1	25	1
Total WMG Adjusted Operating Income	$61	$33	$253	$106
Recorded Music Operating Income (Loss) - GAAP	$27	$2	$215	($934)
Non-recurring severance and other	24	-	24	-
Restructuring Costs	7	17	7	24
Impairment of goodwill and intangible assets	-	-	-	1,019
IPO-related cash bonus	-	-	8	-
Bonus related to stock awards	-	-	12	-
Recorded Music Operating Income Excluding Non-Recurring Charges	$58	$19	$266	$109
FAS 123 expense	5	1	17	1
Recorded Music Adjusted Operating Income	$63	$20	$283	$110
Music Publishing Operating Income - GAAP	$27	$31	$82	$74
Restructuring Costs	-	1	-	1
IPO-related cash bonus	-	-	1	-
Music Publishing Operating Income Excluding Non-Recurring Charges	$27	$32	$83	$75
FAS 123 expense	1	-	3	-
Music Publishing Adjusted				

Operating Income	$28	$32	$86	$75

(a) - The twelve-month period ended September 30, 2004 is the combination of the five months ended February 29, 2004 of the predecessor company and the seven months ended September 30, 2004 of the successor company.

Figure 6. Warner Music Group Corp. - Reconciliation of GAAP to Non-GAAP Adjusted Net Income and Adjusted Earnings Per Share, Three Months and Twelve Months Ended 9/30/05 versus 9/30/04
(dollars in millions except per share amounts)

	Three Months Ended Sept 30, 2005	Three Months Ended Sept 30, 2004	Twelve Months Ended Sept 30, 2005	Twelve Months Ended Sept 30, 2004(a)
	(unaudited)	(unaudited)	(audited)	(unaudited)
Net Income:				
Net loss - GAAP	($30)	($137)	($169)	($1,422)
Impairment of goodwill and intangible assets	-	-	-	1,019
Restructuring costs	7	26	7	34
Loss on termination of management fee	-	-	73	-
Loss on repayment of debt	-	-	35	6
IPO-related cash bonus	-	-	10	-
Bonus related to stock awards	-	-	19	-
Management fees	-	3	6	6
Non-recurring severance and other	24	-	24	-
Deal-related and other transaction costs	-	-	-	63
Legal Settlement	4	-	5	-
Tax effect on non-recurring items	-	(2)	(3)	(2)

Net income (loss) - Excluding Non-Recurring Charges	$5	($110)	$7	($296)
FAS 123 expense	7	1	25	1
Net income (loss) - Adjusted	$12	($109)	$32	($295)
Earnings Per Share:				
EPS - GAAP	($0.21)	($1.27)	($1.40)	
Impairment of goodwill and intangible assets	-	-	-	
Restructuring costs	0.05	0.24	0.06	
Loss on termination of management fee	-	-	0.60	
Loss on repayment of debt	-	-	0.29	
IPO-related cash bonus	-	-	0.08	
Bonus related to stock awards	-	-	0.16	
Management fees	-	0.03	0.05	
Non-recurring severance and other	0.17	-	0.20	
Legal Settlement	0.03	-	0.04	
Tax effect on non-recurring items	-	(0.02)	(0.02)	
EPS - Excluding Non-Recurring Charges	$0.04	($1.02)	$0.06	
FAS 123 expense	0.05	0.01	0.21	
EPS - Adjusted (b) (c)	$0.08	($1.01)	$0.26	

(a) - The twelve-month period ended September 30, 2004 is the combination of the five months ended February 29, 2004 of the predecessor company and the seven months ended September 30, 2004 of the successor company.
(b) - Totals may not add due to rounding.

(c) - Adjusted earnings per share on a fully diluted basis for the three months ended September 30, 2005, the three months ended September 30, 2004, and the twelve months ended September 30, 2005 were $0.08, ($1.01) and $0.25, respectively.

Free Cash Flow

Free cash flow reflects our cash flow provided by operating activities less capital expenditures and cash paid or received for investments. We use free cash flow, among other measures, to evaluate our operating performance. Management believes free cash flow provides investors with an important perspective on the cash available to service debt, make strategic acquisitions and investments, fund ongoing operations and working capital needs and pay ongoing regular quarterly dividends. As a result, free cash flow is a significant measure of our ability to generate long-term value. It is useful for investors to know whether this ability is being enhanced or degraded as a result of our operating performance. We believe the presentation of free cash flow is relevant and useful for investors because it allows investors to view performance in a manner similar to the method used by management. In addition, free cash flow is also a primary measure used externally by our investors and analysts for purposes of valuation and comparing the operating performance of our company to other companies in our industry.

As free cash flow is not a measure of performance calculated in accordance with GAAP, free cash flow should not be considered in isolation of, or as a substitute for, net income (loss) as an indicator of operating performance or cash flow provided by operating activities as a measure of liquidity. Free cash flow, as we calculate it, may not be comparable to similarly titled measures employed by other companies. In addition, free cash flow does not necessarily represent funds available for discretionary use and is not necessarily a measure of our ability to fund our cash needs. As free cash flow deducts capital expenditures and cash paid or received for investments from cash flow provided by operating activities, the most directly comparable GAAP financial measure, users of this information should consider the types of events and transactions that are not reflected. We provide below a reconciliation of free cash flow to the most directly comparable amount reported under GAAP, cash flow provided by operating activities.

Free cash flow includes cash paid for interest and certain non-recurring payments related to our IPO. We also review our cash flow adjusted for these items, a measure we call unlevered after-tax cash flow excluding certain non-recurring IPO related items. Management believes this measure provides investors with an additional important perspective on our cash generation ability. We consider

unlevered after-tax cash flow excluding certain non-recurring IPO related items to be an important indicator of the performance of our businesses and believe the presentation is relevant and useful for investors because it allows investors to view performance in a manner similar to the method used by management. A limitation of the use of this measure is that it does not reflect the charges noted and, therefore, does not necessarily represent funds available for discretionary use, and is not necessarily a measure of the company's ability to fund its cash needs. Accordingly, this measure should be considered in addition to, not as a substitute for, net cash flow provided by operating activities and other measures of liquidity reported in accordance with accounting principles generally accepted in the U.S.

Figure 7. Warner Music Group Corp. - Calculation of Non-GAAP Free Cash Flow, Three Months and Twelve Months Ended 9/30/05 versus 9/30/04 (dollars in millions)

	Three Months Ended Sept 30, 2005	Three Months Ended Sept 30, 2004	Twelve Months Ended Sept 30, 2005	Twelve Months Ended Sept 30, 2004(a)
	(unaudited)	(unaudited)	(audited)	(unaudited)
Net cash flow provided by operating activities	$33	$49	$205	$438
Less: Capital expenditures	10	10	30	39
Less: Cash paid (received) for investments	(10)	5	24	(31)
Free cash flow (b)	$33	$34	$151	$430

(a) - The twelve-month period ended September 30, 2004 is the combination of the five months ended February 29, 2004 of the predecessor company and the seven months ended September 30, 2004 of the successor company.
(b) - Free cash flow includes cash paid for interest and certain non-recurring cash payments as follows (in millions):

	Three Months	Three Months	Twelve Months	Twelve Months

	Ended Sept 30, 2005	Ended Sept 30, 2004	Ended Sept 30, 2005	Ended Sept 30, 2004
Free cash flow	$33	$34	$151	$430
Plus: Cash paid for interest	22	39	151	63
Plus: Cash paid to terminate management agreement	-	-	73	-
Plus: IPO-related cash bonus	-	-	10	-
Plus: Cash bonus related to stock awards	-	-	19	-
Plus: Cash paid for management fees	-	3	6	6
Unlevered after-tax cash non-recurring IPO-related items	$55	$76	$410	$499

Figure 8. Warner Music Group Corp. - Consolidated Balance Sheets as of 9/30/05 and 9/30/04 (dollars in millions)

	Sept 30, 2005	Sept 30, 2004
	(audited)	(audited)
Assets:		
Current Assets		
Cash & cash equivalents	$ 288	$ 555
Accounts receivable, less allowances of $218 and $222	637	571
Inventories	52	65
Royalty advances (to be recouped w/in 1 year)	190	223
Deferred tax assets	36	38
Other current assets	39	86

Total Current Assets	$ 1,242	$ 1,538
Royalty advances (to be recouped after 1 year)	190	223
Investments (a)	21	8
Property, plant & equipment, net	157	189
Goodwill	869	978
Intangible assets subject to amortization, net	1,815	1,937
Intangible assets not subject to amortization	100	100
Other assets	104	117
Total Assets	$ 4,498	$ 5,090
Liabilities & Shareholders' Equity:		
Current Liabilities		
Accounts payable	$ 247	$ 226
Accrued royalties	1,057	1,003
Taxes & other withholdings	23	10
Current portion of long-term debt	17	12
Note payable to shareholders	-	342
Other current liabilities	404	587
Total current liabilities	$ 1,748	$ 2,180
Long-term debt	2,229	1,828
Dividends payable	5	-
Deferred tax liabilities, net	201	265
Other noncurrent liabilities	226	333
Minority interest in preferred stock of subsidiary	-	204
Total Liabilities	$ 4,409	$ 4,810
Common stock	-	-
Additional paid-in capital	548	512
Retained earnings (deficit)	(480)	(238)
Accumulated other comprehensive income (loss)	21	6
Total Shareholders' Equity	$ 89	$ 280
Total Liabilities & Shareholders' Equity	$ 4,498	$ 5,090

Figure 9. Warner Music Group Corp. - Summarized Statement of Cash Flows, Three Months and Twelve Months Ended 9/30/05 versus 9/30/04
(dollars in millions)

	Three Months Ended Sept 30, 2005	Three Months Ended Sept 30, 2004	Twelve Months Ended Sept 30, 2005	Twelve Months Ended Sept 30, 2004(a)
	(unaudited)	(unaudited)	(audited)	(unaudited)
Net cash provided by operating activities	$ 33	$ 49	$ 205	$ 438
Net cash provided by (used in) investing activities	-	(15)	(54)	(2,646)
Net cash provided by (used in) financing activities	(9)	(8)	(416)	2,679
Effect of foreign currency exchange rates on cash	(1)	1	(2)	3
Net increase (decrease) in cash	$ 23	$ 27	$ (267)	$ 474

(a) - The twelve-month period ended September 30, 2004 is the combination of the five months ended February 29, 2004 of the predecessor company and the seven months ended September 30, 2004 of the successor company.

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EXHIBIT CO 0951

July 27, 2006

Entertainment

WMG

$25.21

12-Month Target:
$25.00

Total Return To Target:
1.2%

Neutral

Market Cap.	Volatility
$3,794.1 MM	High

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Warner Music Group Corp

EMI/WMG Merger Shelved; Reducing PT to $25 from $26.50

- **We are lowering our price target to $25 from $26.50,** reflecting today's announcements that EMI and Warner are longer pursuing bids for each other. We expect WMG shares to trade down towards their fundamental value, which we estimate to be $25.
- **Not surprisingly, both EMI and Warner Music announced they are dropping their respective bids.** Both companies cited the recent ruling by the E.U. Court of First Instance that the Sony/BMG merger may have violated anti-trust laws as the cause. EMI and Warner left the door open for future M&A.
- **We do not view Warner's decision to drop its bid for EMI as a negative.** In our view, WMG may be better served on its own, at least near term. We were never completely convinced that the potential maximum estimated synergies were achievable and do not believe Warner needed to do a deal to remain competitive.
- **Warner can now again focus on its operations, which continue to outperform expectations.** For FY3Q06, we estimate revenue of $794.3M, OIBDA of $82.0M, and EPS of ($0.16). This compares to Street consensus of $784M, $78M, and ($0.19), respectively. Given the recent *Red Hot Chili Peppers* and *Madonna* releases and continued digital momentum, we believe both ours and Street estimates could prove conservative.
- **Valuation and Target Price Analysis:** Our valuation is based on the combination of a DCF and a discounted P/FCF.
- **PORTFOLIO MANAGERS' SUMMARY:** Page 3.

Changes at a glance

(Please see page 2 for additional detail)

Rating?		Target Price?	
No	◄►	Yes	▼
Maintain Neutral		$26.50 to $25.00	

Revenue (MM)			Prev	Curr	
FY05	*		–	$3,488.0	
FY06E	*		–	$3,600.0	

EPS**			Prev	Curr	P/E
FY05	No	◄►	–	$0.16	N/M
FY06E	No	◄►	–	$0.29	86.9
FY07E	*		–		

* No Previous Values

▲ = Up; ▼ = Down; ◄► = No Change. ** These estimates adjusted to account for FAS 123r, Expensing of Employee Stock Options.

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Warner Music Group Corp

Company Data	
52-Week Range	$31-15
Market Capitalization (MM)	$3,794.1
Shares Outstanding (MM)	150.5
Float (MM)	34.4
Short Interest	1.2%
Average Daily Volume	665,182
Dividend/Yield	$0.52/2.1%
03/05 ROE/ROIC	0%/0%
Exchange-Traded Funds	
Convertibles	NO
Proj. 3-Yr EPS Growth Rate	
–	

Balance Sheet (03/05)	
Net Cash/Share	$1.85
Book Value/Share	
Price/Book Value	
Debt/Cap.	None

Estimates (FYE Sep)	2005A	2006E Prev	2006E Curr	2007E Prev	2007E Curr
EPS*					
1Q (Dec)	$0.31	–	$0.46A	–	
2Q (Mar)	(0.28)	–	(0.05)A	–	
3Q (Jun)	(0.27)	–	(0.16)E	–	
4Q (Sep)	0.08	–	0.03E	–	
Fiscal Year	**$0.16**	–	**$0.29**	–	
First Call Mean			$0.24		$0.40
Calendar Year	**$0.30**	–	**$0.25**	–	
P/E	84.0		N/M		
Revenue (MM)					
1Q (Dec)	$1,073.9	–	$1,027.4A	–	
2Q (Mar)	767.1	–	795.7A	–	
3Q (Jun)	742.0	–	794.3E	–	
4Q (Sep)	905.0	–	982.6E	–	
Fiscal Year	**$3,488.0**	–	**$3,600.0**	–	
First Call Mean			$3,537.8		$3,665.7

* These estimates adjusted to account for FAS 123r, Expensing of Employee Stock Options. First Call Mean estimates might not have been similarly adjusted.

Top Picks

The News Corporation Limited
(NWS.A, $18.99, B, $24.00 Target)

Least Favorites

NONE

Company Description

- Warner Music Group is a leading music content company with a roster of over 38,000 artists. WMG has two businesses: 1) Recorded Music, which sells and markets recorded music in physical and digital formats and 2) Music Publishing, which receives royalties from the rights to music compositions. In calendar 2005, WMG had a roughly 15% share of the domestic recorded market.

Sector View

- Our sector view is overweight. Despite repeated confirmations of slowing secular growth, visibility is growing of better capital allocation and asset rationalization.

Portfolio Managers' Summary

- **Our 12-month thesis on the stock.** We believe that WMG offers an attractive LT opportunity in the small- / mid-cap media sector for two reasons: 1) we expect growth in digital music sales to offset declining physical sales and 2) even under difficult industry conditions, we believe that Warner has the ability to generate stable FCF.
- **Our call today in a nutshell.** We are lowering our price target to $25 from $26.50, reflecting today's announcements that EMI and Warner are longer pursuing bids for each other. We expect WMG shares to trade down towards their fundamental value, which we estimate to be $25.
- **Upcoming catalysts.** Now that a deal with EMI is shelved indefinitely, we believe the focus for WMG returns to operations. Upcoming catalysts include further data points that show digital music is performing well and upcoming album releases from Warner's artist roster.
- **12-month valuation.** Our Price Target of $25.00 reflects our estimated fair value of WMG on a standalone basis. To determine our price target, we employed the average of a discounted cash flow (DCF), using a weighted average cost of capital (WACC) of 10%, FCF growth in perpetuity of 3.0% and a discounted price to free cash flow (P/FCF) analysis, which applies a multiple of 12x to estimated 2008, 2009, and 2010 FCF, respectively.
- **Risks to our call.** Although unlikely, the door is still open for WMG and EMI to pursue further M&A activity.

Investment Considerations

We are lowering our price target to $25 from $26.50, reflecting today's announcements that EMI and Warner are longer pursuing bids for each other. We expect WMG shares to trade down towards their fundamental value, which we estimate to be $25.

Not surprisingly, both EMI and Warner Music announced they are dropping their respective bids for each other. Both companies cited the recent E.U. Court of First Instance's decision to annul the validity of the European Commission's original decision to approve the Sony/BMG joint venture as the cause. As expected, both EMI and Warner left the door open for future M&A plans.

We do not view Warner's decision to drop its bid for EMI as a negative. Recall that we recently wrote that we believe that WMG may be better served, at least near term, on its own (see *WMG: M&A Musical Chairs?*, dated July 13, 2006). We have never been convinced that a deal over the near-term was "necessary" and we've questioned the maximum estimated synergies from a deal, which some speculated could be as much as $400 million per year. While we believe a deal between the two companies does contain meaningful synergies and makes sense longer term, there were numerous near-term risks. For example, the negotiating process was and would likely continue to be acrimonious, the antitrust review process would clearly be very lengthy, and there's the risk that the management teams could lose operational focus. Also, given Warner's private equity sponsorship and their willingness to be sellers at a lower valuation, we believed Warner's bid for EMI seemed somewhat counterintuitive.

We think the likelihood of the Sony/BMG deal being reversed is low, but at this stage it may not even matter for EMI and Warner. It will be difficult to prove that anyone other than Sony and BMG has been harmed from the merger. Obviously, the focus will be on the antitrust merits of the deal, not the market impact since it was first approved. However, we think it will be hard to ignore the latter. Also, from a political perspective, a reversal of the deal would have wide-reaching negative implications for business throughout the E.U. Although Sony/BMG may continue to operate in its current form and no further regulatory action is pursued, we believe the current regulatory environment proved too difficult for EMI and Warner.

Warner can now again focus on its operations, which continue to outperform expectations. For FY3Q06, we estimate revenue of $794.3 million, OIBDA of $82.0 million, and an EPS loss of $0.16. This compares to Street consensus of $784 million, $78 million, and a loss of $0.19, respectively. Given the recent *Red Hot Chili Peppers* and *Madonna* releases and continued digital momentum, we believe both ours and Street estimates could prove conservative. Warner will report FY3Q06 results on August 3 at 10 a.m. ET. The dial-in number is 800-857-2625 and the passcode is "Warner Music."

Figure 1

Warner Music Group
DCF Analysis

	2004	2005	2006E	2007E	2008E	2009E	2010E	2011E	2012E
DCF Valuation									
EBITDA	$390	$323	$494	$538	$607	$676	$723	$770	$804
Growth	NA	-17.2%	52.7%	9.0%	12.7%	11.4%	7.0%	6.5%	4.4%
Less...									
Change in Working Capital	20.0	(1.3)	0.3	20.0	20.0	20.0	20.0	20.0	20.0
Less...									
Capital Expenditures (Capex + Advances)	68.0	80.9	88.3	94.8	101.1	107.9	115.1	122.8	131.0
Growth	NA	19.0%	9.1%	7.3%	6.7%	6.7%	6.7%	6.7%	6.7%
Less...									
Normalized Cash Taxes	30.2	55.0	47.4	56.5	63.7	70.9	75.9	80.9	84.4
Equals...									
Unlevered After-Tax Free Cash Flow	271.9	188.6	357.5	366.8	421.8	476.9	511.8	546.4	568.2
Growth	NA	-30.6%	89.5%	2.6%	15.0%	13.0%	7.3%	6.7%	4.0%
Terminal Value 2012(FCFt+1)/(WACC-g)			$0	$0	$0	$0	$0	$0	8,102.8
Imputed EBITDA Multiple									10.1x

Weighted Average Cost Of Capital	10.2%
Debt Proportion Of Financing	20.0%
After-Tax Cost Of Debt Financing	4.6%
Marginal Tax Rate	35%
Weighted Average Net Cost Of Funds	7.0%
Equity Proportion Of Financing	80.0%
Cost Of Equity Financing	11.6%
10 Year Treasury	5.1%
Market Risk Premium	5.5%
Beta	1.19

	2006E	2007E
NPV 5-Year Forward FCF Stream	$1,719	$1,877
NPV 2012 Forward Terminal Value	4,519	4,981
Total NPV	6,237.5	6,857.5
Less... Net Debt and Preferred	1,927	1,790
Plus... Off Balance Sheet Assets at PMV	76	10
Plus... Options Exercise	0	0
Equals...Private Equity Value	4,386.8	5,077.7
Less...25% Public Discount		
Target Public Equity Value	3,290	3,808
Target Eq. Value per Share (CY)	3,420	3,895
Target Public Equity Value per Share (CY)	$23	$26
Current Price	$25.21	
Potential Appreciation	-9%	3%

Sources: Company Reports, Banc of America Securities LLC estimates.

Figure 2

Warner Music Group
P/FCF Analysis

	2004	2005	2006E	2007E	2008E	2009E	2010E	2011E	2012E
EBITDA	$390	$323	$494	$538	$607	$676	$723	$770	$804
Less... Capex	68.0	80.9	88.3	94.8	101.1	107.9	115.1	122.8	131.0
Less... Cash Interest Expense	55.5	127.8	153.0	119.1	113.7	107.8	101.3	94.5	81.4
Less... Normalized Cash Taxes	30.2	55.0	47.4	58.5	63.7	70.9	75.9	80.9	84.4
Less... Preferred Dividends	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Less... Changes in Working Capital	20.0	(1.3)	0.3	20.0	20.0	20.0	20.0	20.0	20.0
Equals... Levered After-Tax Free Cash Flow	$216.4	$60.8	$204.5	$247.7	$308.1	$369.1	$410.5	$451.8	$488.7
FCF/Share		$0.41	$1.37	$1.68	$2.06	$2.47	$2.75	$3.02	$3.26
Note: Current P/FCF Multiple		62.0	18.4	15.2	12.2	10.2	9.2	8.3	7.7
Note: Forward 3-Year FCF CAGR		*72%*	*22%*	*18%*	*14%*	*10%*			

Times... Assumed P/FCF Multiple on Forward FCF		12.0x	12.0x	12.0x	
Equals...Firm Equity Value	$0	$4,429	$4,928	$5,422	$0
Divided By... Fully-Diluted Share Count	149.5				
Equals...Firm Equity Value/Share	$0.00	$29.63	$32.96	$36.28	$0.00

	2006E	2007E
NPV '08 Value	$23.78	$26.54
NPV '09 Value	$23.69	$26.45
NPV '10 Value	$23.35	$26.07
Average of '08-10 NPV	23.61	26.35
Equals... Equity Value (FY)	24.36	26.86
Equals... Equity Value (CY)	24.98	27.55
Equals... Price Target (CY)	$25	$28
Implied Multiple of Forward EBITDA	11.5x	11.2x
Current Price	$25.21	
Appreciation Potential	-1%	9%

Sources: Company Reports, Banc of America Securities LLC estimates.

2Q05	3Q05	4Q05	2005	1Q06	2Q06	3Q06E	4Q06E	2006E	2007E
121.1	$588.0	$775.2	$2,924.2	$920.0	$875.8	$844.0	$854.1	$3,093.8	$3,294.9
154.0	161.0	137.0	607.0	131.4	129.1	157.2	135.4	553.2	577.5
(8.0)	(7.0)	(7.2)	(43.2)	(24.0)	(9.0)	(7.0)	(7.0)	(47.0)	(48.2)
167.1	742.0	905.0	3,488.0	1,027.4	795.7	794.3	982.6	3,600.0	3,824.2
6.4%	3.5%	13.4%	2.7%	-4.3%	3.7%	7.0%	8.6%	3.2%	6.2%
124.0	108.5	183.9	583.1	168.6	137.0	132.9	184.2	622.7	659.6
132.0	246.3	256.2	1,065.2	315.7	213.2	243.5	273.7	1,046.1	1,080.3
45.8	44.5	52.9	183.7	40.2	33.9	40.5	48.0	168.6	188.5
17.8	17.0	23.0	78.8	23.0	21.9	20.3	26.6	91.9	95.1
(8.3)	(3.6)	(3.0)	(19.9)	(7.0)	(7.0)	(7.0)	(7.0)	(28.0)	(7.0)
111.5	412.6	485.0	1,881.3	528.5	405.0	430.3	525.5	1,889.3	2,023.5
155.6	329.4	420.0	1,506.8	498.9	390.8	364.0	457.1	1,710.7	1,800.7
56.3%	44.4%	46.4%	46.1%	48.6%	49.1%	45.8%	46.5%	47.5%	47.1%
				531.5	356.0	364.5	446.9		
17.3	14.2	27.4	84.9	23.5	21.0	17.7	34.2	96.4	95.5
89.3	82.3	105.8	397.6	123.0	98.8	92.9	135.8	450.3	467.9
20.4	19.9	21.6	82.9	21.8	21.8	21.8	23.8	88.9	93.2
33.6	31.9	33.2	130.7	32.6	35.7	35.4	35.6	139.4	145.9
96.9	93.8	98.9	378.2	93.4	100.0	97.0	102.1	392.6	407.7
23.5	124.7	62.0	250.2	10.0	22.0	25.0	25.0	82.0	84.5
(13.5)	(4.5)	(6.0)	(41.0)	(8.0)	(12.5)	(7.8)	(4.0)	(32.3)	(32.1)
167.5	362.3	342.7	1,283.5	296.1	286.9	282.0	352.2	1,217.1	1,262.7
72.0	47.0	103.0	417.0	205.8	81.1	72.0	98.2	457.0	513.3
47.3	28.1	43.0	142.2	24.0	46.8	35.1	31.7	137.6	152.4
119.3	75.1	146.0	559.2	229.8	127.9	107.0	129.9	594.6	665.7
		40%							
88.1	(33.0)	77.3	323.2	202.8	103.9	82.0	104.9	493.8	538.1
5.9%	-142.5%	-16.2%	-17.2%	6.3%	17.9%	NA	35.8%	52.7%	9.0%
1.5%	-4.4%	8.5%	9.3%	19.7%	13.1%	10.3%	10.7%	13.7%	14.1%
14.0	12.0	11.0	51.0	11.0	11.0	13.4	13.4	48.8	50.3
47.0	47.0	47.0	187.0	47.0	48.0	54.5	54.5	204.0	204.0
127.1	($92.0)	$19.3	$85.2	$144.8	$44.9	$14.1	$37.0	$240.8	$283.8
0.7%	-668.2%	-39.6%	-39.9%	10.6%	65.8%	-115.4%	92.0%	182.5%	17.9%
3.5%	-12.4%	2.1%	2.4%	14.1%	5.6%	1.6%	3.8%	6.7%	7.4%
52.0	50.0	42.0	182.0	45.0	45.0	33.0	30.0	153.0	119.1
(39.0)	33.0	(2.0)	16.0	-	(3.0)	-	-	-	-
-	-	-	-	-	-	-	-	-	-
13.0	83.0	40.0	198.0	45.0	42.0	33.0	30.0	153.0	119.1
14.1	(178.0)	(20.7)	(112.8)	99.8	2.9	(18.9)	7.0	90.8	164.7
10.0	4.0	9.0	55.0	$30.0	$10.0	$5.0	$2.4	47.4	157.7
71%	-2%	-43%	-43%	30%	NA	NA	35%	52%	35%
4.1	(179.0)	(29.7)	(167.8)	69.8	(7.1)	(23.9)	4.5	43.3	107.1
$0.04	($1.41)	($0.21)	($1.24)	$0.49	($0.05)	($0.17)	$0.03	$0.31	$0.76
NA	NA	NA	NM	NA	NA	NA	NA	-124.8%	145.5%
($0.28)	($0.27)	$0.08	($0.15)	$0.46	($0.05)	($0.16)	$0.03	$0.29	$0.71
NA	NA	NA	NA	45.1%	NM	NM	NM	NA	NA
107.7	127.0	141.2	120.9	141.2	141.9	141.9	141.9	141.7	141.7
123.5				150.5	150.5	150.5	150.5	150.5	150.5

nates.

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Volatility		Ratings		
		Buy	Neutral	Sell
Low	0%-25%	11%+	10.9%-0.1%	0% or worse
Medium	25%-35%	15%+	14.9%-(2.9)%	(3)% or worse
High	35%-55%	20%+	19.9%-(6.9)%	(7)% or worse
Extreme	55%+	32%+	31.9%-(14.9)%	(15)% or worse

Source for volatility: Bloomberg.

Rating Distribution*

Global Coverage

Coverage Universe	Companies	Pct.	Investment Banking Clients	Companies	Pct.**
Buy	357	43	Buy	278	78
Hold	447	53	Hold	353	79
Sell	33	4	Sell	26	79

Media/Telecom Services Sector

Coverage Universe	Companies	Pct.	Investment Banking Clients	Companies	Pct.**
Buy	24	46	Buy	17	71
Hold	28	54	Hold	20	71
Sell	0	0	Sell	0	0

* For the purposes of this Rating Distribution, "Hold" is equivalent to our "Neutral" rating.
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Warner Music Group Corp (WMG)

Target Price, Valuation Method, Risk Factors

Target Price:	$25.00
Valuation Method Used To Reach Target Price:	Our Price Target of $25.00 reflects our estimated fair value of WMG on a standalone basis. To determine our price target, we employed the average of a discounted cash flow (DCF), using a weighted average cost of capital (WACC) of 10%, FCF growth in perpetuity of 3.0% and a discounted price to free cash flow (P/FCF) analysis, which applies a multiple of 12x to estimated 2008, 2009, and 2010 FCF, respectively.

Risk Factors:

1. Greater than expected decrease in physical sales
2. Music is a hit-driven business
3. Digital piracy is greater than expected

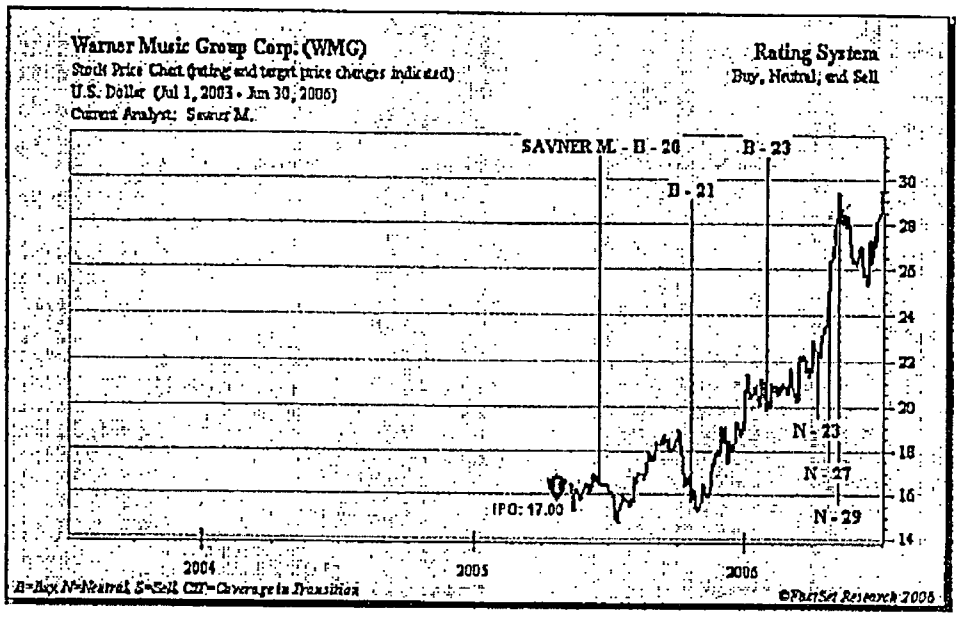
The News Corporation Limited (NWS.A)

Target Price, Valuation Method, Risk Factors

Target Price:	$24.00
Valuation Method Used To Reach Target Price:	Our price target is based on a combination of DCF, using a WACC of 9.3% and 5% FCF growth in perpetuity, and P/FCF, based on the average discounted value of applying a projected 20x FCF multiple in 2007, 2008 and 2009.

Risk Factors:

1. Exposure to advertising market weakness.
2. Volatility of film business.
3. Succession plans and potential departure of senior management.
4. Volatility of early-stage businesses.
5. Acquisition risk.


Warner Music Group Corp. (WMG)
Stock Price Chart (rating and target price changes indicated)
U.S. Dollar (Jul 1, 2003 - Jun 30, 2006)
Current Analyst: Savner M.
Rating System
Buy, Neutral, and Sell
SAVNER M. - B - 20
B - 21
B - 23
N - 23
N - 27
N - 29
IPO: 17.00
30
28
26
24
22
20
18
16
14
2004
2005
2006
B=Buy, N=Neutral, S=Sell, CIT=Coverage in Transition
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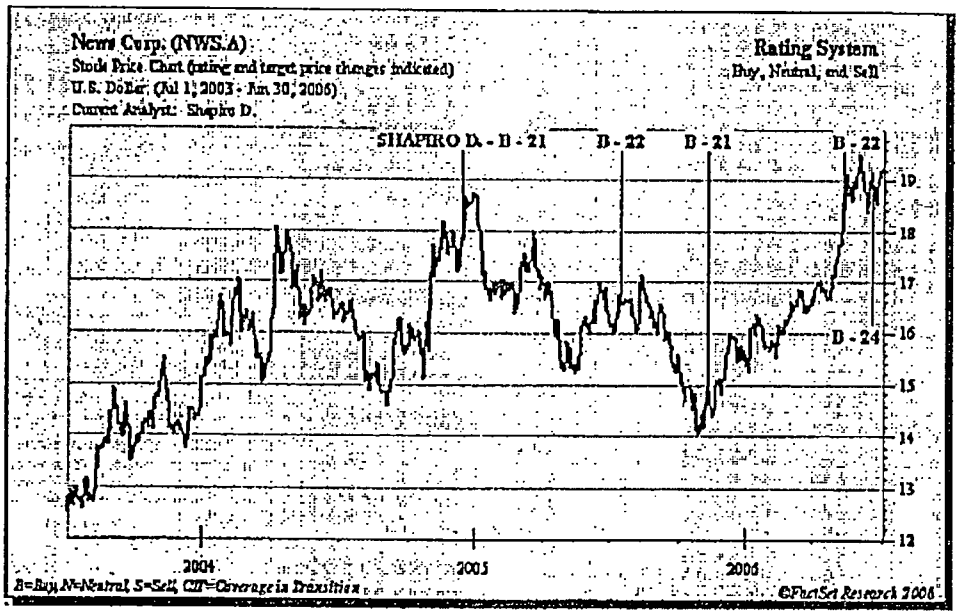
News Corp. (NWS.A)
Stock Price Chart (rating and target price changes indicated)
U.S. Dollar (Jul 1, 2003 - Jun 30, 2006)
Current Analyst: Shapiro D.
Rating System
Buy, Neutral, and Sell
SHAPIRO D. - B - 21
B - 22
B - 21
B - 22
B - 24
19
18
17
16
15
14
13
12
2004
2005
2006
B=Buy, N=Neutral, S=Sell, CIT=Coverage in Transition
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Bank of America.

EXHIBIT CO 0952

EQUITY RESEARCH
United States

Bank of America

April 6, 2006

Entertainment

WMG

$22.79

12-Month Target:
$23.00

Total Return To Target:
3.3%

Market Cap.	Volatility
$3,429.9 MM	High

Michael L. Savner, CFA
212.847.5678
msavner@bofasecurities.com

Changes at a glance

(Please see page 2 for additional detail)

Rating?	Target Price?
Yes	No
Buy to Neutral	Maintain $23.00 Target

Revenue (MM)			Prev	Curr	
FY05	*		–	$3,502.3	
FY06E	*		–	$3,542.2	

EPS**			Prev	Curr	P/E
FY05	No		–	$0.16	N/M
FY06E	No		–	$0.19	N/M
FY07E	*		–		

* No Previous Values

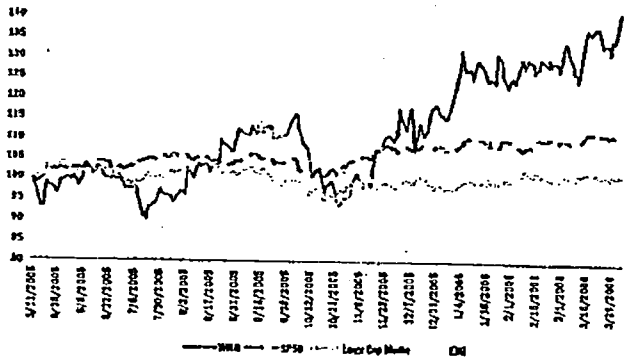
– Up; – Down – No Change. ** These estimates adjusted to account for FAS 123r, Expensing of Employee Stock Options.

Warner Music Group Corp

Downgrading to Neutral; Maintaining Price Target and Positive Bias

- **We are downgrading shares of Warner Music Group to Neutral from Buy based on valuation.** We maintain our $23 price target and our positive long term bias on the stock.
- **WMG shares are up 34% since the IPO in May 2005 and 55% from their low in July 2005.** The S&P 500 is up approximately 11.5% since the IPO. We calculate WMG is trading at 11.2x 2006E EBITDA and 16.6x FCF, a slight premium to traditional media companies based on EBITDA and generally in line based on FCF.
- **We believe that WMG shares partly reflect takeover expectations.** Warner has long been considered a merger partner for EMI Group. While we do not think a deal is imminent, if Warner is the acquired company we would not expect material upside from current levels.
- **We would get more constructive on Warner if there was:** 1) a pullback in valuation, 2) faster and more profitable-than-expected digital growth, or 3) evidence that a deal with EMI is imminent.
- **Separately, we recently hosted investor meetings with management** and came away with more conviction that Warner is executing its digital strategy significantly better than its peers.
- **Why not increase our price target?** 1) We have increased our target 15% in the past five months, 2) we believe a buyout much above $26 is unlikely, 3) a potential secondary offering could limit the shares, and 4) competitive pressures related to physical sales and piracy still persist.
- **Valuation and Target Price Analysis:** Our valuation is based on the combination of DCF and discounted P/FCF.
- PORTFOLIO MANAGERS' SUMMARY: Page 3.

Figure 1: WMG Shares Are Up 34% Since the IPO on May 11, 2005



Source: FactSet

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Warner Music Group Corp

Company Data	
52-Week Range	$23-15
Market Capitalization (MM)	$3,429.9
Shares Outstanding (MM)	150.5
Float (MM)	31.1
Short Interest	5.6%
Average Daily Volume	306,335
Dividend/Yield	$0.54/2.4%
03/05 ROE/ROIC	0%/0%
Exchange-Traded Funds	
Convertibles	NO
Proj. 3-Yr EPS Growth Rate	

Balance Sheet (03/05)	
Net Cash/Share	$1.85
Book Value/Share	
Price/Book Value	
Debt/Cap.	None

Estimates (FYE Sep)	2005A	2006E Prev	2006E Curr	2007E Prev	2007E Curr
EPS*					
1Q (Dec)	$0.31	–	$0.46A	–	
2Q (Mar)	0.03	–	(0.15)E	–	
3Q (Jun)	(0.27)	–	(0.15)E	–	
4Q (Sep)	0.08	–	0.03E	–	
Fiscal Year	$0.16	–	$0.19	–	
First Call Mean			$0.06		$0.16
Calendar Year	$0.30	–	$0.25	–	
P/E	76.0		91.2		
–					
Revenue (MM)					
1Q (Dec)	$1,088.0	–	$1,044.3A	–	
2Q (Mar)	766.8	–	743.4E	–	
3Q (Jun)	742.0	–	788.2E	–	
4Q (Sep)	905.0	–	966.4E	–	
Fiscal Year	$3,502.3	–	$3,542.2	–	
First Call Mean			$3,470.0		$3,541.7

* These estimates adjusted to account for FAS 123r, Expensing of Employee Stock Options. First Call Mean estimates might not have been similarly adjusted.

Top Picks
The News Corporation Limited
(NWS.A, $16.69, B, $21.00 Target)

Least Favorites
Pixar Animation Studios
(PIXR, $65.66, N, $64.00 Target)

Company Description

- Warner Music Group is a leading music content company with a roster of over 38,000 artists. WMG has two businesses: 1) Recorded Music, which sells and markets recorded music in physical and digital formats and 2) Music Publishing, which receives royalties from the rights to music compositions. In calendar 2005, WMG had a roughly 15% share of the domestic recorded market.

Sector View

- Our sector view is overweight. Despite repeated confirmations of slowing secular growth, visibility is growing of better capital allocation and asset rationalization.

Michael L. Savitz, CFA 212.847.5678
Michael L. Savitz, CFA 212.847.5678

Portfolio Managers' Summary

- **Our 12-month thesis on the stock.** We still believe that WMG offers an attractive LT opportunity in the small / mid-cap media sector for three reasons: 1) we expect growth in digital music sales to offset declining physical sales; 2) even under difficult industry conditions, we believe that Warner has the ability to generate stable FCF; and 3) the company's underlying fundamentals are better than its valuation reflects.
- **Our call today in a nutshell.** We are downgrading shares of Warner Music Group to Neutral from Buy based on valuation. We are maintaining our $23 price target and our positive long term bias on the stock. We believe that WMG shares partly reflect takeover expectations. Warner has long been considered a merger partner for EMI Group. While we do not think a deal is imminent, if Warner is the acquired company, we do not expect the deal to be worth much more than $26 per WMG share.
- **Upcoming catalysts.** Upcoming catalysts include increased digital sales channels and potential M&A activity in the sector.
- **12-month valuation.** To determine our price target of $23, we employed the average of a discounted cash flow (DCF), using a weighted average cost of capital (WACC) of 9.0%, FCF growth in perpetuity of 3.0% and a discounted price to free cash flow (P/FCF) analysis, which applies a multiple of 15x to estimated 2007, 2008, and 2009 FCF, respectively.
- **Risks to our call.** We could get more constructive of WMG shares if there was: 1) a pullback in valuation, 2) faster and more profitable-than-expected digital growth, or 3) evidence that a deal with EMI were imminent.

Investment Overview

We are downgrading WMG shares based on valuation.

We are downgrading shares of Warner Music Group to Neutral from Buy based on valuation. We maintain our $23 price target and our positive long term bias on the stock.

WMG has outperformed the S&P and its peers since the IPO in May 2005.

Shares of Warner Music Group have increased 34% since the company's IPO on May 11, 2005 and 55% from their low in July 2005. The S&P 500 is up approximately 11.5% since Warner's IPO. We calculate WMG is currently trading at 11.2x 2006E EBITDA and 16.6 FCF, which represents a slight premium relative to other media companies on an EV/EBITDA basis and is essentially in line based on P/FCF multiples.

At its current price, we believe the market expects a merger with EMI.

Although Warner has been executing above our expectations since its IPO, we believe that its current valuation partly reflects takeover expectations. Warner has long been considered a merger partner for EMI Group, and while we do not think a deal is necessarily imminent, if Warner is the acquired company, based on our analysis we do not expect the deal to value WMG shares much above $26. Further, if a deal with EMI is not reached, we believe that Warner's private equity investors, who still hold about 70% of Warner shares, would consider a secondary offering. Warner Music Group CEO Edgar Bronfman has said that he believes WMG shares would benefit from greater float.

We would get more constructive on Warner Music shares if there was: 1) a pullback in valuation, 2) faster and more profitable-than-expected digital growth, or 3) evidence that a deal with EMI were imminent.

Separately, a few weeks ago we hosted investor meetings with Warner management and came away with more conviction that the company is executing its digital strategy significantly better than its peers. We also believe that operational momentum would likely be more sustainable if Warner did not attempt a merger near term.

The story is somewhat binary. If a deal with EMI is reached, it could provide another 10-20% upside in the stock. If a deal with EMI is not reached, WMG shares could pull back 10-15%.

A fair question is why don't we simply increase our price target if we remain positive on the story? That's easier said than done. We have increased our target price by 15% in the past five months, which we believe reflects the better-than-expected financial performance and more aggressive digital growth assumptions. Also, as we show in this report, we do not believe a deal would value WMG shares much higher than $26 per share. Lastly, with WMG shares now within the original IPO range of $22-$24 its private equity investors may consider a secondary offering if a deal with EMI does not materialize, given that they still own 70% of the company and management has expressed interest in increasing the float. As a result, we think the near term story is somewhat binary. If a deal with EMI is reached, it could provide another 10-20% upside in the stock. If a deal with EMI is not reached (or the market losses confidence that a deal will be reached), WMG shares could pull back 10-15%.

To determine our price target of $23, we employed the average of a discounted cash flow (DCF), using a weighted average cost of capital (WACC) of 9.0%, FCF growth in perpetuity of 3.0% and a discounted price to free cash flow (P/FCF) analysis, which applies a multiple of 15x to estimated 2007, 2008, and 2009 FCF, respectively.

WMG Shares Appear Near Fair Value

Warner Music Group went public on May 11, 2005 at $17 per share. The company originally proposed pricing the shares between $22 - $23. Since the IPO, WMG shares have increased 34% and have increased 55% from their low in July 2005. The S&P 500 is up approximately 11.5% since the IPO and EMI (traded on the FTSE) is up 11.8% over the same period. The strong performance of WMG shares has been driven by better-than-expected financial performance, particularly in digital music, and increasing speculation about a merger with EMI Group, in our view. We have increased our price target from $20 to $23 over the past five months to reflect the better-than-expected operational performance. Our $23 price target does not reflect a potential buyout by EMI Group, which could add another $2-$4 per share based on our analysis.

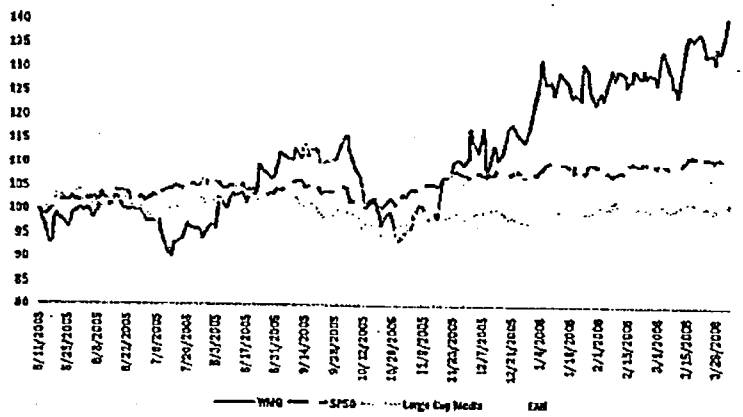
We believe our digital assumptions are already optimistic. We recently increased our digital growth forecast from a five-year CAGR (2006E – 2011E) of 28% to 36% (see our report, *SMID-Cap Entertainment 4Q05 Preview*, dated January 30, 2006). Offsetting our more aggressive digital forecast, we increased the rate of physical sales losses to an annual decline of 4%, from our previous estimate of 1%. As a result, we currently forecast that in 2009 digital revenue will account for 28% of Warner Music's total revenue, which is bullish relative to Street estimates.

Increasing our digital estimates further has a modest impact on valuation. When we perform a sensitivity increasing the pace of digital revenue growth by 15%, the net impact to our valuation is modest. Under our more aggressive scenario, we increased our five-year digital revenue CAGR (2006-2011) to approximately 40% and increased the pace of physical losses slightly, to 5% annually from 4%. The net impact on our valuation was an increase of approximately $1.25 per share.

We calculate WMG is currently trading at 11.2x 2006E EBITDA and 16.6 FCF, essentially in line with other media companies. We forecast five-year CAGRs for OIBDA of 7.6% and for FCF of 14.7%.

Figure 2

Warner Music Group
WMG Share Price Performance Since IPO (May 11, 2005)



Sources: FactSet and Banc of America Securities LLC estimates.

Figure 3

Warner Music Group
Comparable Company Analysis

Company	Ticker	Rating	Price Target	Fiscal Year End	Price	Diluted Shares	Equity Market Cap.	Net Debt @12/06 & Preferred	Other Assets @ 12/06	Enterprise Value	EBITDA (CY)	EV/EBITDA Multiple (CY)	Levered FCF (CY)	Adjusted P/FCF (CY)
Pure Play Content														
Discovery Holding Co.	DISCA	NEUTRAL	$14	DEC	$15.06	280	$4,217	$1,477	$545	$5,150	$343	15.0x	NM	NM
DreamWorks Animation	DWA	BUY	$31	DEC	$27.67	103	$2,853	($273)	$0	$2,580	$73	35.0x	$18	155.6x
Expedia	EXPE	NEUTRAL	$23	DEC	$20.06	356	$7,144	($1,637)	$102	$5,405	$656	8.2x	$701	10.0x
Lions Gate Entertainment	LGF	BUY	$11.00	MAR	$10.01	142	$1,421	($203)	$16	$1,201	$67	21.4x	$99	14.3x
Marvel Enterprises	MVL	NEUTRAL	$16	DEC	$20.39	102	$2,079	($409)	$0	$1,809	$111	15.1x	$108	18.2x
Pixar Animation	PDR	NEUTRAL	$64	DEC	$63.82	125	$7,984	($1,188)	$0	$6,798	$174	39.1x	$120	66.6x
Playboy Enterprises	PLA	NEUTRAL	$16.25	DEC	$13.75	34	$472	$72	$13	$530	$41	12.8x	$22	21.9x
Warner Music Group	WMG	BUY	$23	SEP	$22.67	149	$3,388	$1,927	$0	$5,315	$478	11.1x	$205	16.6x
Average (ex Expedia)												21.4x		49.0x
Average (ex CG Animators, Expedia)												15.1x		18.0x
Median (ex Expedia)												15.1x		20.5x
Film Exhibitors														
Regal Entertainment	RGC	BUY	$22	DEC	$19.21	153	$2,941	$1,712	$0	$4,653	$545	8.5x	$252	11.7x
Carmike Cinemas	CKFC	BUY	$30	DEC	$24.31	13	$321	$330	$0	$651	$98	6.6x	$40	8.1x
Average												7.6x		9.9x
Diversified Media														
Liberty Media	L	BUY	$10	DEC	$8.24	2,817	$23,209	$18,183	$0	$42,392	$2,760	15.4x	$1,403	16.5x
IAC/InterActiveCorp	IACI	BUY	$33	DEC	$29.86	344	$10,285	($1,234)	$0	$9,051	$935	9.7x	$435	23.6x
The following companies are covered by BAS Analyst Douglas Shapiro														
Disney	DIS (3)	NEUTRAL	$27	SEP	$27.77	2,399	$66,624	$9,059	($624)	$76,307	$6,697	11.3x	$2,763	24.4x
News Corp.	NWS.A	BUY	$21	JUN	$16.84	3,195	$53,798	$6,788	$16,097	$44,495	$5,272	8.3x	$2,489	16.2x
Time Warner	TWX	BUY	$22	DEC	$16.80	4,751	$79,820	$30,040	$2,176	$107,685	$11,930	9.0x	$4,417	17.6x
Viacom	VIA.B	BUY	$51	DEC	$38.97	791	$30,814	$5,186	$867	$35,133	$3,060	11.5x	$1,514	19.8x
Average												10.0x		19.5x

Sources: Company Reports and Banc of America Securities LLC estimates.

We would look for a pullback in valuation or signs of potential financial outperformance to get more constructive on WMG shares. Based on the Banc of America Securities ratings system, we need to have 15% or greater potential upside to our price target to reconsider our rating. However, we continue to monitor the digital and physical music market for indications that Warner is performing significantly better or worse than its peers. Growth in digital music downloads remains robust and the domestic market for ringtone sales is still relatively untapped. As a result, we could at some point further increase our valuation to reflect market conditions and Warner's performance specifically.

A Merger with EMI Is an Opportunity, Not an Answer

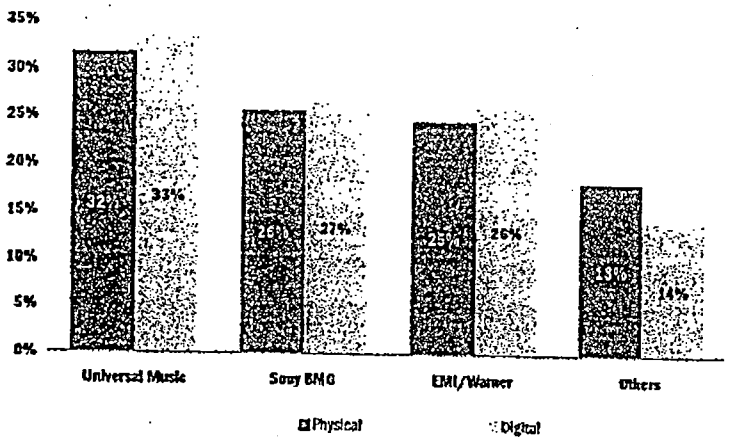
A combination between EMI and Warner Music has been contemplated for years. We believe a combination between the two companies makes sense strategically, but is based primarily on cost saving opportunities, not revenue synergies, and is not without significant risks. We also believe that if a deal is reached, and if Warner is the acquired company, Warner shareholders are not likely to receive a significant premium from current levels.

The key benefits to a merger would be the potential to combine Warner's strong U.S. business with EMI's strong European business. There are obvious economies of scale in this business and we believe annual cost savings could eventually be in excess of

$100 million. Based on 2005 data from SoundScan, a combined WMG/EMI would hold roughly 25% of recorded physical sales, have a 26% share of digital sales in the U.S. and an approximately 25% share worldwide. This compares to Universal with a 32% domestic physical share, 33% domestic digital share, and 26% worldwide share and to Sony/BMG with a 26% domestic physical share, 27% domestic digital share and 22% worldwide share.

Figure 4

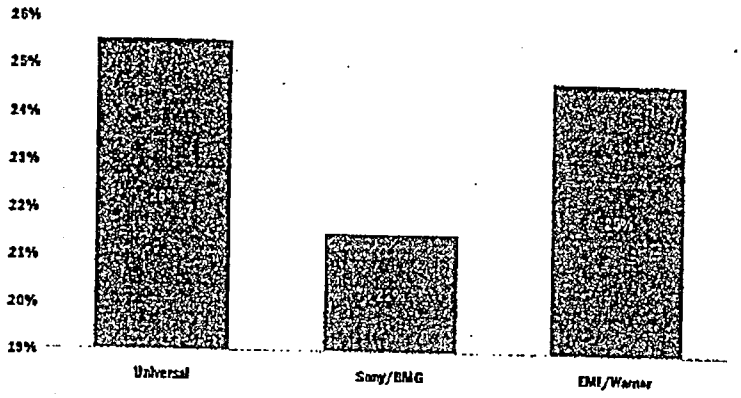
Warner Music Group
2005 Domestic Market Shares Pro-Forma for EMI/Warner Merger



Sources: SoundScan and Banc of America Securities LLC estimates.

Figure 5

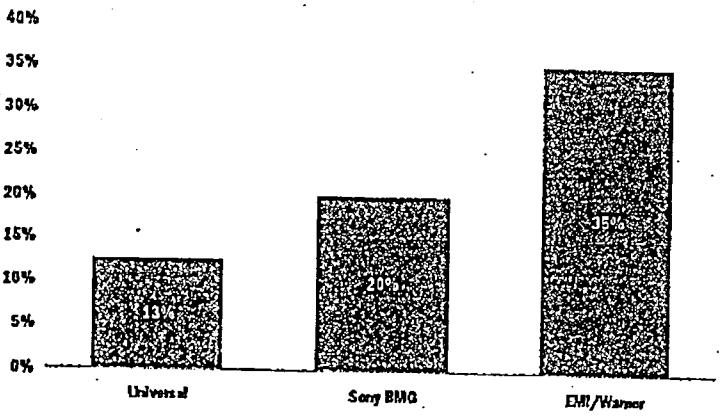
Warner Music Group
2004 Worldwide Recorded Music Market Shares Pro-Forma for EMI/Warner Merger



Sources: IFPI and Banc of America Securities LLC estimates.

Figure 6

Warner Music Group
2004 Worldwide Music Publishing Market Shares Pro-Forma for EMI/Warner Merger



Sources: Music & Copyright, Company Reports and Banc of America Securities LLC estimates.

A deal between the two companies also carries a number of risks. For starters, WMG/EMI would have an approximately 35% share of Music Publishing. It is widely believed (and acknowledged by both companies) that a sale of one of the companies' Publishing businesses would likely be necessary to clear antitrust concerns. In addition, given that this deal would be an international transaction it is possible that it would take longer than usual to close and could face more challenges than a typical domestic merger. There is also the opportunity cost that both companies would face. Warner has been the industry leader in digital innovation and there is a risk that the company could lose its focus if it becomes overly focused on merger approval and integration.

As we show in Figure 7, at $26 per WMG share, we estimate the new company would be trading at roughly 10.8x 2006E EBITDA (March yearend) and be levered 4.1:1. In our analysis, we assume EMI would acquire Warner Music for roughly $5.85 billion and would likely divest Warner's Music Publishing business to satisfy regulatory concerns. We value Warner Publishing business at approximately $1.44 billion by applying an 11x multiple to our 2006E Music Publishing EBITDA forecast of $131 million. Assuming the deal would be financed using equal parts debt and equity, we calculate that the new company would take on an incremental $2.2 billion in debt. With EMI's estimated net debt at $1.52 billion for 2006, we estimate the new combined company would have roughly $3.73 in debt at yearend 2006. We calculate that the new company would have 1.38 billion shares outstanding based on EMI's existing 875 million shares outstanding plus the additional 504 million shares EMI would issue to fund the acquisition. Based on EMI's closing price of 257p on April 4th, the new company would have an equity market cap of $6.0 billion and an enterprise value of $9.76 billion. We forecast the new company would generate roughly $900 million in EBITDA in 2006 before realizing any cost synergies and $1.06 billion in 2007 after realizing roughly $50 million in synergies. As a result, we calculate that the new company would be trading at 10.8x 2006E pro-forma EBITDA, 9.1x 2007E EBITDA (before synergies), 8.7x 2007E EBITDA (post synergies). We further calculate the company would be levered 4.1x at yearend 2006 and levered 3.0x at yearend 2007 (post synergies).

Figure 7

Warner Music Group
Pro-Forma EMI/WMG Merger Scenario Analysis

EMI/WMG Pro Forma P&L - March Year End in $US		
Income Statement	2006E	2007E
EMI Consensus Revenue	3591	3644
WMG Recorded Music	2882	3070
Combined Revenue	$6,473	$6,713
% Growth	2.7%	3.7%
Costs	$5,572	$5,703
Cost Savings	$0	$50
EMI Consolidated	475	515
WMG Recorded Music	426	446
Combined EBITDA	$901	$1,010
% Margin	13.9%	15.0%
Share Analysis	2006E	2007E
EMI Average number of shares	786	786
EMI Options	10	11
EMI Convertibles	79	79
EMI Fully Diluted Shares	875	876
Shares Issued by EMI (50/50 debt-equity)	504	504
New Average Shares	1379	1380

Note:
WMG estimates adjusted for March year end.
EMI estimates based on Street consensus.

Merger Scenario - March Year End		
WMG Takeout Price	$26	
WMG Current Price	$22.79	
EMI Current Price	250.0p	
Exchange Rate (£GBP to $US)	1.75	
	2006E	2007E
WMG Fully Diluted Shares	149.5	149.5
WMG Market Cap @ Takeout Price	$3,886	$3,886
WMG Net Debt	$1,963	$1,823
Total WMG Enterprise Value	$5,849	$5,709
Assumptions for Publishing Sale		
WMG Publishing OIBDA	$131	
WMG Publishing Multiple	11.0x	
WMG Publishing Value	$1,439	
WMG Net Acquisition Price (excl. Publishing)	$4,410	NA
Pro Forma WMG/EMI Capital Structure		
EMI Net Debt (pre-deal)	$1,523	
EMI Incremental Debt (50/50 debt-equity)	$2,205	
Pro Forma Net Debt	$3,727	$3,187
EMI Shares (pre-deal)	875	1,379
New Shares Issued (50/50 debt-equity)	504	0
Pro Forma Shares Outstanding	1,379	1,379
EMI/WMG Pro Forma Market Cap	$4,833	$8,033
EMI/WMG Pro Forma EV	$9,760	$9,220
EMI/WMG Pro Forma EBITDA (pre-cost savings)	$901	$1,010
Annual Cost Savings	$0	$50
EMI/WMG Pro Forma EBITDA (post-cost savings)	$901	$1,060
EV/EBITDA	10.8x	8.1x
EV/EBITDA (post-synergy)	NA	8.7x
Debt/EBITDA	4.1x	3.2x
Debt/EBITDA (post-synergy)	NA	3.0x

Note: Estimates are for March yearend.

Sources: Company Reports, Street Consensus, FactSet and Banc of America Securities LLC estimates.

Meetings with Management Support L-T Thesis

We recently hosted investor meetings with Warner CEO Edgar Bronfman Jr. and CFO Michael Fleisher in California. While we now believe that WMG shares are trading close to fair value, Mr. Bronfman and Mr. Fleisher did a good job articulating Warner's

long term opportunity to capitalize on the transition to digital music. Specific highlights included:

- **Digital growth continues to track ahead of expectations.** In fiscal 2005 digital revenues made up roughly 4.6% of Warner's total revenue. In 1Q06 digital revenue made up 6.6% of total revenue and Warner's U.S. market share of digital revenue was materially higher. The company expects digital revenue to comprise more than 20% of its total revenue by 2008, consistent with our forecasts.

- **Warner Music is also outperforming its peers in digital music.** In the December 2005 quarter Warner's physical market share was 17% and its digital market share was 23%, the widest margin of any of its peers. Warner Music has been the most aggressive in selling digital albums, using enhanced bundles (which include various pieces of content, such as digital tracks, ringtones, videos, wallpaper, etc.) to increase volume and profitability. The company had particular success with the recent Madonna album, which sold significantly more enhanced digital albums (priced at $12.99 or higher) versus the basic album (priced at $9.99).

- **The mobile opportunity is significant, particularly in the U.S.** Management expects the opportunity in wireless mobile to become more visible in 2006 and 2007. Mr. Bronfman noted that next generation handsets are just now beginning to hit the market and are far easier to use. He noted a wide range of new offerings, such as SMS Tones, which plays musical tones when a text message is received on a handset. Although SMS Tones are unlikely to be a major financial contributor on their own, they provide a simple example of one of the new opportunities in the mobile market. Today, mobile services account for 30% of Warner's total digital revenue. The company expects mobile to exceed 50% of total digital revenue in two to three years.

- **A merger with EMI could provide an opportunity, but is not without risks.** Mr. Bronfman noted a number of risks associated with a merger, including other industry mergers that have not gone smoothly, the erosion of value in a merger of equals, regulatory risks, and the opportunity costs in lost innovation. The benefits to a deal would be substantial cost savings and economies of scale opportunities, particularly as Warner's innovations in digital music are applied to other platforms. Following management's comments we came away believing that a deal is possible, but not necessarily imminent.

- **Physical sales are still eroding, but Warner believes there is enough leverage in the model to be successful.** Mr. Fleisher noted that 76% of Warner's costs are variable and that the company could do well financially even if physical sales eroded 3-5% per year because further costs could be taken out of the business (assuming digital sales continue to grow). Specifically, expenses related to its distribution network and sales & marketing effort could be scaled back or reallocated to the digital product. Warner is also working to improve the quality of physical albums to help drive new growth.

- **The opportunity in emerging markets is mostly related to digital.** Management noted that the physical business in countries such as Russia and China is extremely difficult (if not impossible) because of piracy. Warner is looking for ways to be involved in legitimate digital businesses in markets such as these.

- **Competition with Apple's iTunes is inevitable.** Amazon.com recently announced its entry into the subscription music business and Warner is working with other companies to develop alternative channels to Apple, which currently has an 80% market share. Once there is greater competition in digital distribution Warner may be able to also capture the casual music consumer, who might download just a handful of songs each year, but currently isn't spending any money on music.
- **Warner may be able to increase its dividend or return cash to shareholders in other ways over time.** The company currently pays $0.55 per year in regular dividends, equating to a current yield of 2.5%. While the company does not expect to increase its dividend soon, the stable FCF structure of the business should provide it with opportunities to increase the yield over time.

Figure 8

Warner Music Group
Digital Summary

Digital Detail			Dec05	Mar06	Jun06	Sep06							
CONSOLIDATED	2004	2005	1Q06E	2Q06E	3Q06E	4Q06E	2006E	2007E	2008E	2009E	2010E	2011E	2012E
Recorded	$32.0	$139.9	$64.9	$66.0	$77.9	$97.5	$305.4	$540.9	$818.5	$1,084.6	$1,265.9	$1,426.2	$1,571.4
% Growth	NA	337.2%	166.7%	114.1%	105.0%	107.1%	118.3%	77.1%	51.3%	32.5%	16.7%	13.5%	9.4%
Publishing	$0.0	$30.0	$5.2	$6.5	$9.9	$9.9	$31.4	$55.0	$79.2	$99.8	$117.1	$131.9	$145.1
% Growth	NA	NA	30.0%	61.3%	64.6%	64.6%	57.0%	75.0%	44.2%	25.7%	17.6%	12.6%	10.0%
Total Digital Sales	$32.0	$159.9	$69.2	$72.4	$87.8	$107.4	$336.8	$595.8	$897.7	$1,184.2	$1,383.2	$1,560.2	$1,716.5
% Growth	NA	393.7%	147.1%	108.0%	98.5%	102.3%	110.6%	76.9%	50.7%	31.9%	16.8%	12.4%	9.5%
% Total Revenue	0.9%	4.6%	6.6%	9.7%	11.1%	11.1%	9.9%	15.9%	22.0%	28.3%	32.0%	35.2%	37.7%
				4.6%									
RECORDED SEGMENTAL													
Mobile/Other	$15.0	$67.0	$31.0	$26.2	$37.0	$43.2	$138.3	$241.6	$348.4	$452.9	$523.7	$591.4	$638.5
% Growth	NA	346.7%	138.5%	104.7%	93.5%	94.7%	106.5%	74.7%	44.2%	30.0%	15.6%	12.9%	8.0%
Internet	$17.0	$72.9	$33.0	$39.8	$40.0	$54.3	$167.1	$299.3	$470.1	$631.7	$742.2	$844.9	$932.9
% Growth	NA	328.8%	200.0%	120.8%	118.5%	118.1%	129.1%	79.2%	57.1%	34.4%	17.5%	13.8%	10.4%
Digital Recorded Revenues	$32.0	$139.9	$64.9	$66.0	$77.9	$97.5	$305.4	$540.9	$818.5	$1,084.6	$1,265.9	$1,436.2	$1,571.4
% Growth	NA	337.2%	166.7%	114.1%	105.0%	107.1%	118.3%	77.1%	51.3%	32.5%	16.7%	13.5%	9.4%
% of Recorded Sales		4.8%	7.1%	11.9%	13.2%	12.4%	10.2%	17.1%	24.5%	30.8%	35.0%	38.8%	41.8%
PUBLISHING SEGMENTAL													
Internet Downloads	$0.0	$10.7	$2.6	$4.4	$5.1	$5.1	$17.3	$30.2	$43.1	$53.3	$62.1	$69.2	$76.1
% Growth	NA	NA	30.0%	63.9%	70.8%	70.8%	61.4%	75.0%	42.6%	23.6%	16.5%	12.5%	10.0%
Ring Tones	$0.0	$9.3	$2.6	$7.0	$4.8	$4.8	$14.1	$24.7	$36.1	$46.3	$55.1	$62.7	$69.0
% Growth	NA	NA	30.0%	55.8%	58.3%	58.3%	51.9%	75.0%	46.2%	28.2%	18.9%	13.9%	10.0%
Digital Publishing Revenues	$0.0	$20.0	$5.2	$6.5	$9.9	$9.9	$31.4	$55.0	$79.2	$99.8	$117.1	$131.9	$145.1
% Growth	NA	NA	30.0%	61.3%	64.6%	64.6%	57.0%	75.0%	44.2%	25.7%	17.6%	12.6%	10.0%
% of Music Publishing Sales		3.3%	3.96%	4.25%	5.30%	7.06%	6.3%	6.9%	12.1%	14.3%	15.9%	16.8%	17.6%

Sources: Company reports and Banc of America Securities LLC estimates.

Figure 9

Warner Music Group
DCF Valuation

($ in millions)

DCF Valuation	2004	2005	2006E	2007E	2008E	2009E	2010E	2011E	2012E	2006-2011 CAGR
EBITDA	$390	$322	$474	$489	$547	$605	$644	$683	$710	7.6%
Growth	NA	-17.5%	47.2%	3.2%	12.0%	10.5%	6.4%	6.1%	3.9%	
Less...										
Change in Working Capital	20.0	(1.3)	0.3	12.0	12.0	12.0	12.0	12.0	12.0	
Less...										
Capital Expenditures (Capex + Advances)	68.0	79.4	87.3	93.7	99.9	106.6	113.8	121.4	129.6	6.8%
Growth	NA	16.8%	9.9%	7.3%	6.7%	6.7%	6.7%	6.7%	6.7%	
Less...										
Normalized Cash Taxes	30.2	45.8	49.7	51.3	57.5	63.5	67.0	71.7	74.0	
Equals...										
Unlevered After-Tax Free Cash flow	271.9	197.9	338.4	332.0	378.1	422.7	450.3	478.1	494.0	7.3%
Growth	NA	-27.2%	70.0%	-1.3%	13.9%	11.8%	6.5%	6.2%	3.3%	
Terminal Value 2012(FCFt+1)/(WACC-g)			$0	$0	$0	$0	$0	$0	7,304.3	
Imputed EBITDA Multiple									10.3x	

Weighted Average Cost Of Capital	10.0%
Debt Proportion Of Financing	20.0%
After-Tax Cost Of Debt Financing	4.2%
Marginal Tax Rate	35%
Weighted Average Net Cost Of Funds	6.5%
Equity Proportion Of Financing	80.0%
Cost Of Equity Financing	11.4%
10 Year Treasury	4.5%
Market Risk Premium	5.8%
Beta	1.19

	2006E	2007E
NPV 5-Year Forward FCF Stream	$1,538	$1,668
NPV 2012 Forward Terminal Value	4,131	4,542
Total NPV	5,668.2	6,208.4
Less... Net Debt and Preferred	1,862	1,752
Plus... Off Balance Sheet Assets at FMV	85	42
Plus... Options Exercise	0	0
Equals...Private Equity Value	3,890.9	4,498.6
Less...25% Public Discount		
Target Public Equity Value	2,918	3,374
Target Eq. Value per Share (CY)	3,032	3,441
Target Public Equity Value per Share (CY)	$28	$32
Current Price	$22.23	
Potential Appreciation	-0%	4%

Sources: Company reports and Banc of America Securities LLC estimates.

Figure 10

Warner Music Group
P/FCF Valuation

	2004	2005	2006E	2007E	2008E	2009E	2010E	2011E	2012E
EBITDA	$390	$322	$474	$489	$547	$605	$644	$683	$710
Less... Capex	68.0	79.4	87.3	93.7	99.9	106.6	113.8	121.4	129.6
Less... Cash Interest Expense	55.5	127.8	143.0	119.1	113.7	107.8	101.3	94.5	81.4
Less... Normalized Cash Taxes	30.2	45.8	49.7	51.3	57.5	63.5	67.6	71.7	74.6
Less... Preferred Dividends	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Less... Changes in Working Capital	20.0	(1.3)	0.3	12.0	12.0	22.0	12.0	12.0	12.0
Equals... Levered After-Tax Free Cash Flow	$216.4	$70.1	$193.4	$212.9	$264.3	$314.9	$349.0	$383.5	$412.6
FCF/Share		$0.47	$1.29	$1.42	$1.77	$2.11	$2.34	$2.57	$2.78
Note: Current P/FCF Multiple		47.4	17.2	15.6	12.6	10.6	9.5	8.7	8.1
Note: Forward 3-Year FCF CAGR		56%	18%	18%	13%	9%			

Times... Assumed P/FCF Multiple on Forward FCF		15.0x	15.0x	15.0x	
Equals...Firm Equity Value	$0	$4,724	$5,235	$5,753	$0
Divided By... Fully-Diluted Share Count	149.5				
Equals...Firm Equity Value/Share	$0.00	$31.61	$35.03	$38.49	$0.00

	2006E	2007E
NPV '08 Value	$25.47	$28.37
NPV '09 Value	$25.34	$28.22
NPV '10 Value	$24.99	$27.84
Average of '08-10 NPV	25.26	28.15
Equals... Equity Value (TY)	26.02	28.71
Equals... Equity Value (CY)	26.69	29.46
Equals... Price Target (CY)	$27	$29
Implied Multiple of Forward EBITDA	12.6x	12.8x
Current Price	$22.23	
Appreciation Potential	20%	33%

Sources: Company reports and Banc of America Securities LLC estimates.

Figure 11

Warner Music Group
Income Statement

	2004	1Q05	2Q05	3Q05	4Q05	2005	1Q06	2Q06E	3Q06E	4Q06E	2006E
Revenue:											
Recorded Music	$2,851.2	$939.9	$821.0	$568.0	$775.2	$2,924.1	$928.0	$598.8	$630.1	$833.5	$2,987.3
Music Publishing	560.0	155.4	153.8	161.0	137.0	607.2	131.3	151.7	165.1	139.9	587.9
Intersegment Elimination	(18.0)	(7.4)	(8.0)	(7.0)	(7.2)	(29.6)	(7.0)	(7.0)	(7.0)	(7.0)	(28.0)
Total Revenue	3,393.2	1,088.0	966.8	742.0	905.0	3,501.8	1,044.3	743.4	788.2	966.4	3,542.2
Growth	NA	-6.1%	6.3%	3.5%	13.4%	3.1%	-4.0%	-3.1%	6.2%	6.8%	1.2%
Expenses											
Cost of Revenue											
Royalties	530.0	166.7	125.1	103.5	183.9	584.2	103.6	110.9	128.9	178.3	583.7
A&R	994.7	360.8	235.1	248.3	258.2	1,088.4	316.0	229.1	242.9	270.3	1,058.3
Other	233.3	41.0	44.0	44.5	52.9	182.3	42.6	38.2	39.8	46.8	167.4
Total Corporate	78.1	21.1	17.9	17.0	23.0	78.9	23.0	17.4	19.8	25.9	86.1
Total COGS	(26.6)	(7.0)	(6.3)	(3.6)	(3.0)	(19.9)	(7.0)	(7.0)	(7.0)	(7.0)	(28.0)
	1,809.5	572.6	415.7	412.6	485.0	1,886.0	531.2	388.6	424.4	514.3	1,858.5
Gross Profit	1,585.7	515.4	351.0	329.4	420.0	1,615.8	513.0	354.7	363.8	452.1	1,683.7
Margin	46.7%	47.4%	45.8%	44.4%	46.4%	46.1%	49.1%	47.7%	46.2%	46.8%	47.5%
Distribution							531.5	358.0	364.5	446.9	
Variable Marketing	94.0	26.0	17.0	14.2	27.4	84.6	23.5	18.9	17.3	33.3	93.1
Selling Overhead	419.4	120.4	88.9	82.3	105.5	397.1	123.0	88.3	91.2	132.6	435.0
Marketing Overhead	83.7	21.0	20.4	19.9	21.6	82.9	21.6	21.7	21.8	23.6	88.8
G&A Overhead	161.8	32.0	33.6	31.9	33.2	130.7	32.8	35.4	35.4	35.6	139.0
Corporate Overhead	397.7	88.6	94.1	93.8	98.9	375.4	93.7	96.1	97.0	102.1	388.9
Other	76.4	55.0	22.5	124.7	62.0	264.2	26.0	25.0	25.0	25.0	100.0
Total Operating Expenses (Ex. D&A)	(42.4)	(17.0)	(13.5)	(4.9)	(6.0)	(41.0)	(8.0)	(15.0)	(7.8)	(4.0)	(34.8)
	1,195.6	326.0	262.9	362.3	342.7	1,294.0	311.4	270.3	279.9	348.3	1,210.0
OIBDA	390.1	189.4	88.1	(33.0)	77.3	321.8	201.6	84.4	83.9	103.8	473.7
Growth	NA	11.2%	75.9%	-142.5%	-16.2%	-17.5%	6.5%	-4.2%	-354.5%	34.3%	47.2%
Margin	11.5%	17.4%	11.5%	-4.4%	8.5%	9.2%	19.3%	11.4%	10.6%	10.7%	13.4%
Depreciation	67.0	14.0	14.0	12.0	11.0	51.0	11.0	13.4	13.4	13.4	51.2
Amortization	181.8	48.0	47.0	47.0	47.0	187.0	47.0	54.5	54.5	54.5	210.5
Operating Income	$141.8	$123.4	$27.1	($92.0)	$19.3	$83.8	$143.6	$16.5	$16.0	$35.9	$212.0
Growth	NA	23.3%	-340.8%	-668.2%	-39.6%	-40.9%	11.0%	-39.1%	-117.4%	86.3%	153.0%
Margin	4.2%	11.3%	3.5%	-12.4%	2.1%	2.4%	13.8%	2.2%	2.0%	3.7%	6.0%
Other Expenses:											
Interest Expense	55.5	38.0	62.0	60.0	42.0	182.0	45.0	35.0	33.0	30.0	143.0
Other Gains/Losses	-	24.0	(39.0)	33.0	(2.0)	18.0	-	-	-	-	-
Management Fees	10.0	-	-	-	-	-	-	-	-	-	-
Total Other Expenses	65.5	62.0	13.0	83.0	40.0	198.0	45.0	35.0	33.0	30.0	143.0
Pre-Tax Income	76.3	67.4	14.1	(175.0)	(20.7)	(114.2)	98.6	(18.5)	(17.0)	5.9	69.0
Income Tax Expense	92.0	32.0	10.0	4.0	9.0	55.0	$30.0	$4.0	$5.0	$2.1	41.1
Tax Rate	NM	47%	71%	-2%	-43%	-43%	30%	NA	NA	35%	60%
Net Income	(15.7)	35.4	4.1	(179.0)	(29.7)	(169.2)	68.6	(22.5)	(22.0)	3.8	27.9
EPS - Basic	NA	$0.33	$0.03	($1.41)	($0.21)	($1.25)	$0.48	($0.16)	($0.16)	$0.03	$0.20
Growth	NA	NA	NA	NA	NA	NM	NA	NA	NA	NA	-115.7%
Adjusted EPS - Diluted	NA	$0.31	$0.03	($0.27)	$0.08	$0.16	$0.46	($0.15)	($0.25)	$0.03	$0.19
% Growth	NA	NA	NA	NA	NA	NA	48.5%	NM	NM	NM	NM
Basic Shares Outstanding		107.5	127.0	127.0	141.2	125.7	141.2	141.2	141.2	141.2	141.2
Diluted Shares Outstanding		115.3					150.5	150.5	150.5	150.5	150.5

Sources: Company reports and Banc of America Securities LLC estimates.

EXHIBIT CO 0953

citigroup

See page 18 for Analyst Certification and Important Disclosures

BUY (1)
High Risk (H)

EQUITY RESEARCH: UNITED KINGDOM

Media — General

Price:	£2.55
Target:	£2.70
Mkt Cap:	£2,026.7m

25 January 2006

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EMI

Keep Holding On

- Early 2006 (and it is early) has seen a pick-up in US for digital and overall market; if trend continues, risk of EMI restructuring falls, and probability of industry returning to growth rises; given a soft US and UK Q4 (industry and EMI), this is vital
- Press reported on 24 January that EMI Publishing may sign pan-European royalty collection contract for English language; should be source of upgrades
- View: risk reward still works, but risks high; conservative 8.5x NPS multiple for publishing, 50% estimated merger savings and 7.2x EBITDA for recorded music (ie flat growth) gets us to 270p

Rating: Unchanged Target Price: Unchanged Estimates: Changed United Kingdom

EMI.L **Price: £2.55**

Year to Mar	Revenues (£m)	PBT (£m)	EPS (p)	EPS (Old) (p)	P/E Multiple	P/E Relative	EV/ Revenue	Operating Margin (%)	EV/ EBITDA	Net Div (p)
2004A	2,120.7	163.1	15.6	15.8	16.1	0.9	1.4	11.8	10.8	8.0
2005A	1,942.7	141.9	13.5	13.5	18.8	1.1	1.6	12.0	11.9	8.0
2006E	2,052.4	151.9	14.5	14.9	17.5	1.2	1.5	11.9	10.9	8.0
2007E	2,084.1	168.9	16.0	16.6	15.9	1.2	1.5	12.4	10.4	8.5
2008E	2,116.6	183.6	17.7	18.3	14.4	1.2	1.4	13.1	9.7	9.4

52W Price Range: £2.81 to 2.07

				Price Performance (%)	Yld	-1m	-3m	-12m
Expected Share Price Return	5.9%	Shares Outstanding	785.5m	Absolute	6.0	6.4	21.3	2.2
Expected Dividend Yield	3.1%	Market Cap.	£2,028.6m	Relative to Local	5.4	4.3	10.0	-16.4
Expected Total Return	9.0%			Relative to DJ STOXX	5.5	4.5	9.7	-18.0

Sources: Company reports and Citigroup Investment Research estimates.

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Investment Analysis

In the last month, we have met with all four majors and wanted to pass on feedback and views. All groups we have met acknowledge the risk that physical percentage declines could remain close to double-digit for some time. This comes on the back of calendar Q4 2005, which was weak for the industry (US & UK), and for EMI from a market share perspective (US, Japan). More recently, January 2006 data in the US is very encouraging, but it is too early to say we have turned the corner. Easing comps for Sony BMG and improvement in DRM should be beneficial for the industry in 2006.

We still see risk to EMI (and WMG) market share (which could catalyse a potential merger[1]), although we expect Norah Jones to release in 2006. Our 270p target price for EMI seems balanced if conservative, factoring in some possibility of merger and a stabilising market, but not a rerating for publishing or an assumption of a turn in recorded music.

We leave our operational forecasts for EMI intact, increase interest costs but reduce tax rate and adjust currency — overall the impact is immaterial. Improving digital data and Q4 release schedule should offset a weak Q3.

Near-term data tilting positively: of concern is the slowdown in UK growth (from almost flat first nine months to –6% calendar Q4 for volumes — source BPI). But the US has started 2006 positively, and for EMI fiscal Q4 in the US is very important (heavy release schedule) — each of the last five weeks have seen positive growth for the overall market, and digital has doubled its share from 7.5% last year to 15% at the start of this year.

Medium-term story still encouraging. Recent stabilisation of the global market and piracy levels lend optimism. Industry is diversifying from CDs: digital downloads; subscription; video streams and downloads; ring-tones; ring-backs (both could move from mobile to land line); licensing deals. Sony BMG stabilisation would help global trends.

Risks: weak industry creativity; piracy; competition for consumer dollar; portability of all content (although music as 'eyes close' medium still has USP); strength of Apple, and related lack of iTunes format compatibility, lack of flexibility on single download pricing, and dragging heals on encryption. EMI market share (especially in the US) volatility is still concerning.

Lack of cash generation has been a major issue for EMI historically. If the industry is stabilising, restructuring charges should not recur, and mix shift to digital should improve margins and release working capital. The group is focused on finding further efficiencies in cash handling, and refinancing (a three-year task) should ultimately save another £25m. All told, cash generation post servicing the dividend could move from £49m that we model for 2007E to £85m. 90% of this is dependent on top-line stabilising. This is why restructuring in the US would be particularly painful (as it would for WMG outside the US).

---

[1] See our report '*Warner Music Group — Get Together*', 22 September 2005.

Three parts to our valuation for EMI: 1) recorded music multiple; 2) if industry fails to recover, merger likelihood increases — value of synergies; and 3) what would a buyer pay for publishing (in a merger, major publishing asset would likely be sold)? Risk reward tilts very much to the upside, but risks are high. March 2007E P/E of 16.6x requires either a merger, a re-rating of publishing or a return to growth of recorded music. We see all of these as reasonably likely.

Investment Summary

Recorded Music: Evidence Mixed

- 2004 saw a global music decline of -1%, and H1 2005 saw the same level of decline according to the IFPI; this follows a 23% organic decline in 1999-2003.
- Soundscan data would suggest that US purchased music declined at almost 3.9% during 2005. This may prove slightly conservative as a read for the overall revenues. We believe growth from subscription and other new sources will slightly outweigh the decline from DVD music. However, physical growth was -8.9%, and this decline (as retailers look to stock higher-return goods) is an ongoing cause for concern.
- Early signs for 2006 are encouraging, with the market (defined as physical and digital albums and digital tracks on an album equivalent basis, 10 to 1) up 5.8% last week (yoy), and having been up consistently for the last month. In addition, digital single-track downloads were 11.6m, over twice the level of last year, again trending similarly over the last month.
- 2004 and 2005 have not been helped by WMG's restructuring and Sony BMG's joint venture. WMG has seen a recovery (market share up from 16% to 17% US), and we would expect Sony BMG to stabilise, as the 3ppt drop in market share has been consistent throughout 2005 in the US. Greater stability among the majors (75% global market) should help overall global growth in 2006.
- The other risk (on top of physical declines) is market share for EMI. We think EMI was down 10% in fiscal Q3 in the US (seasonally vital) on a weak release schedule in a market down 3.7%. The improving market in Q4 is very encouraging as EMI's release schedule is highly Q4 weighted this year, and the comparable extremely easy. In 2006, we would expect Norah Jones to release, and we would hope this would make up for the absence of a Coldplay release.
- Data on detected hardcopy piracy suggests there has been a stabilisation since 2003, and over the last six months, P2P traffic in music has declined despite strong growth in broadband penetration.

[2] WMG is covered by Jason Bazinet and rated 2S (current price $21.18).

Near term: global market may have deteriorated slightly in H2 2005 — Christmas Blues . . . still a risk

EMI put up the following slide at its H1 results presentation:

Figure 1. Global Market Trends

Region	Change H1 2005/2006		Trends and outlook
	Physical only	Physical & Digital	
Global	-4.7%	-0.9%	Digital sales growth almost offset decline in physical sales. Continued variation in growth by region
North America	-7.3%	-2.7%	Digital represents significant proportion of total sales. Tough H1 due to weaker release schedule
Continental Europe	-6.7%	-3.0%	Continuing improved trend driven by French and Spanish markets. Germany and Italy remain challenging
UK & Ireland	-1.1%	2.8%	Digital sales growth more than offsetting decline in physical sales. Softer retail environment
Japan	0.8%	3.6%	Improving trend driven by strong industry wide release schedule, particularly of local repertoire
Latin America	11.3%	12.0%	Return to growth in Brazil, growth across all other markets
Australasia	-5.1%	-4.1%	Improved trend driven by stronger industry release schedule
SEA ex Japan	-12.4%	-8.2%	Difficult trading conditions in China. Very strong growth in digital mobile music

Source: EMI and Citigroup Investment Research.

While data is scant outside the US and UK, from qualitative comments in the global press, we do not think 2H calendar 2005 trends in continental Europe or Japan have changed a great deal. However, Japan was the one market in which EMI's year-on-year market share declined in H1, and Q3 trends are similar. The US, from Soundscan data, has been reasonably consistent throughout the year, while the UK deteriorated in Q4 considerably. BPI data suggests that after a flat first three quarters, calendar Q4 was down around 6%. The Christmas quarter for the global industry is probably 30% revenues and 40% profits. Last year, EMI warned in February — further weakness in the US might prompt further restructuring and put a hole in the idea of improving cash generation.

But 2006 has started encouragingly and EMI's release schedule is stronger than fiscal Q3

This was the release schedule EMI presented at the H1 results. Only KoRn, Beastie Boys and Chris Cagle released in the US in Q3; the rest are coming in Q4, so it is encouraging that the overall market has picked up in the US, as already described.

Figure 2. EMI — Highlights of the H2 2005/06 Planned Release Schedule

UK	Kate Bush, Depeche Mode, John Lennon, Massive Attack, Placebo, Starsailor, Robbie Williams
US	Beastie Boys, Ben Harper, Bubba Sparxxx, Chingy, Chris Cagle, Dem Franchise Boys, KoRn, LIFE, Pharrell Williams, The Little Willies, Yellowcard
France	Jean-Louis Aubert, Gam's, Michel Legrand, Rohff
Italy	Tiziano Ferro, Vasco Rossi
Spain	Arrebato, Luz
Brazil	Marisa Monte
Japan	175R, Kishidan
Global	Live 8

Source: EMI and Citigroup Investment Research.

With the market in the US overall up mid single-digits year to date 2006, digital more than doubling its contribution, and EMI's comparable very easy (we estimate down mid teens last year), we would expect to see decent growth.

Medium term: piracy not the drag it was at start of the decade

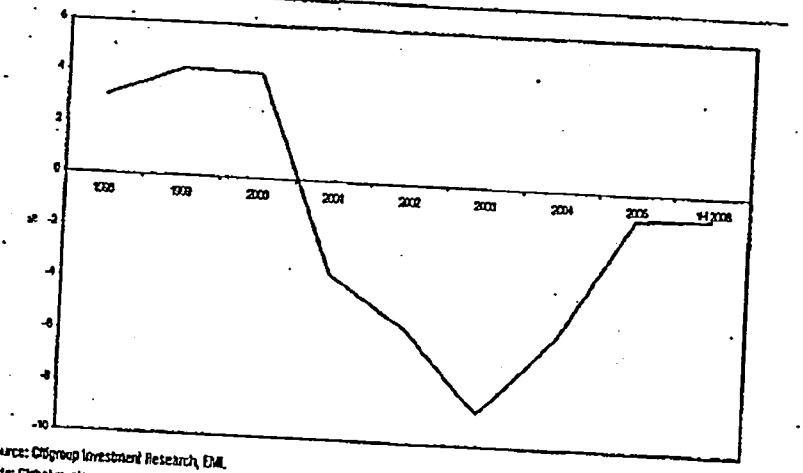
The recorded music industry has had positive court rulings on both Asia and the US. The most important ruling was in the *Grokster* case in the US, in which the Supreme Court ruled that if the predominant use of P2P networks was for purposes that breach copyright, then the services themselves are illegal. Since that ruling, 'cease & desist' letters have been sent out to all seven of the major P2P networks in the US, and all have agreed either to close or turn legitimate. P2P is still an issue (beyond the US as well), and piracy finds new modes, but our sense is that piracy is stabilising now, rather than growing.

Copyright protection remains a major issue for the music industry. Last year, Sony put CDs into the market that automatically uploaded spy-ware to customers' hard-drives. Sony did not ask permission to install spy-ware (which allows Sony to track media consumption). This increased the chances of hacking/viruses. Although these CDs have been withdrawn, this has pushed back industry efforts to come up with a solution to copyright protection, which protects 'fair use'.

EMI is confident that its efforts in copyright protection are bearing fruit. Its Microvision 300 allows seven single-track copies and three album copies. If the consumer abandons copy control, he loses the value-added content, eg video clips. EMI believes that Apple is technologically able to facilitate uploads from this technology, but as a result of the Sony BMG problems has pushed back the timing of any agreement.

Trends for global music consumption are encouraging

Figure 3. Global Music Growth (%)



Source: Citigroup Investment Research, EMI.

Note: Global music growth is stated pre-currency, and is for EMI's fiscal period ends, ie the year to March.

The recorded music market is beginning to look more like music publishing. The publishing industry has been able to diversify away from its core, declining music purchasing revenue stream into performance (media play), synchronisation and ring tones.

Sources of demand for music evolving quickly — major positive to diversify away from physical music

We are moving from a situation in which CD sales were over 90% of the legitimate market as recently as two years ago to a very new order. Each of the following revenue sources is likely to see material growth in the coming years:

- Music video downloads — iTune videos and 3G should drive this.
- Pay per click revenues on video streams — the music companies get close to 1c per stream, and we estimate for EMI this will contribute over £8m in 2007E.
- There is an evolving trend for music companies to participate in revenues from merchandise and concerts.
- Ring-tunes and ring-back tunes may move from mobile to fixed line and also to Skype and equivalent services. This has been a completely new revenue source for the industry in mobile.
- Subscription services like Napster and Yahoo are gathering pace.
- *Imesh* is moving its illegal service to legitimate P2P. This kind of development should help drive digital downloads (both single and album). Last week EMI signed a contract to licence Gnab technology to help facilitate P2P.

In addition, the trajectory of digital growth looks encouraging, as we start the year. Last week (which may have normalised for the high level of gift vouchers) saw downloads of 11.5m in the US compared to 5.5m to 6m for Q1 2005.

While some of this is digital growth in precipitating an acceleration in the decline of the physical market, we would argue that a good proportion of it (especially the single download market) is likely to be incremental.

There are further potential drivers of growth in 2006 . . .

- Expansion in broadband, iPod, PC and 3G handset penetration should help drive digital growth harder. iPod has been a fast-selling Christmas gift for the past three years, and as its price point has declined, it has continued to stimulate the market.
- There is a likelihood at some stage of variable pricing for downloads. We note that in Japan, iTunes pricing is already variable.
- Royalty rates from internet and satellite radio broadcasters may rise.

. . . and risks:

- As usage of internet radio etc rises, there is a risk that consumers, who can to a large extent 'tailor-make' their own channels, will purchase less music. Therefore, unless royalty rates move ahead materially, there is a risk that this exacerbates the decline of the physical market. We attempted to address this issue in our September 2005 report *'Warner Music Group — Get Together'*.

- Over the next 18 months the music industry is due to renegotiate terms with a number of its end users. In all likelihood the industry is unlikely to reach an accommodation without arbitration. Royalty rates that end broadcasters have to pay to the music industry are regulated (by CARP, Copyright Arbitration Royalty Protection). The upcoming arbitrations are:
  - 1. Internet radio — currently we understand the music industry receives 0.07c per song, or roughly 1c per hour of listening. The implication is that internet radio companies need to generate a CPM of $10 to break even (assuming they are paying 1c per customer to the industry — arguably the breakeven point is much lower, as customers will see more than one advert per hour). This looks extremely low, and as these businesses have scaled over the last five years, we think there is a good chance that the music industry will see a reasonable uplift.

    The difficulty will be in proving not only that these services can afford to pay more (and from an equitable standpoint should), but also that these services are cannibalising music purchase, because technology is facilitating highly focused segmentation (close to pull) and storage (almost purchase, without paying).
  - 2. Mobile radio.
  - 3. Satellite radio — in our report '*Warner Music Group — Get Together*', we constructed a model attempting to demonstrate potentially lost revenues from the music industry as customers satisfy their demand for music via satellite radio. We argued that for the music industry not to lose out, royalty rates would have to move from 70c per subscriber per month to $2.50-3.00. We refer investors back to this report. The same rationale would apply to internet and mobile radio (numbers will differ).
- Apple's grip on the digital market is a concern, and may pressure dealer share medium term. However, we note that many of the global technology majors are beginning to enter the market: Sony and Yahoo have existing products, and Microsoft and Google may well become distributors medium term. The lack of compatibility of iTunes to hardware devices other than iPod could protect Apple's advantage, but equally could eventually destroy its grip on the market.

On balance we are encouraged, and believe positive evidence is building that the overall market is stabilising and the growth of digital is coming through.

We forecast 2.3% organic growth in recorded music 2006E (market share driven), and 1% in out years

Figure 4. EMI Recorded Music — Revenues & EBIT (March Year-End, Pounds in Millions)

EMI Recorded Music			IFRS				
Revenues & EBIT (March year end)	2004	2005	2006E	2007E	2008E	2009E	2010E
Revenues	1,723	1,542	1,604	1,620	1,636	1,652	1,669
EBIT	147	133	141	150	163	175	187
EBIT margin %	8.5%	8.6%	8.8%	9.3%	10.0%	10.6%	11.2%
EBIT growth	-2%	-10%	6%	6%	9%	8%	7%
Revenue growth %							
Global market share	13.5%	12.9%	13.3%	13.3%	13.3%	13.3%	13.3%
Growth from market share	6.3%	(4.4%)	3.1%	0.0%	0.0%	0.0%	0.0%
Growth in $ global market	(5.6%)	(3.1%)	(0.9%)	1.0%	1.0%	1.0%	1.0%
Currency impact	(1.3%)	(3.1%)	1.8%	0.0%	0.0%	0.0%	0.0%
Acquisition impact	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Total	(0.6%)	(10.5%)	4.0%	1.0%	1.0%	1.0%	1.0%
EMI recorded units (mn)	363	328	321	311	298	282	265
Unit declines (partly due to digital migration)	0.7%	(6.1%)	(4.3%)	(4.3%)	(5.1%)	(6.5%)	(6.8%)
EMI recorded revs (£mn)	1,723	1,542	1,604	1,620	1,636	1,652	1,669
growth	(2.9%)	(10.5%)	4.0%	1.0%	1.0%	1.0%	1.0%
Royalties are c.23% dealer revenues - sales driven							
artist royalties 13.5% retail price	326	289	301	304	307	310	313
mechanical royalties at 5.4%	95	83	87	87	88	89	90
A&R function 7% revs	124	108	112	113	115	116	117
Total	544	481	500	505	510	515	520
% total	31.6%	31.2%	31.2%	31.2%	31.2%	31.2%	31.2%
Production / Distribution /Manufacturing - flexed with physical prodn							
Distribution	97	92	90	86	82	78	74
manufacturing costs	145	105	114	118	110	104	99
production costs $400k per album (studio)	85	74	77	79	80	82	84
Total	327	271	281	281	272	264	256
% total	19.0%	17.6%	17.5%	17.3%	16.6%	16.0%	15.4%
Back office / centrally allocated							
Other related costs	418	406	409	413	417	422	426
investment in IT	10						
Option costs			8	8	8	9	9
Total	428	405	417	421	426	430	435
Production related costs - driven by album production	24.9%	26.3%	25.5%	25.5%	25.5%	25.5%	25.5%
Marketing							
marketing	276	251	265	262	265	268	270
% total	16.0%	16.3%	16.5%	16.2%	16.2%	16.2%	16.2%
Total costs	1,676	1,509	1,462	1,470	1,473	1,477	1,482
net change in cost base	(46)	(166)	53	7	3	4	5
of which:							
currency	(20)	(48)	26	0	0	0	0
inflation (rate of 1.6%)	28	0	23	23	24	24	24
gross saving (note EMI has targeted £85mn between '04 and 06); 2005 saving includes cut to marketing, prodn etc. as result of delay of album releases. Some of costs go into 2006, hence the negative gross cost savings number	(54)	(118)	5	(16)	(20)	(20)	(19)
EMI profit (£mn)	147.4	132.7	141.2	150.2	163.0	175.4	187.2
Margin	8.5%	8.6%	8.8%	9.3%	10.0%	10.6%	11.2%

Source: Company Reports and Citigroup Investment Research estimates

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Publishing: Digital Beneficiary

- The mobile music market is worth around $4bn. Publishers' royalties on this should be 10% and we estimate that EMI has a 25% market share. As such, EMI should be generating close to $100m of revenues but, according to the group, currently only generates $25m. Some of this is due to piracy, but much is the lack of collection systems in digital, which should improve over time. On 24 January, the *FT* reported that EMI has signed heads of agreement for a pan-European contract which would allow a single collection society to collect royalties for all of EMI's English spoken language across Europe. This should lead to a faster and more effective collection system.
- Publishing royalty rates are already rising (and have been consistently over time). Rates are likely to continue rising as the mix shift to digital gains pace and all participants attempt to take part in the uplift in margins to recorded music as physical costs fall away.
- This is a double-edged sword for EMI, as we estimate that its Net Publishers' Share is 45% (ie 55% of revenues goes straight to the artist), but EMI is better positioned than the rest of the recorded music industry, as all the other majors are far less exposed to publishing. As such, as publishing rates move up to the cost of recorded music, their claw-back is far lower.

EMI continues to take share in publishing

EMI stated at the H1 that all its publishing royalty streams had seen growth. Given the three- to six-month lag in collections (revenue is recognised on a cash basis), we were surprised that mechanical royalties were growing given how soft the US market was in the preceding quarters. Some of this may have been due to new artists, such as *Eminem*, but we still believe like-for-like growth overall was ahead of the market.

In our view, given the positive momentum for the publishing industry in general, and for EMI in particular, this asset deserves a premium rating.

Figure 5. Music Publishing — Year-End March (£m)

Year End March (£m)	2004	2005	2006E	2007E	2008E	2009E	2010E
Underlying $ growth	(1.9%)	4.7%	3.0%	3.7%	3.8%	3.9%	3.9%
Currency impact	0.0%	(4.2%)	1.7%	0.0%	0.0%	0.0%	0.0%
Acquisition impact	1.1%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Total revenue growth	(0.8%)	0.5%	4.7%	3.7%	3.8%	3.9%	3.9%
Mechanical	199	178	180	182	184	185	187
Performance	104	106	113	119	125	131	138
Synchronisation	63	71	78	84	91	98	106
Other	32	46	48	50	52	54	57
Revenues	398	400.7	419	435	452	469	487
growth	(0.8%)	0.7%	4.7%	3.7%	3.8%	3.9%	3.9%
Direct costs	(219)	(220)	(231)	(239)	(248)	(258)	(268)
Net publisher share	179	180	189	196	203	211	219
Overheads	81	80	85	86	88	90	92
EBIT	101.9	100.2	104.1	109.5	115.2	121.2	127.7
EBIT growth	(1.5%)	(1.7%)	3.9%	5.1%	5.2%	5.3%	5.4%
EBIT margin	25.6%	25.0%	24.8%	25.2%	25.5%	25.8%	26.2%
NPS margin as % revenue	45.0%	45.0%	45.0%	45.0%	45.0%	45.0%	45.0%
Overheads growth	2.0%	(1.2%)	5.7%	2.0%	2.0%	2.0%	2.0%

Source: Company Reports and Citigroup Investment Research.

Figure 6. Music Publishing Valuation (£m)

Music publishing valuation	2005	2006E	2007E	2008E	2009E	2010E
EBITA (assumes depn equal to capex)	100	104	109	115	121	128
one third of interest	-33.4	-31.4	-30.5	-30.1	-29.7	-29.3
PBT	67	73	79	85	92	98
Tax at 30%	-20.0	-21.8	-23.7	-25.5	-27.5	-29.5
PAT	47	51	55	60	64	69
less catalogue purchase	-5.8	-7.3	-8.8	-10.3	-11.8	-13.3
less minorities (one third)	-0.4	-1.4	-1.4	-1.5	-1.5	-1.5
FCF (pre-interest)	74	74	76	78	80	83
DCF sensitivity to terminal growth rates						
Discount rate						
Present value of cash flows						
Terminal value		304	304	304	304	304
Assumed growth		1,260	1,367	1,494	1,644	1,826
PV (Terminal value)						
Total value		828	899	982	1,081	1,200
Less 2005E debt		1,133	1,203	1,286	1,385	1,505
Value of equity						
Per share (p)		846	917	1,000	1,099	1,218
		1.08	1.17	1.27	1.40	1.55
Implied EV/EBITDA multiple		10.1	9.9	10.1	10.4	10.7

Source: Company Reports and Citigroup Investment Research.

In our report '*Get Together*' (see above), we valued Warner Chappell (part of WMG) on an LBO basis at £1bn, which equated to 13x EBITDA. However, the exit multiple we used was arguably conservative at 12x, and we assumed no cost savings. Therefore, we argue that 12x-13x EBITDA for publishing assets is likely to be on the conservative side. Improvements in rates and collection could prompt a further rerating.

Valuation: Risk Reward Attractive

- We see publishing as a high multiple business, and the potential for EMI/WMG consolidation as high
- We believe downside for the stock is still meaningful should recorded music move back into decline; however, we see upside as greater given the previous point
- The key issue for EMI over the last five years has been cash generation. If we are right to think that the recorded music industry has stabilised, cash generation should improve; the major driver of this, however, is refinancing, and this remains a two- to three-year fix

Publishing and potential for consolidation make risk reward attractive

There is no question that an investment in music remains high risk. If consolidation does not occur, and the recorded music industry stutters, we believe the stock could see 170p.

Figure 7. EMI Price Parameters

	Downside	Middle	Upside	Comment
Publishing	7x NPS Mar 2007	8.5x NPS	10x NPS	Transaction multiples have been 9-11x, and this equates to 11-14x EBITDA; DCF sensitivity range is 2.5% to 4.5% l-t growth on 9% WACC
Publishing Value (£m)	1,218	1,479	1,740	
Average net debt fiscal 2006 (£m)	-950	-950	-950	
Recorded music	6x EBITDA	7.2x EBITDA	12x EBITDA	On DCF, this is range of -1% l-t growth to 4.7%, and WACC of 9%. Ie. at bottom end, flat top line for industry, inflationary costs, so no benefit on shift to digital
(£m)	1,062	1,505	2,124	
Merger	no	50% allocation	yes	
		319	637	
Total (£m)	1,330	2,122	3,551	
Per share (£)	1.69	2.70	4.52	

Source: Company Reports and Citigroup Investment Research.

In all likelihood, however, our upside scenario undercooks the true upside, as publishing acquisition multiples have come far higher than our top end, and should recorded music return to growth, there would be upside here as well.

The question of cash generation continues to dog EMI — all about recorded music revenue growth

We have EMI generating only £50-60m annually post servicing of debt and dividends. This is on average net debt, which we estimate will be close to £1bn this year. There are four factors that may affect this assumption:

- It is reliant on an absence of restructuring charges going forward, which effectively means the industry needs to have stabilised.

- As the group gradually refinances its debt, cash interest charges are likely to fall. We are arguably conservative in only slightly reducing 2007E interest relative to 2006E even though refinancing, which has already been announced, should knock £4m off the charge. Once the group has fully refinanced its debt, cash generation should rise by £20-25m. The main refinancing is May 2008 and August 2009, and we believe it will become economic to refinance these instruments (ceteris paribus rates etc) in two to three years.
- The mix shift to digital should improve cash generation as working capital requirements fade (no stock in digital and no returns). Based on our current projections of the digital mix shift, this may release £5m working capital annually.
- The group also believes there are cash handling efficiencies to be garnered.

Multiples reasonable, but admittedly not stand-out

The current P/E, 15.9x March 2007E, is not attractive in our view on a standalone basis. However, given that EMI's share of cost savings in a merger could be 45% of our forecast 2006E PBT, and given the potential operational leverage on an improving top line for recorded music, we still feel comfortable being positive on the stock.

Figure 8. EMI Valuation Multiples at Target Price

Share price EMI		270p					
number shares	Shares in issue (2005)	786					
Market capitalisation		2,121					
net debt	Net (debt)/cash (2005)	(950)					
Minorities		45					
Unadjusted EV		3,116					
Key financials		2003	2004	2005	2006E	2007E	2008E
Continuing Sales		2,175	2,121	1,943	2,052	2,084	2,117
Depreciation		43	35	24	36	36	36
Total EBITA		254	249	233	245	259	278
EBITA margin		11.7%	11.8%	12.0%	11.9%	12.4%	13.1%
EBITDA		297	284	257	280	295	314
NOPAT		180	189	175	185	194	207
Free cash flow		27	124	51	86	111	122
Per share data		2003	2004	2005	2006E	2007E	2008E
Adj EPS		15.6	16.5	13.0	14.1	15.4	16.9
	% growth	32%	-1%	-16%	8%	9%	10%
FCF per share		3.5	14.9	5.9	9.8	12.7	14.0
	% growth		329%	-61%	67%	29%	10%
DPS		6.0	8.0	8.0	7.8	8.5	9.4
	Dividend cover	2.0x	1.9x	1.6x	1.8x	1.8x	1.8x
Multiples		2003	2004	2005	2006E	2007E	2008E
EV/Sales		1.43x	1.47x	1.61x	1.52x	1.50x	1.47x
EV/EBITDA		10.5x	11.0x	12.1x	11.1x	10.6x	9.9x
EV/NOPAT		17.4x	16.5x	17.8x	16.9x	16.1x	15.1x
PE on Adj EPS		17.3x	17.5x	20.8x	19.2x	17.5x	16.0x
FCF yield		1.3%	5.8%	2.4%	4.0%	5.2%	5.8%
Group EV/EBITDA		10.5x	11.0x	12.1x	11.1x	10.6x	9.9x
Dividend yield		3.0%	3.0%	3.0%	2.9%	3.2%	3.5%

Source: Company reports and Citigroup Investment Research estimates.

Our target price of 270p is based on a 5% premium rating to the sector (ie 17.2x March 2007E P/E) justified because of the potential for consolidation. A sum-of-the-parts basis, valuing publishing at 12.5x EBITDA, would imply a value for recorded music of 9x EBITDA, which we see as fair given (a) the evidence provided which gives hope to the view the industry has stabilised, and (b) the possibility of consolidation.

Our DCF (8.8% WACC and 3% long-term growth) also drives a 270p target.

Multiples on potential WMG consolidation, even after the move in WMG and EMI's share prices, look attractive

Figure 9. EMI Capitalisation/Valuation Statistics

Capitalisation / Valuation Statistics	EMI	Warner	EMI post
Zero premium merger			
£ share price	255p	$21.0	
Number of shares - FD pre convertible	796	£11.73	
Mkt cap (m)	£2,029	154	
Split	53%	£1,809	£3,315
Net Debt	-£817	47%	
Minorities	48	-£1,116	(959.3)
EV (m)	£2,894		48
Assumed Debt from Warner	-£1,116	£2,925	£4,323
Less proceeds from WC disposal	£973		
Total Debt (m)	-£959		
Combined EBITDA	494.0		
Gear up to 3x EBITDA	£1,482		
Extra debt (m)	£523		
Equity left to finance (m)	£1,287		
NOSH to issue	505		
Total shares in issue	1,300		
Market Cap	3,315		
EV	4,323		
Value of Warner Chappel			
Publishing OIBDA	62.2		
Share of allocated costs (one third)	-10.1		
Net Publishing OIBDA	72.1		
Multiple	13.5x		
Value	£973		
Multiples	2006	2007	2008
EV/Revenues	1.2x	1.2x	1.2x
EV/EBITDA	7.0x	6.8x	6.5x
EV/NOPAT	10.9x	10.3x	8.8x
P/E	9.8x	9.1x	8.4x
FCF yield (enterprise)	-6.4%	7.9%	8.8%
FCF yield equity	-10.1%	8.7%	10.0%
Dividend yield	4.1%	4.4%	4.8%

Source: Company reports and Citigroup Investment Research estimates.

For a full explanation of this model, we refer investors back to our report '*Warner Music Group — Get Together*', published in September 2005.

EMI Financials

Figure 10. EMI — P&L (Pounds in Millions)

	2004	2005	IFRS 2006E	2007E	2008E	2009E	2010E
Recorded Music Revenues	1,723	1,542	1,634	1,650	1,666	1,682	1,699
% change	-2.9%	-10.5%	5.9%	1.0%	1.0%	1.0%	1.0%
Music Publishing Revenues	397.9	400.7	418.8	434.4	450.9	468.3	486.7
Total Revenues	2,121	1,943	2,052	2,084	2,117	2,151	2,185
Recorded Music EBITA	147	133	141	150	163	175	187
% margin	8.6%	8.6%	8.6%	9.1%	9.8%	10.4%	11.0%
Music Publishing EBITA	101.9	100.2	103.8	109.1	114.8	120.9	127.4
% margin	25.6%	25.0%	24.8%	25.1%	25.5%	25.8%	26.2%
Total EBITA	249.3	233.0	245.0	259.3	277.9	296.3	314.6
Margin	11.8%	12.0%	11.9%	12.4%	13.1%	13.8%	14.4%
Exceptional	0.0	0.0	-5.2	0.0	0.0	0.0	0.0
J/Vs & Associates	-0.3	1.1	1.1	1.1	1.2	1.2	1.3
Net Interest	-85.9	-92.1	-94.1	-91.5	-90.4	-89.2	-88.1
Adjusted PBT	163.1	141.9	151.9	168.9	188.6	208.3	227.8
Tax	-32.5	-31.4	-33.4	-38.9	-45.3	-50.0	-68.3
Tax rate	19.9%	22.1%	22.0%	23.0%	24.0%	24.0%	30.0%
Adjusted PAT	131	111	119	130	143	158	159
Minorities	-6.5	-4.3	-4.3	-4.4	-4.5	-4.6	-4.7
Adjusted Net Income	124.3	106.4	114.2	125.6	138.9	153.7	154.8
Basic shares in issue	784	786	786	786	786	786	786
Impact of convertible on share count	39	79	79	79	79	79	79
Options		8	10	10	10	10	10
FD number of shares	827	873	874	874	874	874	874
Earnings adjustment for convertible	3.5	6.9	8.9	8.9	8.9	8.9	8.9
Basic EPS	15.8	13.5	14.5	16.0	17.7	19.6	19.7
FD EPS (p)	15.5	13.0	14.1	15.4	16.9	18.8	18.7
growth			8.4%	9.3%	9.8%	10.1%	0.6%
DPS (p)	8.0	8.0	8.0	8.5	9.4	10.3	10.4

Source: Company Reports and Citigroup Investment Research.

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Figure 11. EMI — Cashflow Statement (Pounds in Millions)

	2004	2005	IFRS 2006E	2007E	2008E	2009E	2010E
Group operating profit pre exc. and amort.	249.3	233.8	245.0	259.3	277.9	295.3	314.6
Depreciation	35.0	23.9	35.0	35.7	36.4	37.1	37.9
EBITDA	284.3	258.9	280.0	295.0	314.3	333.4	352.5
Operating exceptionals	0.8	(70.7)	(15.0)	0.0	0.0	0.0	0.0
Fixed asset write backs	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Provisions created (Esop transactions)	-	10.1	0.0	0.0	0.0	0.0	0.0
Provisions used	(35.1)	0.0	0.0	0.0	0.0	0.0	0.0
Changes in working capital	60.4	25.1	0.0	0.0	0.0	0.0	0.0
Operating cash flow	309.4	221.4	265.0	295.0	314.3	333.4	352.5
Purchase of tangible fixed assets	(51.3)	(28.0)	(40.0)	(40.8)	(41.6)	(42.4)	(43.3)
Purchase of music copyrights	(5.1)	(5.8)	(7.3)	(8.8)	(10.3)	(11.8)	(13.3)
Purchase of other fixed asset investments	-	(3.2)	0.0	0.0	0.0	0.0	0.0
Sale of fixed asset investments		3.3					
Capital expenditure and financial investment	(56.4)	(35.8)	(47.3)	(49.6)	(51.9)	(54.2)	(56.6)
Operating cash flow post capex	253.0	185.8	217.7	245.4	262.4	279.2	295.9
Corporation tax paid	(30.6)	(32.7)	(33.4)	(38.9)	(45.3)	(50.0)	(68.3)
Net interest paid	(95.4)	(100.3)	(94.1)	(91.5)	(90.4)	(89.2)	(88.1)
Minority dividends paid	(3.6)	(1.3)	(4.3)	(4.3)	(4.4)	(4.5)	(4.6)
	0.0	-	-	-	-	-	-
Equity free cashflow	123.5	51.5	85.0	110.7	122.3	135.5	134.9
Acquisitions and disposals	(9.9)	(72.9)	0.0	0.0	0.0	0.0	0.0
Ordinary dividends paid	(62.7)	(63.0)	(62.6)	(61.4)	(67.2)	(73.7)	(81.2)
Dividends received	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Cash flow post servicing of finance	51.0	(84.3)	23.1	49.4	55.2	61.9	53.8
Issue of shares	0.0	-	-	-	-	-	-
(Repayment) of / increase in gross debt	185.3	0.0	0.0	0.0	0.0	0.0	0.0
Cash generation	236.3	(84.3)	23.1	49.4	55.2	61.9	53.8
Opening net debt	(859.8)	(748.2)	(829.5)	(834.4)	(785.0)	(729.8)	(668.0)
IFRS adjustment			(28.0)				
Cash generation pre adjustments to gross debt	51.0	(84.3)	23.1	49.4	55.2	61.9	53.8
Fx movement on debt	60.6	1.8	0.0	0.0	0.0	0.0	0.0
Financing	0.0	1.2	0.0	0.0	0.0	0.0	0.0
Closing net debt	(748.2)	(829.5)	(834.4)	(785.0)	(729.8)	(668.0)	(614.2)
Opening gross debt	960.5	1,145.8	1,179.8	1,130.3	1,097.4	-	-
Closing gross debt	1,145.8	1,179.8	1,130.3	1,097.4	1,049.0	-	-
Implied debt rate	8.2%	8.2%	8.2%	8.2%	8.2%	0.0%	0.0%
Interest paid	86.4	85.4	94.7	91.3	88.0	-	-
Opening cash	100.2	285.5	100.2	100.2	100.2	-	-
Closing cash	285.5	100.2	100.2	100.2	100.2	-	-
Implied cash rate	3.0%	3.0%	3.0%	3.0%	3.0%	0.0%	0.0%
Interest received	5.8	5.8	3.0	3.0	3.0	--	-
Cash dividend cover	0.8x	1.3x	NM	NM	NM	0.0x	0.0x
FCF per share	15.74	6.55	10.93	14.09	15.56	17.25	17.17

Source: Company Reports and Citigroup Investment Research.

Investment thesis

We see the impact of technology as positive for music, now that illegal downloading seems to have stabilised. The revenue model is evolving with digital download and new revenue streams like video streams. While these developments do not drive a replacement cycle, they should mitigate physical declines and possibly drive growth. Album unbundling poses risks, but we assume that consumers will spend as much on music as historically, but at a higher gross margin, on a lower fixed cost base, and in a financial model, which releases working capital. We rate EMI Buy/ High Risk (1H).

Valuation

We have a 270p price target, which is derived from a DCF based off a WACC of 8.8% and long-term growth of 3%. In 2006E, we forecast global market share increasing to 12.8% (compared to 12.5% 2005E, a level well below the 13.2% of 2004) and EBITA margins of 9.9%. At 270p, the group would trade at a March 2006E P/E of 18.3x, and a FCF yield of 4.8%. The less attractive yield relative to P/E reflects the group's catalogue acquisition. We acknowledge that to support these multiples, the market would need to have a clearer view on the long-term margin and revenue base of the group. We forecast medium-term margins of 13.5% in recorded music due to the mix shift to digital.

Risks

We view EMI as High Risk.

The risk rating on the stock is derived after consideration of a number of factors. These factors include an assessment of industry-specific risks, financial risk and management risk. In addition, we consider historical share price volatility, based upon the input of the Citigroup quantitative research team, as a possible indicator of future stock-specific risk.

With specific reference to EMI, we highlight five classes of risk:

1. There is a high level of operational and financial gearing, and this can work both ways. In particular, there is risk to our medium-term margin assumption of 13.5%. We acknowledge that the release schedule of Sony BMG will improve and make market share gains for EMI more difficult going forward, and we also acknowledge that EMI has been successful in the last two years selling multi-platinum new artists (favourable for margins as emerging stars tend to command lower royalties) and this may be difficult to repeat. The warning on EMI's global share this year gives further vent to these risks.
2. There is a risk that US and European growth remains weak.
3. Although we are positive on the move to digital, the model is very uncertain, and there is a risk that our positive view, particularly on revenue growth, could be optimistic. Linked to this, we are concerned that pricing could come under more pressure than it has in the last few years, and piracy could become a more significant negative.
4. Even if we are right, there is a risk that the artists and the A&R workforce take the upside, so margins never materialise.
5. Macro — EMI is a dollar-exposed consumer cyclical.

The above risks could cause the shares to deviate from our target price.

ANALYST CERTIFICATION

Appendix A-1

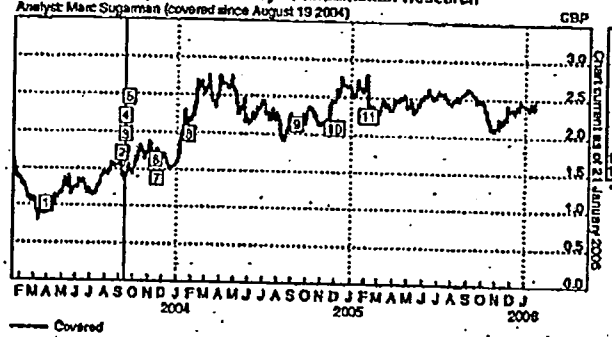
I, Marc Sugarman, research analyst and the author of this report, hereby certify that all of the views expressed in this research report accurately reflect my personal views about any and all of the subject issuer(s) or securities. I also certify that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

IMPORTANT DISCLOSURES

EMI (EMI.L)

Ratings and Target Price History - Fundamental Research

Analyst: Marc Sugarman (covered since August 19 2004)



#	Date	Rating	Target Price	Closing Price
1:	28 Mar 03	2H	*1.15	0.93
2:	5 Sep 03	2H	*1.40	1.39
3:	12 Sep 03	Stock rating system changed		
4:	12 Sep 03	*2M	*1.40	1.41
5:	22 Sep 03	2M	*1.50	1.52
6:	17 Nov 03	2M	*1.60	1.55
7:	19 Nov 03	2M	*1.90	1.79
8:	28 Jan 04	2M	*2.10	2.18
9:	10 Sep 04	2M	*2.30	2.14
10:	29 Nov 04	*1H	*2.80	2.46
11:	8 Feb 05	1H	*2.70	2.37

*Indicates change.

—— Covered
------ Not covered

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Data current as of 31 December 2005

	Buy	Hold	Sell
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% of companies in each rating category that are investment banking clients	47%	48%	37%
Media–General – Europe (40)	43%	48%	10%
% of companies in each rating category that are investment banking clients	41%	42%	50%

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