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October 22, 1997

Ms. Blanca Bayo, Director  
Division of Records and Reporting  
Florida Public Service Commission  
2540 Shumard Oak Boulevard  
Tallahassee, Florida 32399-0850

via Hand Delivery

Re: Applications for Authority to Provide  
Interexchange Telecommunication Service  
Within the State of Florida for Time Warner — 904 1393 - 10564 - 001  
Communications and Digital Media Partners — 904 1392 - 10563 - 007

Dear Ms. Bayo:

Enclosed for filing and attachment to the above-described applications, which were filed Monday, October 20, 1997, please find twelve copies of Exhibit A. Please date-stamp the copy of this letter to indicate that the original was filed and return to me.

If you have any questions regarding this matter, please feel free to contact me.

Very truly yours,

Robert S. Cohen

- ACK \_\_\_\_\_
- AFA   1
- APP \_\_\_\_\_
- CAF \_\_\_\_\_
- CMU \_\_\_\_\_
- CTR \_\_\_\_\_
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# 1994 Annual Report

## Contents

### CHAIRMAN'S MESSAGE

*Time Warner is uniquely positioned to reap the benefits of the telecommunications revolution and worldwide demand for software.*

### A WORLD OF CHANGE

*The globalization of commerce and the accelerating power of communications technology are fundamental and irreversible.*

### TIME INC.

*Time Inc. owns the world's premier collection of publishing brands and information franchises.*

### MUSIC

*Warner Music Group is the world's most diversified, vertically integrated and profitable music company.*

### FILMED ENTERTAINMENT: WARNER BROS.

*Warner Bros. is the world's foremost producer and distributor of movies, TV programming and home video.*

### FILMED ENTERTAINMENT: SIX FLAGS

*Six Flags theme parks soared to new heights in family entertainment.*

### HBO-PROGRAMMING

*With quality programming, innovative marketing and a revitalized pay-TV environment, Home Box Office hit double-digit growth.*

### CABLE

*Time Warner Cable is the cable company best positioned to enter the new age of telecommunications.*

### OTHER INVESTMENTS

*Companies in which Time Warner has a financial stake.*

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View sections of the annual report that cover other Time Warner divisions

- WARNER MUSIC GROUP
- TIME WARNER CABLE
- WARNER BROS.
- TIME INC.



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- SIX FLAGS

- HBO

Or return to:

- THE OFFICIAL WORD HOMEPAGE



Gerald M. Levin  
Chairman and CEO

# Dear Shareholders:

**Record Earnings**  
**Cable's Clear Advantage**  
**Copyright Plus Distribution**

**In 1994 the proliferation of new technologies and the spread of free-market economic systems continued to expand the voracious global appetite for Time Warner's products. In terms of technology, the cable industry is now leading the telecommunications revolution, changing forever how consumers receive information and entertainment. With Time Warner leading the cable industry, we are positioned to become a major player in delivering the full range of telecommunication services.**

*Time Warner is uniquely positioned to reap the benefits of the telecommunications revolution and the worldwide demand for software. No competitor can match the scope of our copyrights and distribution networks.*

**Amid all these changes one thing remains the same. The ultimate test of every business—the measure of its strength and the proof of its leadership—is performance. This is where strategy is tested by reality and the validity of a company's vision is either confirmed or repudiated.**

**For the year, Time Warner's content businesses—Time Inc., Warner Music Group, Filmed Entertainment (including Warner Bros. and Six Flags), and Home Box Office (HBO)—achieved combined double-digit growth and record earnings before interest, taxes, depreciation and amortization (EBITDA). Due to the impact of government rate regulation, Time Warner Cable experienced an overall decline, which had a negative impact on our stock and the stock of every major cable player. Cable, however, has worked its way through the worst effects of re-regulation and in the fourth quarter showed an increase in EBITDA for the first time since 1993.**

**The creative soul of Time Warner is most often described as residing in our content or copyright businesses. These are hugely successful enterprises that can be imitated but never duplicated. In franchises such as Time, People, Sports Illustrated, Book-of-the-Month Club, Time-Life Books, Warner Bros. Records,**



**Elektra, Atlantic Records, HBO, Warner Bros., Looney Tunes, DC Comics-the list is long- we possess not just lucrative brands but American cultural icons. They are Time Warner's alone.**

**A brand's power lies in the certainty that it will deliver value day after day, year after year. In the information and entertainment industry, this certainty isn't a function of a standardized manufacturing process but of highly talented journalists and artists gifted with the ability to reach minds and touch hearts. Past, present and future, these women and men are the source of our success.**

**The myriad acts of creation that define and distinguish Time Warner don't take place in a vacuum. From the beginning, this has been a company with a profound sense of the importance of controlling distribution in generating more business, keeping a larger share of the profits and creating products that increase consumers' understanding and enjoyment. Distribution is an essential part of who we are and what we do.**

**Together, content and distribution are at the center of our strategic mission: Time Warner is home to the world's premier journalists and creative artists. We distribute the products of their minds and imaginations to the broadest audience across the globe. This combination of strengths is reflected in our 1994 performance.**

## **Record Earnings**

**In publishing, Time Inc. produced double-digit EBITDA growth and record results. Among the ingredients in its success were circulation and advertising growth, impressive rate-base increases at Entertainment Weekly, Parenting, Cooking Light, Martha Stewart Living, and Sports Illustrated For Kids, and ongoing cost management. By any standard Time Inc. remains the industry leader. It is also becoming a major presence in the development of software for new media. Already a leading direct marketer of books, music and video, Time Inc. is repackaging its copyrights for resale as CD-ROMs and through online services.**

**Warner Music Group's eleventh straight record year reinforced its position as the world's No.1 music company. Vertically integrated, in charge of its own manufacturing and distribution, this is a truly global operation. The Group's non-U.S. businesses, now accounting for over 50% of its revenues, have a ten-year compound annual growth rate of better than 20%. Here in the U.S., Warner Music labels continue to hold by far the strongest position on the music charts. A quarter of the titles in Billboard's top-200-selling albums for the year were from the Group's artists. The Group's roster of worldwide-selling artists included All-4-One, Anita Baker, Eric Clapton, Green Day, Luis Miguel, John Michael Montgomery, R.E.M., Stone Temple Pilots, Mariya Takeuchi and The**

### 3 Tenors.

Driven by the success of films such as *Interview With the Vampire*, *Maverick*, *The Client* and *Disclosure*, Warner Bros. had its twelfth straight year of record results. Warner Bros., however, is more than just the world's most consistently successful film studio. Warner Bros. Television is the leading creator of primetime programming, including breakout hits *ER* and *Friends*. The 1995 launch of The WB Network demonstrates our commitment to build a primetime broadcast outlet for our new and classic copyrights. WB Studio Stores are continuing to open new outlets in America and overseas. Warner Bros.' investment in a theatrical animation business promises to bring the Studio the same level of quality and success in animated features that it now enjoys in every other area of family entertainment.

For HBO and Cinemax, 1994 was a championship season. At year-end, their subscriber count was up 2.3 million from 1993, the largest increase in over a decade. As well as winning new subscribers, HBO scored 23 CableACE Awards, far more than its nearest competitor, and four Golden Globe Awards, more than any broadcast network. HBO's growth comes from a number of factors. Multichannel HBO and Cinemax, for example, have improved penetration. The introduction of HBO en Español has resulted in double-digit subscriber growth in a demographic segment increasing at five times the general rate.

Our four content businesses had a year of unqualified success. Each is positioned for double-digit growth well into the future.

### Cable's Clear Advantage

Time Warner Cable has absorbed the pain of rate re-regulation and is now moving beyond it. In the fourth quarter of this year, we expect the cable company to return to a double-digit growth rate and to deliver consistent double-digit growth in 1996 and beyond. Driving that growth was a healthy increase in subscribers in 1994. Another key to growth is that cable has won the race to be the first to bring broadband, digital interactivity into America's homes and businesses. This isn't a boast. It's a simple technological fact.

*As regulatory barriers fall, cable will be in the telephone business long before the phone companies are in cable's....By emphasizing our ability to package TV and telephone services, we intend to go after the 20% of the telecommunications market that generates 80% of the revenues.*

There has been a good deal of confusion over which industry-cable or telephone-has the competitive advantage in offering consumers telephone and video services. There shouldn't be. Cable already has in place the basic wiring for delivering programming services and true video on demand. Adding

telephony to our basic cable services is a relatively small step. In contrast, to add video capacity to their primary business, the phone companies face the immensely expensive, time-consuming job of bringing broadband to local neighborhoods. As regulatory barriers fall, cable will be in the telephone business long before the phone companies are in cable's.

Compared to other cable operators, Time Warner Cable possesses another crucial strength: clustering. Over the years, Time Warner's strategy of concentrating its systems in densely populated urban and suburban markets has made it far and away the best-clustered systems operator. In late 1994 and early 1995, the cumulative impact of fast-developing technological innovations, the convergence of the cable and telephone industries and rate re-regulation resulted in several well-situated, demographically attractive cable systems becoming available for acquisitions or joint ventures. Presented with the chance to strengthen our clusters and complete our cable footprint, we seized it.

Our agreements to enter a joint venture with Advance/Newhouse and to acquire KBLCOM, Cablevision Industries and Summit will dramatically expand our cable presence in New York, Florida, North Carolina, Ohio and Texas. Once the deals close, our systems in these states will serve over six million of our 11.5 million subscribers, with nearly three-quarters of our customers in 34 geographic clusters of 100,000 or more.

Near term, the investments in enhancing our clusters and upgrading their architecture will bring immediate access to new revenues through more reliable service—thereby increasing penetration and decreasing customer churn—and through expanded pay-per-view and targeted advertising packages. In addition, for a relatively small incremental investment, we will enter the \$100-billion-a-year local telephone industry, a step that we will take later this year in Rochester, New York. By emphasizing our ability to package TV and telephone services, we intend to go after the 20% of the telecommunications market that generates 80% of the revenues.

Time Warner has already entered the \$28-billion-a-year long-distance-access business. We now provide companies in twelve locations across the country with connections to their long-distance carriers, as well as data-transport services. Our presence expanded rapidly in this part of the telephone business in 1994, and we expect the growth to continue.

Long term, new revenue streams will come from the introduction of interactive services. We know that Time Warner will be both a beneficiary and a creator of the interactive future. This was made clear on December 14, 1994, in Orlando, Florida, when Time Warner introduced the Full Service Network™ (FSN) and successfully demonstrated its capability to deliver movies on demand video games and home shopping services.

## Copyright Plus Distribution

Time Warner is uniquely positioned to reap the benefits of the telecommunications revolution and the worldwide demand for software.

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### *Time Warner Senior Management*



*(left to right) Norman Pearlstine, Don Logan, Reginald K. Bruck, Robert W. Pittman, Gerald M. Levin, Richard D. Parsons, Robert J. Morgado, Robert A. Daly, Joseph J. Collins, Terry S. Semel, Jeffrey L. Bewkes, Michael J. Fuchs.*

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No competitor can match the scope of our copyrights and distribution networks. But our leadership isn't a matter of coasting on the momentum of past success.

We are putting in place a new generation of executive talent. At Corporate, Dick Parsons, our new President, and Rich Bresler, our new Chief Financial Officer, bring depth, vision and enthusiasm. Our divisions have long been recognized for the quality and stability of management. The appointments of Don Logan as Time Inc. CEO and Norman Pearlstine as Editor in Chief—the first from outside the Time & Life Building—add new perspectives and abilities to our publishing operations. Warner Music Group has a new divisional head of its U.S. operations, Doug Morris, and n

*The future belongs to those who refuse to be mere caretakers, who insist on finding newer, better, more efficient, more responsive, more imaginative ways to serve their audiences.*

Going forward, we are committed to achieving three strategic objectives that will solidify the progress we've already made and ensure we remain the global leader in media and entertainment. The first is financial restructuring. We will pursue simplification of our corporate structure by creating a stand-alone, self-financing enterprise to manage our cable and telecommunications properties. This new enterprise will help Time Warner exploit its crucial technological advantage and help shareholders evaluate both sides of the company—content creation and distribution; and telecommunications.

Second is improving our financial strength. As part of a continuing reassessment of where individual parts of our core businesses fit into our mission, we will offer for sale carefully targeted, non-strategic assets from both the cable and content sides. The proceeds will be used to reduce debt. Third, we will continue to make strategic investments for growth. Over the past few years, at the same time as we've completed our cable footprint and upgraded our systems, we've invested aggressively in all our content businesses. This includes the start-up of Entertainment Weekly; the creation of a theatrical animation business; the launch of a "fifth" network; the international expansion of HBO; and the entry of Warner Music Group into new forms of direct marketing and overseas music channels.

Each of these investments is adding to the creative strengths of our divisions and underlines their importance to our future. In today's competitive environment, the willingness to invest in sustained growth-growth that builds on itself from year to year-is more necessary than ever.

As always, the future belongs to those who refuse to be mere caretakers, who insist on finding newer, better, more efficient, more responsive, more imaginative ways to serve their audiences. The keys are the willingness to be an agent of change, the ability to nurture creativity, and the discipline to pay careful attention to business fundamentals.

The combined forces of technology and globalization will continue to transform the face of the media and entertainment industry. The pace will only increase. Yet no competitor possesses the resources Time Warner does: the talent and the creativity; the libraries of copyrighted images, stories, music and films; the scope of distribution and marketing prowess; the commitment to innovation; or the global reputation for the best in information and entertainment. We remain the one company with the power to shape the future as well as profit from it.

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View sections of the annual report that cover other Time Warner divisions:

- WARNER MUSIC GROUP
- TIME WARNER CABLE
- WARNER BROS.
- TIME INC.
- SIX FLAGS
- HBO

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# A World Change

## Opening Markets The Digital Decade Brands in Demand

*Today's media and entertainment industry--shaped by opening global markets, a revolution in digital technology and the growing value of powerful brands--looks very different than it did ten years ago. In another decade, it will be unrecognizable.*

*The forces that are molding our collective future--the globalization of commerce and the accelerating power of communications technology--are fundamental and irreversible. Combined with underlying demographic trends and the spread of copyright protection, these forces are creating not just new industries but a new economy. It is an economy based on intellectual property...and intellectual capital. An economy in which the lingua franca is the digital bit...and in which the ability to coin words and ideas, to create images and music, is the coin of the realm. No company faces this changing world with more hope or better prospects than Time Warner....*

\* \* \* \* \*

## Opening Markets



Creating Free Markets and Protecting Creativity  
Youth + New Media = Worldwide Growth



*The next decade presents one of the most significant international business opportunities in history. Every day, more and more countries are opening their doors wider to fresh ideas, new opportunities and the energizing force of the free marketplace. People in every corner of the globe are waking up to more and more options in the information and entertainment they can receive and enjoy.*

## No. 1 in the World

If Time Warner's international operations were a stand-alone business, that business would rank as the 130th largest company on the *Fortune* 500. Time Warner's international divisions bring in more revenue and EBITDA than the non-U.S. media and entertainment operations of any other corporation in the world. Time Warner's overseas revenues have grown from less than \$740 million in 1984 to more than \$4 billion in 1994. That's a compound annual growth rate of nearly 20%.

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*In 1970 Warner Music Group did business in three countries. Today it operates in more than 65 and is Time Warner's largest global business. Non-U.S. markets generate 57% of its recorded-music revenues.*

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In the decade ahead, this growth rate is expected to accelerate.

Why? Because of a worldwide pattern of economic, political and demographic trends. The rapid development of market economies, spreading copyright protection, the growth of younger population segments and the widespread adoption of new communications technologies--all these developments are both fundamental and irreversible. And all bode extremely well for Time Warner.

## Creating Free Markets and Protecting Creativity

State-controlled economies are rapidly giving way to the free market. Time Warner--with the world's premier collection of journalists and creative artists, unsurpassed marketing expertise and global distribution networks (e.g., Warner Bros. controls more of its worldwide distribution than any other studio)--is poised to enter promising new markets, from Eastern Europe to the Pacific Rim.

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*Who, the Australian version of People, is that country's fastest-growing magazine.*

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Protection of intellectual property is making significant progress in many markets around the world. In Singapore, for instance, our industries' losses from piracy have dropped from an estimated \$358 million in 1984 to \$27 million in 1993. China recently signed a major intellectual property agreement with the U.S. Time Warner is the world's leading owner and creator of copyrights and brands—from Bugs Bunny to HBO Ole, from the premier portfolio of publishing titles to the largest library of music copyrights. We benefit directly and materially everywhere intellectual property is strengthened and piracy is thwarted.

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*In 1994 Warner Bros. struck a trail-blazing deal to distribute films in China.*

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## Youth + New Media = Worldwide Growth

Young people are the most voracious consumers of media and entertainment products, and their numbers are growing throughout the world. In India, for example, the 18-24 age group is expected to grow 18% between 1992 and the year 2000, resulting in a population segment of 314 million. In Brazil the same age group is expected to grow 17%, to 53 million. At the turn of the century, the world may be home to a prime movie, television and music audience that is larger than today's by more than a billion people.

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*Through television, video, licensing and retail, Warner Bros.' Looney Tunes characters are known and loved worldwide.*



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The world circa 2000 will also contain one billion television households. Technology is revolutionizing the information, entertainment and communications industries, and no media and entertainment company has so effectively turned technology into businesses around the world as has Time Warner. Warner Home Video is the world's leading home video distributor (and is pioneering the next generation of digital storage, the digital video disc); Warner Music Group is among the world's leading suppliers of CDs and audiotapes; Warner Bros.

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*Warner Music Group's joint-venture VIVA--a hit in Germany-- is a model for music-video channels around the world that will emphasize local artists.*

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Television is the world's leading producer and distributor of television programming; and Time Warner Cable, the world's leading cable operator in both clustering and technology, is moving aggressively to expand its international presence, including recent deals in China, Japan, Spain, France and Taiwan. The world is changing. No company faces this changing world with better prospects than Time Warner.

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**Cable Telephones and Digital Movies**  
**The Full Service Network**

The power of digital technology is transforming the way people communicate. Every day, new advances are expanding the amount and quality of the information and entertainment that society creates and receives. More important, these advances are giving each of us more control, more ways to shape communications to our own needs. We're moving from the broadcast world...through a narrowcast phase...and into a new world of individual interaction, personal

expression and choice.

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*Time Warner's Full Service Network (TM) provides true video-on-demand, interactive shopping and games--with full VCR functionality.*

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## No. 1 in Applying New Technology

No media and entertainment company has been as consistently prescient in its development and use of new technology as Time Warner. Our company pioneered the synchronized talking motion picture...satellite-delivered pay television...broadband fiber-optic/coaxial-cable architecture (winner of the cable industry's first-ever technology Emmy Award)...selective magazine binding and ink-jet printing...inter-active multimedia based on magazines, books and entertainment (via CD-ROM, home games and online services)...cable-delivered telephony...local-news video-journalism...the next generation of home entertainment, the digital video disc (DVD)...and the world's first digital, switched, interactive communications system, the Full Service Network™(FSN). As profound as the impact of new communications technologies has already been, in the decade ahead their transforming power will increase exponentially.

## Cable Telephones and Digital Movies

The digital broadband revolution is not years away; it's happening now. Not only can technologically advanced cable systems like Time Warner's offer enhanced pay-per-view and numerous new viewing options, but they can also provide advanced voice and data connections significantly sooner than regional telephone companies-with their existing plant based on low-capacity copper wire-will be able to offer video.

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*Time Warner's joint-venture The Sega Channel is the first truly interactive cable service, supplying 50 video-game hits like Sonic the Hedgehog for a monthly fee.*

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At each stage of a cable system's upgrade, significant new revenue streams are created. Perhaps the most promising is telephony. The local telephone business in the U.S., including access to long distance, currently brings the regional Bell operating companies \$100 billion a year. Aided by its strategic partnership with U S WEST, Time Warner is already in the telephone business today. As the result of agreements entered into in 1994 and early 1995, we expect to expand our cable footprint substantially in 1995, positioning the company to realize significant revenues from telephony in the years ahead.

Digitization is enhancing both networks and hard-copy formats. Case in point: the digital video disc. This technological breakthrough, announced January 24, 1995, by Time Warner and Time Warner Entertainment partner Toshiba, multiplies by 15 the storage capacity of today's audio CD (or multimedia CD-ROM). Not only will this high-powered disc permit affordable digital versions of movies superior in quality to 12-inch laser video discs--promising to supercharge the selling of films directly to consumers--but it will also provide a potent new storage device for computers, direct-broadcast satellite services and even interactive systems like Time Warner's FSN.



*The Time Warner/Toshiba digital video disc has won widespread support from Hollywood studios and consumer electronics manufacturers alike (left).*

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## The Full Service Network

The broad outlines of the digital revolution are becoming clear. It even has a name--the Full Service Network--and a prototype, currently operating in Orlando, Florida. Time Warner's FSN is widely acknowledged to be the most advanced communications system ever deployed to the consumer--and the only two--way, switched, digital interactive system currently in operation. It is, in fact, a real-world laboratory for the digital age, providing Time Warner and its partners with invaluable insights into the capabilities of the technology and consumer needs and preferences.

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*Time Warner is aggressively entering the telephone marketplace--both business and residential--through such ventures as Time Warner Cellular in Rochester, New York.*

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The long-prophesied convergence of computers, telecommunications and content is under way, and at a dizzying pace. The rule of thumb is called "Moore's Law": Every 18 months computing power doubles and its cost decreases by half. Time Warner-with the premier collection of clustered technologically sophisticated cable systems and the world's largest portfolio of information and entertainment copyrights and brands-is poised both to drive and to profit from this accelerating change.

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**Trusted Titles and Favorite Songs**  
**Classic Characters and Unmatched Programming**

*In a world of proliferating choice, popular brands are the key to global success. Every day, consumers are offered more and more channels of information, entertainment and communication. These range from television, music, books, magazines, movie theaters, theme parks, retail stores and catalogs, to phones, online services, multimedia CD-ROMs and interactive cable. And the list is growing. When faced with such a welter of options, people will gravitate to the brands they know and trust.*

# No.1 in Brands and Copyrights

Time Warner creates and owns more information and entertainment copyrights and brands than any other company in the world, and it markets them with unsurpassed skill.

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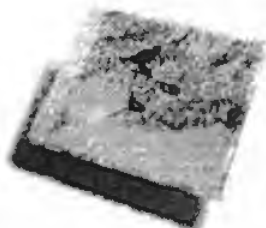


*Time Warner's unmatched storehouse of copyright assets includes such widely recognized world-class brands as HBO.*

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Intellectual property is not created on an assembly line. It is created one song or story or image at a time, by unique individuals. The key to managing enterprises like ours is to find the best creative people and build long-term relationships with them. Year-in and year-out, Time Warner has done that better than any company in the world. We invented the newsmagazine and the talkie; established modern photojournalism, personality journalism and the personal finance magazine; set the standard for pay-TV programming; led the music industry into modern rock and rhythm & blues; and created the comic-book superhero. And in every area of Time Wa

As valuable as Time Warner's copyrights and brands have been in the past, their worth will be multiplied in the decades to come.



## Trusted Titles and Favorite Songs

Time Inc. owns the most preeminent portfolio of brand names and powerful franchises of any publishing company in the world--from trusted magazine titles like *Time*, *People*, *Sports Illustrated*, *Fortune*, *Money*, *Life*, *Entertainment Weekly*, *Martha Stewart Living* and *Southern Living*, to leading direct-marketers of books, music and video, Time Life and Book-of-the-Month Club. These renowned brands are constantly being extended into profitable new products that leverage the company's editorial and marketing expertise--everything from *SI For Kids* to *Time Online*, from Children's BOMC to Oxmoor House's *Southern Living Annual Recipes*.

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*Sports Illustrated--named by Advertising Age as "Magazine of the Year"--is a powerful franchise with many profitable extensions, from special editions and spin-off titles to videos and multimedia.*

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Warner Music Group (WGM) includes the world's largest holder of music copyrights, Warner/Chappell music publisher, owner of more than a million musical favorites from *Rhapsody in Blue* to ñHappy Birthday to You.î And WGM's labels dominate the charts with the premier roster of U.S. and international musical superstars, from You.î And WGM's labels dominate the charts with the premier roster of U.S.

## Classic Characters and Unmatched Programming

Warner Bros.' unique libraries contain more than 3,000 feature films and more than 25,000 television episodes. They also include such beloved Looney Tunes characters as Bugs Bunny, Daffy Duck and Tweety Bird; newer favorites like the denizens of *Tiny Toons* and *Animaniacs*; and classic DC Comics characters such as Superman, Batman and Wonder Woman. These evergreen trademarks and one-of-a-kind copyrights are an unending source of new products and revenues: everything from worldwide home video sales to consumer products, from the Batman movies to Batman The Ride at Six Flags Theme Parks.

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*DC Comics characters like Batman are more than comic-book superheroes. They are American icons who regularly make the leap into new media.*

*Warner Bros.' Looney Tunes characters like Marvin the Martian are an evergreen source of licensing revenues worldwide*

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HBO's brand awareness in the U.S. is near the highest levels possible and is being rapidly exported around the world. The power of the HBO brand is constantly being enhanced by the company's marketing prowess and its established reputation as the creator of the best original

programming on television.

The world of media and entertainment is changing. No company faces this changing world with better prospects than Time Warner.

★ ★ ★ ★ ★

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# Time Inc.

*Time Inc. owns the world's premier collection of publishing brands and information franchises.*

Tops in the Trade  
Variety and Innovation  
A World of Books and Direct Marketing  
1995 Best Sellers

With double-digit earnings growth and innovative product extensions in 1994, Time Inc.--already the preeminent magazine publisher in America and a leading direct marketer of books, music and video--strengthened its position as a broad-based information company. Thanks to its array of creative resources, an existing infrastructure to develop and support multiple new products and ongoing cost management, the company expects continued improvement in its profits.

In 1994 Time Warner's Publishing division reported an increase of 16% in EBITDA to \$430 million, from \$372 million in 1993, a record for continuing operations. Contributing to this excellent performance was healthy growth in operating income by the company's major magazines. Emerging along with the rest of the industry from a protracted advertising slump, Time Inc.'s advertising revenues remained more than double those of its closest competitor in magazine publishing.

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## Publishing - Financial Highlights

<i>(in millions)</i>	<i>1994</i>	<i>1993</i>
Revenues	\$3,433	\$3,270
EBITDA	430	370

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# Tops in the Trade

In 1994 Time Inc.'s collection of 24 leading general-interest, regional and lifestyle magazines showed overall increases in both circulation and advertising revenue. The company held the No. 1 or No. 2 spot in most major ad categories, including automotive, computers and toiletries/cosmetics. At the same time, the company's dependence on the cyclical advertising marketplace continues to decline (from about 40% of total revenues a decade ago to about one-third today) through the growth of more stable revenue streams such as circulation and direct marketing.

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## Time Inc.'s Magazines

*Time*  
*Fortune*  
*Life*  
*Sports Illustrated*



*People*  
*Sports Illustrated For Kids*  
*Entertainment Weekly*  
*In Style*  
*Southern Living*  
*Progressive Farmer*  
*Southern Accents*  
*Cooking Light*  
*Parenting*  
*Baby Talk*  
*Barbara Stewart Living*  
*Sunset*  
*Health*  
*Hippocrates*  
*Asiaweek*  
*President*  
*Dancyu*  
*Who*  
*Vibe*

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The benefits of Time Inc.'s 1993 reorganization were evident in 1994 in solid performances by core franchises and numerous product extensions. *Time*, the world's leading newsmagazine, reinforced its position as the preeminent news journal in cyberspace by supplementing *Time* Online with *Time* Daily on both America Online

and the company's new *Pathfinder* site on the Internet.

*Sports Illustrated* marked its 40th anniversary with special editions; a primetime TV special; expansion of targeted selective-edit projects like "NFL Plus," "Golf Plus," and special collector's editions; and the launch of SITV, which produced regular segments for *ABC's Wide World of Sports. People*, reaching 30 million readers a week, celebrated its 20th birthday with a record-breaking special anniversary issue and a highly rated TV special, and expanded its franchise with the success-ful launch of a monthly celebrity lifestyle magazine, *In Style*.

*Money* enhanced its position as the nation's leading personal finance publication by debuting rapidly growing newsletters for retirees and 401(k) plan participants. *Fortune*, which received its second National Magazine Award in 1994, had an exceptionally strong year, fueled by substantial increases in advertising revenues. *Life* expanded its franchise with special single-subject issues, *Remembering Jackie* (later published as a book by Warner Books) and *The Roots of Country*. Impressive increases in guaranteed circulation were announced in 1994 by *Entertainment Weekly* (to 1.125 million), *Parenting* (to 1 million) and *Sports Illustrated For Kids* (to 950,000), and in 1995 by *Martha Stewart Living* (to 1.2 million), the magazine's seventh rate-base increase in four years.

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#### 1994 U.S. Magazine Industry Ranking

	1994 Rank	1994 Advertising Revenues
PEOPLE	1	\$382.8 million
Sports Illustrated	2	\$366.2 million
TV Guide	3	\$365.1 million
TIME	4	\$361.6 million

Source: Publishers Information Bureau

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Although best known for its national magazines, Time Inc. is also America's leading regional magazine publisher. In 1994 *Sunset*, the No.1 Western U.S. lifestyle magazine, increased its readership to more than six million. Southern Progress Corp. (SPC) enjoyed a record-breaking year, with revenues from each of its titles--*Southern Living*, *Progressive Farmer*, *Southern Accents* and *Cooking Light*--reaching all-time highs. SPC's book publishing arm, Oxmoor House, also achieved record results and placed its first book on the New York Times best-seller list, *The Bubba Gump Shrimp Co. Cookbook*.

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Time-Life Video has built a successful business marketing a wide

variety of video series. Nearly five million tapes were sold in 1994.

---

## Variety and Innovation

Time Inc.'s journalistic expertise is an invaluable resource for the coming "information superhighway," evident in 1994 in numerous digital interactive publications in both CD-ROM and online formats. Building on the experience of *Time Online*-the first national newsmagazine to be available interactively and still the most popular online magazine-the company launched *Pathfinder*, an Internet site that provides text, photos, graphics, audio and video from *Time*, *Sports Illustrated*, *Money*, *People*, *Vibe*, *Entertainment Weekly*, *Sunset*, *Southern Living*, *Time Life*, Warner Books, Little, Brown and other Time Warner divisions.

By March 1995 *Pathfinder* was receiving more than three million requests for material each week. Other online services announced in 1994 were from *Sports Illustrated*, *SI For Kids*, *People*, *Fortune*, *Money*, *Hippocrates* and *Entertainment Weekly*, which also began the first review section in any weekly magazine covering multimedia. Finally, the company is collaborating with Time Warner Cable to create The News Exchange, an interactive news-on-demand service for Time Warner's Full Service Network.

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*Time Inc. has a strong, varied presence in the world of interactive multimedia-from CD-ROMs based on the company's magazines to one of the most-visited sites on the Internet (right).*

---

In September Time Telepictures Television, a collaboration between Time Inc. and Warner Bros., launched *EXTRA-The Entertainment Magazine*, a six-times-weekly entertainment-news broadcast that is earning the highest ratings of any new 1994-95 series in syndication. Time Telepictures also produced successful ABC specials based on *Sports Illustrated* and *People*. Martha Stewart Living Television saw continued ratings and revenue growth for its syndicated series. And Time Inc.

announced *Your Mind and Body*, a new weekly half-hour syndicated fitness program to be based on Time Inc. Ventures' award-winning *Health* magazine.

## A World of Books and Direct Marketing

Time Inc.'s direct-marketing and book companies distributed 159 million units worldwide in 1994. Time Life had several million-plus sellers, including *Weight Watchers*® *Smart Choice Recipe Collection* from Time-Life Books, *Sounds of the '70s* from Time-Life Music and *Predators of the Wild* from Time-Life Video. Time-Life Digital was created to produce multimedia products based on Time Life's extensive source material, and Time-Life Medical was formed (with partners including forneDigital was created to produce multimedia products based on Time Life's extensive source

Book-of-the-Month Club's (BOMC) dramatic improvement was driven by a record year for Quality Paperback Book Club, which celebrated its 20th anniversary, and continued record performances by Children's BOMC and History Book Club. In addition, BOMC's international business expanded into more than 40 countries.



*Book-of-the-Month Club isn't just best-sellers. America's oldest book club has diversified into seven separate clubs.*

Time Inc.'s trade publishing imprints enjoyed a banner year on the best-seller lists. Warner Books' *The Bridges of Madison County* by Robert James Waller continued as the fiction phenomenon of the '90s, extending its run on the *New York Times* hardcover best-seller list to 134 straight weeks as of March 5, 1995 (with another boost expected this summer upon the release of Warner Bros.' film starring Clint Eastwood and Meryl Streep). Other successful Warner Books titles included Waller's *Slow Waltz in Cedar Bend* and James Redfield's *The Celestine Prophecy*. Little, Brown's trade division published best-sellers like Allan Folsom's *The Day After Tomorrow* and Nelson Mandela's *Long Walk to Freedom*.



Time Warner's trade publishers, Warner Books and Little, Brown, have been on a roll. Best-sellers in 1994 included James Patterson's *Kiss the Girls*, Nelson Mandela's *Long Walk to Freedom* and James Redfield's *The Celestine Prophecy*.

---

## 1994 Best-Sellers

### Book-of-the-Month Club

*Debt of Honor*, Tom Clancy  
Toni Morrison Set

### Time Life

*Sounds of the '70s*, Time-Life Music  
*Weight Watchers® Smart Choice Recipe Collection*, Time-Life Books

### Little, Brown

*The Day After Tomorrow*, Allan Folsom  
*Long Walk to Freedom: The Autobiography of Nelson Mandela*

### Warner Books

(hardcover) *The Celestine Prophecy*, James Redfield  
(paperback) *Pleading Guilty*, Scott Turow

### Oxmoor House

*The Bubba Gump Shrimp Co. Cookbook*  
*Southern Living 1994 Annual Recipes*

### Sunset Books

*Starbucks Passion for Coffee*  
*Sunset Recipe Annual 1994*

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*Warner Music Group is the world's most diversified, vertically integrated and profitable music company.*

Around the Globe and Across the Street

The Product is Talent

Warner Music Group

New Voices, New Market

Warner Music Group (WMG) achieved its eleventh consecutive year of record EBITDA in 1994, posting a 12% increase, to \$720 million from \$643 million in 1993, with double-digit growth in domestic and international recorded-music sales, worldwide music-publishing and direct-marketing revenues. Warner Music Group's multi-national family of labels boasts a roster of artists ranging from Green Day to Anita Baker, from Japan's Mariya Takeuchi to Stone Temple Pilots.

WMG also includes Warner/Chappell, the largest music publisher in the world; half ownership of Columbia House, the world's largest music and video club; and peerless manufacturing facilities and distribution networks, which it is leveraging to establish itself in such growing entertainment businesses as home video, audiobooks and interactive multimedia.

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## Music - Financial Highlights

<i>(in millions)</i>	<i>1994</i>	<i>1993</i>
Revenues	\$3,986	\$3,334
EBITDA	720	643

---

## Around the Globe and Across the Street

With more than 57% of its recorded-music revenues coming from non-U.S. markets, Warner Music Group is Time Warner's most global division, conducting business in more than 65 countries. The overseas affiliates of Warner Music International (WMI) are full-service, indigenous music companies. Dual marketing operations around the



world enable these companies to build the careers of their local artists, while also expanding sales for the Music Group's U.S. and transnational superstars.

In 1994 WMI expanded its reach by establishing Warner Music Thailand and acquiring leading Thai independent labels D-Day Entertainment and Muser Music; acquiring NVC Arts classical-video company in the U.K.; forming an international marketing alliance with leading U.K. independent China Records; creating Warner Music Benelux (combining affiliates in the Netherlands and Belgium); and expanding and extending the company's worldwide recording and publishing agreements with international superstar Phil Collins. WMI artists won more than 70 international awards, including laurels for Sally Yeh, Gilberto Gil and Kronos Quartet. WMI's best-selling international artists included Mexico's Luis Miguel, Germany's Westernhagen and Italy's Laura Pausini.

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*Warner Music Group boasts an unsurpassed talent roster, representing every genre and style of music from around the world*

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## The Product Is Talent

Musical artists from Warner Bros., Elektra, Atlantic and their affiliated labels enjoyed exceptional chart success in 1994. The creative vitality of Warner Music U.S. was evidenced by the fact that a quarter of the titles on *Billboard's* chart of the top-200-selling albums for the year were from its artists. Warner Music U.S. artists also received 76 nominations for the 1995 Grammy Awards, including three out of five nominations for Album of the Year. Best-selling albums came from established superstars such as Anita Baker, Eric Clapton, R.E.M., John Michael Montgomery, Madonna, Stone Temple Pilots and Keith Sweat, and from such major new talents as



Green Day, Candlebox and All-4-One.

The Music Group's stability is anchored by the breadth of its roster, with only 6% of WMG revenues coming from its top-five-selling artists, and by a rich catalog of older product. only 6% of WMG revenues coming from its top-five-selling artists, and by a rich catalog of older product.

Enhancing WMG's strength in the music marketplace in 1994 were new label associations with country-music powerhouse Curb Records, Britain's blues label Code Blue and the highly respected alternative rock label Sub Pop. Warner/Chappell became a leading creator of sheet music with the acquisition of CPP/Belwin; was named ASCAP Publisher of the Year and BMI Pop Music Publisher of the Year; and expanded its catalog to more than a million copyrights, through agreements with leading songwriters like Alan Jackson.

The gathering-together of the usic Group's domestic labels to form Warner Music U.S. in 1994 put in place a new generation of leadership to carry the company's U.S. recorded- music operations into the next century. Warner Music U.S.'s leadership and all major label heads are executives promoted from within the company, demonstrating the Group's depth of management talent.

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## Warner Music Group

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<i>Major Labels</i>	<i>1994 Major Releases</i>	<i>1995 Major Releases</i>
<b>Warner Bros. Records</b>		
<i>Warner Bros.</i>	David Ball	David Ball
<i>Reprise</i>	Candlebox	Belly
<i>Giant</i>	Eric Clapton	Enya
<i>Maverick</i>	Coolio	Fourplay
<i>Qwest</i>	Jeff Foxworthy	Faith Hill
<i>Warner Bros./Sire</i>	Green Day	Chris Isaak
<i>Warner Nashville</i>	Faith Hill	k d lang
<i>Warner/Reprise Home</i>	Little Texas	Little Texas
<i>Video</i>	Madonna	Ministry
<i>American Recordings</i>	Tom Petty	Porno For Pyros
<i>Slash</i>	Prince	Prince
<i>Tommy Boy</i>	R.E.M.	Red Hot Chili Peppers
	Seal	Rod Stewart
	Travis Tritt	Travis Tritt
	Neil Young	Van Halen
<b>The Atlantic Group</b>		
<i>Atlantic</i>	All-4-One	All-4-One
<i>Interscope</i>	Tori Amos	Boy Howdy
<i>Rhino</i>	Blackstreet	Jose Carreras
<i>Time Warner</i>	Brandy	Clannad
<i>AudioBooks</i>	Changing Faces	Collective Soul

*Atlantic Classics*  
*Atlantic Nashville*  
*Beggars Banquet*  
*Big Beat*  
*Celtic Heartbeat*  
*Curb*  
*Lava*  
  
*Mammoth*  
  
*Matador*  
  
*Mesa Bluemoon*  
  
*1 4 3*  
*TAG*

**Elektra  
Entertainment Group**

*Elektra*  
*EastWest*  
  
*Asylum*  
  
*Elektra Sire*

**Warner Music  
International**

*WEA*  
*East West*  
*Teldec*  
*Erato*  
*Nonesuch*  
*Fimlandia*  
*CGI*  
*Carrere*  
*DRO*  
*WEA Latina*  
*PWI*  
*Z11*  
*rooArt*  
*Magneoton*  
*UFO*

Collective Soul  
Confederate Railroad  
Hootie & The Blowfish  
Jerkie Boys  
Tracy Lawrence  
Gerald Levert  
Neal McCoy  
John  
Michael Montgomery  
Nine Inch Nails  
Jimmy Page & Robert  
Plant  
Pantera  
Liz Phair  
Stone Temple Pilots  
The 3 Tenors in Concert  
1994

Anita Baker  
Natalie Cole  
Gershwin The Piano  
Rolls  
Gipsy Kings  
Metallica  
Molley Crue  
Keith Sweat  
Dawn Upshaw

Phil Collins  
Enya  
Inner Circle  
Andy Lau  
Leandro & Leonardo  
Noriyuki Makihara  
Mana  
Loreena McKennitt  
Luis Miguel  
Jimmy Nail  
Laura Pausini  
Pretenders  
Chris Rea  
Seal  
Mariva Takeuchi

Michael Crawford  
Encomium A Tribute to Led Zeppelin  
Four Seasons  
Juliana Hatfield  
Intro  
Bette Midler  
Mike & The Mechanics  
John Michael Montgomery  
  
Primus  
  
Rush  
  
Sawyer Brown  
Skid Row  
Pete Townshend

AC/DC  
Bjork  
  
The Breeders  
  
The Cure  
En Vogue  
Ini Kamoze  
Metallica  
Natalie Merchant  
Phish  
Linda Ronstadt  
Silk  
Simply Red  
Keith Sweat

The Beloved  
Miguel Bose  
Jose Carreras  
Enya  
Gilberto Gil  
Phillip Glass  
Henryk Gorecki  
The Human League  
Colin James  
Jorge Ben Jor  
Kulcha  
Kronos Quartet  
Mana  
Luis Miguel  
Mandy Patinkin

Fazer  
Telegram  
Continental

The 3 Tenors in Concert  
1994  
Westernhagen

Steve Reich  
Scorpions  
Simply Red  
Patrick Stewart/Kent Nagano, Opera  
Orchestra of Lyon  
Maxim Vengerov/Claudio Abbado  
Sally Yeh

---

WMG continued the growth of its classical-music operations in 1994, highlighted by the remarkable worldwide success of *The 3 Tenors in Concert 1994*, released internationally by Teldec and in the U.S. by Atlantic. The release was Warner Music Group's top-selling title in 1994. Early in 1995 Atlantic Classics U.S. was formed, under The Atlantic Group, to market classical releases in the U.S. At the same time, the None-such label, with such artists as Philip Glass, Henryk Górecki, Kronos Quartet, Dawn Upshaw and Don Byron, was incorporated into Warner Classics International.

---



## New Voices, New Markets

In 1994 A\*Vision Entertainment emerged as the dominant home video label in the fitness category (e.g., *Buns of Steel*) and a leader in children's video, including such hits as the *Magic School Bus* series. In January 1995 A\*Vision was renamed WarnerVision Entertainment and is now a full-fledged division of Warner Music U.S. Time Warner AudioBooks, a cross-divisional venture between The Atlantic Group, Warner Books, Little, Brown and other publishers, expanded rapidly in 1994 and earned two Grammy nominations in its first full year of operation.

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Successful new ventures WarnerVision and Time Warner AudioBooks (a

*joint effort among The Atlantic Group, Warner Books, Little, Brown and other publishers) have given Warner Music Group a strong marketplace presence in home video and audiobooks.*

---

Warner Music Group, moving aggressively into the growing interactive multimedia marketplace, provides the infrastructure through which all CD-ROM titles published by WMG companies, as well as those from Warner Bros., Time Life, HBO and Time Warner Interactive, will be manufactured and distributed. In 1994 wholly owned WarnerActive was established to act as a publisher of interactive titles. WMG also acquired a minority interest in Accolade; formed Inscape, a multimedia joint venture with HBO; and struck software development deals with leading CD-ROM creators HyperBole Studios and Imagination Pilots, to secure a steady flow of CD-ROM titles. In the U.K., Rene-gade was acquired and became the basis for Warner Music Interactive Entertainment, to publish CD-ROM titles in international markets.



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*Warner Music Group's direct-marketing ventures-including magazine/CD services covering everything from classical music to country, jazz, rock, rap and alternative-grew rapidly in 1994.*

---

Warner Music Group's direct-marketing business continued to grow in 1994. Time Warner Enterprises Ltd., based in London, launched marketing activities in 12 European countries. In the U.S., Music Sound Exchange, a joint venture with Sony Software, doubled its revenues from the sale of music and related product through catalogs and stamp sheets. The success of the classical-music magazine/CD subscription service *BBC Music*, launched in 1993, has led to the creation of parallel services for country music (*New Country*); rock, rap and alternative (*huH*); and jazz (*Jazziz*). A magazine/CD service for children, created in collaboration with Children's Broadcast Corp. and based on its successful nationally syndicated radio network, *Radio Aahs*, debuted in February 1995.



---

*WMG entered the CD-ROM marketplace aggressively in 1994, making*

*equity investments in such software publishers as Accolade, one of the largest privately held game companies in the U.S.*

---

The 24-hour, German-language music-video channel VIVA, established in December 1993 as a partnership among Warner Music Group, Sony, EMI, Polygram and a German radio executive, substantially surpassed its revenue and viewership projections in its first full year of operation and is serving as a model for future services elsewhere. In January 1995 Warner Music Group, Sony Pictures, EMI and Bertelsmann Music Group acquired from Star-TV, an affiliate of News Corp., a 50% interest in Channel [V], which operates English- and Mandarin-language, 24-hour music-video television services reaching 220 million people in Asia.

In addition, WMG made investments in Digital Cable Radio Associates, a digital music subscription service in the U.S., marketed as Music Choice, and an affiliated company, Music Choice Europe.

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**WARNER BROS.**

***Warner Bros. is the world's foremost producer and distributor of movies, TV programming and home video.***

**Movies and More**

**1994 Film Highlights**

**No. 1 on Television**

**Around the World, Into the Future**

**1994/1995 Broadcast Season Primetime Programs**

Time Warner Entertainment's Filmed Entertainment division had a record year in 1994, including Warner Bros.' twelfth straight year of record EBITDA (excluding the pre-acquisition results of Lorimar) and a record performance by Six Flags, America's leading regional theme-park company.

Time Warner's Filmed Entertainment division achieved EBITDA in 1994 of \$565 million, up from \$549 million in 1993.

### **Filmed Entertainment - Financial Highlights**

<i>(in millions)</i>	<i>1994</i>	<i>1993</i>
Revenues	\$5,041	\$4,565
EBITDA	565	549

## Movies and More

For an unparalleled twelfth consecutive year, Warner Bros. was among the top-three film studios in domestic box-office share in 1994, with such hits as *Ace Ventura: Pet Detective*, *Maverick*, *The Client*, *Natural Born Killers*, *The Specialist*, *Interview With the Vampire*, *Richie Rich* and *Disclosure*.

In the past six years, the Studio has had 12 films with domestic grosses of more than \$100 million each, far more than its nearest competitor. Warner Bros.' consistency has been achieved through continuing creative relationships with such stars and filmmakers as Kevin Costner, Michael Crichton, Richard Donner, Clint Eastwood, Mel Gibson, Barry Levinson, Alan Pakula, Steven Seagal, Joel Silver, Sylvester Stallone, Arnon Milchan's New Regency and Jim Robinson's Morgan Creek, generating a steady stream of the best creative product that should continue far into the future. International theatrical revenues in 1994 were the second highest in the Studio's history, and Warner Bros. entered into a precedent-setting agreement to distribute films in the People's Republic of China.

Warner Bros. last year announced the creation of a new division to develop animated theatrical features, which will release its first film in 1997. With this initiative, Warner Bros. expects to bring to the feature animation market the same quality and success it currently enjoys in every other area of family programming. It is expected that Warner Bros.' animated features will generate significant additional revenue from both home video and consumer products.

Warner Bros. Worldwide Consumer Products' Studio Stores division continued its remarkable expansion in 1994, adding 46 outlets in the U.S. and five overseas, including flagship stores in London, Glasgow and Berlin. Substantially exceeding mall sales averages for retailers, Warner Bros. Studio Stores now number 111 worldwide, with plans to add between 20 and 25 stores in 1995. The division also announced plans to expand into Asia through franchise partnerships, teaming with a major retailer in each country it enters. Openings this year are slated for Hong Kong and Singapore, with Japan to follow in 1996.





*Warner Home Video achieved record worldwide revenues in 1994 with such hits as Don Bluth's Thumbelina, Ace Ventura: Pet Detective and The Fugitive.*

---

Warner Bros. Worldwide Consumer Products Licensing achieved more than \$2 billion of retail sales worldwide in 1994. New ventures included agreements with Toshiba to develop "Looney Tunes Tronics" stereo products and with Premiere Cruise Lines, putting Warner Bros. characters on board. The division also launched the touring Warner Bros. Family Entertainment on Ice program. Acme Design and Development is a new unit whose premier toy designers will develop products from Warner Bros. film, television and animation properties.

The Studio's unique libraries contain more than 3,000 feature films and more than 25,000 television episodes, including approximately 3,500 animated cartoons. It owns the rights to classic Looney Tunes characters such as Bugs Bunny, Daffy Duck, Tweety Bird and Tasmanian Devil (who celebrated his 40th birthday in 1994 with a major promotion), as well as DC Comics characters such as Superman, Batman and Wonder Woman. DC has successfully grown sales by expanding its lines of ground-breaking illustrated novels, developing narrative innovations such as 1994's "Zero Hour" multi-title series and launching DC Comics Online, moving comics into the emerging world of new media.

---



*Warner Bros.' hit 1994 releases included Natural Born Killers, Ace Ventura: Pet Detective, L.A. Confidential, The Specialist, and Interview With the Vampire (below).*

## 1994 Film Highlights

**Ace Ventura: Pet Detective**  
Dir.: Tom Shadyac  
Jim Carrey





**Maverick**

Dir.: Richard Donner

el Gibson

Jodie Foster

James Garner

**Wyatt Earp**

Dir.: Lawrence Kasdan

Kevin Costner

Dennis Quaid

Gene Hackman

Isabella Rossellini

**The Client**

Dir.: Joel Schumacher

Susan Sarandon

Tommy Lee Jones

Brad Renfro

**Natural Born Killers**

Dir.: Oliver Stone

Woody Harrelson

Juliette Lewis

Robert Downey Jr.

Tommy Lee Jones

**The Specialist**

Dir.: Luis Llosa  
 Sylvester Stallone  
 Sharon Stone

**Interview With the Vampire**

Dir.: Neil Jordan  
 Tom Cruise  
 Brad Pitt  
 Kirstin Dunst  
 Antonio Banderas  
 Christian Slater  
 Stephen Rea

<b>Disclosure</b> Dir. Barry Levinson Michael Douglas Demi Moore Donald Sutherland	<b>Richie Rich</b> Dir. Donald Petrie Macaulay Culkin John Larroquette
--	---

## 1995 Major Releases

<b>Boys On the Side</b> Dir. Herbert Ross Whoopi Goldberg Mary-Louise Parker Drew Barrymore	<b>Just Cause</b> Dir. Arne Glimcher Sean Connery Laurence Fishburne Kate Capshaw Blair Underwood
<b>Outbreak</b> Dir. Wolfgang Petersen Dustin Hoffmann Rene Russo Donald Sutherland	<b>The Bridges of Madison County</b> Dir. Clint Eastwood Clint Eastwood Meryl Streep
<b>Batman Forever</b> Dir. Joel Schumacher Val Kilmer Tommy Lee Jones Jim Carrey Nicole Kidman Chris O'Donnell	<b>Under Siege 2: Dark Territory</b> Dir. Geoff Murphy Steven Seagal Eric Bogosian
<b>Free Willy 2: The Adventure Home</b> Dir. Dwight Little Jason James Richter	<b>Fair Game</b> Dir. Andrew Sipes William Baldwin Cindy Crawford
<b>Copycats</b> Dir. Jon Amiel Sigourney Weaver Holly Hunter Harry Connick Jr.	<b>The Game of Love</b> Dir. Lasse Hallstrom Julia Roberts Robert Duvall Dennis Quaid
<b>Assassins</b> Dir. Richard Donner Sylvester Stallone	<b>Ace Ventura: Pet Detective II</b> Dir. Tom DeCherchio

Sylvester Stallone Antonio Banderas	Jim Carrey
<b>Heat</b> Dir.: Michael Mann Al Pacino Robert De Niro Val Kilmer	<b>Grumpier Old Men</b> Dir.: Howard Deutch Jack Lemmon Walter Matthau Ann-Margret

---

## No.1 on Television

Warner Bros. Television continued to supply more primetime television programs than any other company, including the 1994-95 season's No. 1-rated new series and new drama, *ER* (the highest-rated drama in more than five years, with the highest-rated single episode in two years), and the breakout hit *Friends* (the No. 1 new comedy series). At year-end Warner Bros. Television had 15 highly rated primetime series on the air, including such longtime favorites as the multiple-award-winning *Murphy Brown*, as well as *Sisters*, *Step By Step*, *Family Matters* and *Full House*.



*Warner Bros. Television's Friends is the No. 1 new comedy in the 1994-95 primetime season.*

---

Warner Bros. Animation continues to dominate children's television programming with *Steven Spielberg Presents Animaniacs*, *Taz-Mania*, *Tiny Toon Adventures* and *The Adventures of Batman & Robin*. For the 1995-96 broadcast season, Warner Bros.' new The WB Television Network has ordered new episodes of the Peabody Award-winning *Animaniacs*, as well as three new comedy series: *Steven Spielberg*



*Presents Freak-azoid!*,

*Pinky & the Brain* (favorite characters from *Animaniacs*) and *The Sylvester & Tweety Mysteries* (the first all-new "Sylvester & Tweety" episodes produced in more than three decades).

Warner Bros. Domestic Television Distribution is one of the industry's leading distributors of first-run and off-network syndicated programming in the domestic marketplace. Its hits include the third-highest-rated talk show, *Jenny Jones*; the new, six-times weekly entertainment magazine, *EXTRA-The Entertainment Magazine* (a joint effort of Warner Bros. and Time Inc.); and the off-network hits *Family Matters* and *The Fresh Prince of Bel-Air*.

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*EXTRA: The Entertainment Magazine, produced by Time Telepictures Television (a joint effort of Warner Bros. and Time Inc.), is the top new series in syndication.*

---

Warner Bros. debuted television's "fifth" network on January 11, 1995, reaching about 80% of U.S. households. The WB Television Network's initial, Wednesday-night lineup features four diverse comedies designed to appeal to the 12-34 age group, highly desirable to advertisers. In August 1995 The WB, as it is called, will add a second primetime night and, in September 1995, will unveil its exciting new children's programming service. Kids' WB will feature six half-hours on Saturday mornings and two half-hour morning series on weekdays.

## Around the World, Into the Future

More than 37% of Warner Bros.' revenues comes from outside the U.S. Operating in 49 countries, more than any other video company, Warner Home Video in 1994 achieved record worldwide revenues of \$1.5 billion, up 21% over 1993. Successful titles released in 1994 included *The Fugitive*, *Ace Ventura: Pet Detective* and *Don Bluth's Thumbelina*.

In January 1995 Warner Home Video and Time Warner Entertainment partner Toshiba introduced a technological breakthrough that is expected to provide a major boost to the already booming home video sell-through business: the digital video disc, or DVD. The Toshiba/Warner Home Video DVD, with 15 times the storage capacity of audio CDs or CD-ROMs, won the endorsement of many of the major consumer electronics and film companies. DVD players and discs are expected to be available in the near future.

Warner Bros. International Television Distribution is the world's largest distributor of

programming. It licenses feature films and television programs in more than 160 countries. WBTD will expand its global presence in television with the creation of a variety of thematic or general entertainment programming services, in both mature and emerging broadcast markets around the world. WBTW-The Warner Channel, a 24-hour, family-oriented service for Latin America that will launch in the spring of 1995, is Warner Bros.' first cable satellite-delivered entertainment channel created exclusively for the international marketplace.

---



*Grand Openings:* In 1994 Warner Bros. Studio Stores opened flagship outlets overseas in London (right), Berlin and Glasgow. And in 1995 the company launched The WB Television Network.

---

*The company began construction in 1994 of Warner Bros. Movie World, a regional theme park and studio complex to debut in 1996 in the Rhine Ruhr region of Germany, modeled on the successful Warner Bros. Movie World in Brisbane, Australia. At the end of 1994, Warner Bros. International Theatres operated or had an interest in 36 multiplexes, consisting of 294 screens in six countries, including the U.K., Germany and Japan-with ten additional multiplexes (81 screens) planned for 1995.*

---

## *1994/1995 Broadcast Season Primetime Programs*

### *Warner Bros. Television*

*ER*

*Family Matters*

*Friends*

*Full House*

*The George Carlin Show*

*The Great Defender\*\**

*Hangin' with Mr. Cooper*

*Hope & Gloria\*\**

*Kung Fu: The Legend Continues*

*Living Single*

*Lois & Clark: The New Adventures of Superman*  
*Medicine Ball\*\**  
*Murphy Brown*  
*On Our Own*  
*The Parent 'Hood\**  
*Pointman\**  
*Sisters*  
*Something Wilder*  
*Step by Step*  
*Under Suspicion*  
*The Wayans Bros.\**

*Witt-Thomas Productions*  
*Daddy's Girls*  
*The John Larroquette Show*  
*uscle\**  
*The Office\*\**

*The WB Television Network*  
*uscle\* (see also Witt-Thomas Productions)*  
*The Parent 'Hood\* (see also WBTV)*  
*Unhappily Ever After\**  
*The Wayans Bros.\* (see also WBTV)*

*Warner Bros. Domestic Pay-TV, Cable and Network Features Distribution*  
*Live From the House of Blues*

*\*1995 debut*

*\*\*March 1995 debut*

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View sections of the annual report that cover other Time Warner divisions:

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- [TIME WARNER CABLE](#)
- [TIME INC.](#)
- [SIX FLAGS](#)
- [HBO](#)

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***Six Flags Theme Parks soared to new heights in family entertainment.***

**A Business for the '90s More Than Thrills**

**Six Flags Theme Parks, with more than 21 million visitors and annual revenues of more than \$500 million, is the largest regional theme-park company in the world and the No. 2 theme-park company overall. It is both a strong cash-flow business in its own right and a unique family-oriented venue to market and merchandise Time Warner's many familiar brand names and franchises.**

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*Every year Six Flags is chosen by more and more Americans as the place for family fun. The company's seven parks-within a day's drive of 85% of the U.S. population-are being upgraded constantly with improved theming and popular new rides like Viper at Six Flags Magic Mountain in Los Angeles.*

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**Since Six Flags' management was taken over by Time Warner in 1992, it has registered its best years ever, with record EBITDA coming from higher attendance, higher revenues per visitor and greater in-park spending. The company's national comparative-marketing strategy has succeeded in creating a two-company category and has significantly increased the public's unaided awareness of the Six Flags brand (from 37% in 1992 to 60% in 1994).**

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*Six Flags has added new rides throughout its parks. Popular attractions include Six Flags Wild Safari Animal Park (New Jersey); Viper (California); Yosemite Sam Sierra Falls (California); virtual-reality flight simulator Space Shuttle America (Chicago); Ninja (Atlanta); and Batman Spectacular Laser & Fireworks Show (Atlanta).*

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## A Business for the '90s

As many predicted, family entertainment has emerged as a key growth sector in the economy of the '90s. In addition, the trend toward more frequent, closer-to-home vacations has also been growing. Six Flags--with seven regional theme parks in such major markets as New York, Chicago and Los Angeles--is uniquely positioned to benefit from these key trends. Fully 85% of the U.S. population is within a day's drive of a Six Flags park.

Theming in each park's fantasy areas has been continually enhanced and expanded by Six Flags' access to the vast array of Time Warner properties. Batman The Ride, the world's first inverted, outside looping thrill ride--already at Six Flags Great America in Chicago and Six Flags Great Adventure in New Jersey, between New York City and Philadelphia--opened at Six Flags Magic Mountain in Los Angeles in 1994 and will debut at Six Flags Over Mid-America in St. Louis in 1995.

Also in 1995 the new Batman Forever Stunt Show will premiere at Six Flags Magic Mountain and Six Flags Great Adventure, to coincide with the release of the Warner Bros. film. Six Flags also continued its participation in the Sports Illustrated Sports Festival, the world's largest traveling sports festival, in 1994.

Exciting new rides and attractions are continually being introduced. Two new virtual-reality flight simulators--Space Shuttle America: The Next Century, at Six Flags Great America, and The Right Stuff: Mach 1 Adventure at Six Flags Great

Adventure-debuted in 1994. Also premiering were such Time Warner tie-ins as the Police Academy Stunt Show, the Warner Music Rock Revue, the Dennis the Menace Screen Test and the Robin Hood Stunt Show, as well as enhanced theming and additional rides in the parks' areas for younger guests. Bugs Bunny Land And this summer, the company will open Six Flags Hurricane Harbor, a 22-acre, 14-attraction, themed water park, adjacent to Six Flags Magic Mountain The resulting Six Flags California complex will be the first multi-gated entertainment location in the state The company plans to continue leveraging its resources and expertise to create



additional multi-gated destinations around theme parks.

its existing

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*Expanded use of properties like Warner Bros.' Looney Tunes characters have enhanced Six Flags' appeal and exposure for Time Warner's brands.*

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## More than Thrills

Six Flags' sponsorship sales reached new heights in 1994, including blue-chip companies like Coca-Cola, MCI, Chevrolet and Kodak. New fantasy-themed concept stores and restaurants debuted, such as the Looney Tunes Shoppe at Six Flags Great Escape and the new Mooseburger Lodge restaurant in High Sierra Territory at Six Flags Magic Mountain.

### **Six Flags Theme Parks**

**Six Flags California:**  
Six Flags Magic Mountain  
Six Flags Hurricane Harbor  
Los Angeles, California



**Six Flags Over Georgia**  
Atlanta, Georgia

**Six Flags Great America**  
Chicago, Illinois

**Six Flags Over Mid-America**  
St. Louis, Missouri

**Six Flags Great Adventure  
and Six Flags Wild Safari**  
Animal Park  
Jackson, New Jersey

**Six Flags Over Texas**  
Dallas/Ft. Worth, Texas

**Six Flags Houston:**  
Six Flags AstroWorld  
Six Flags WaterWorld  
Houston, Texas

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*With quality programming, innovative marketing and a revitalized pay-television environment, Home Box Office hit double-digit growth.*

**The Leader in Premium Programming**  
**New Pathways and Consumer Value**  
**Growth Through Diversification**  
**Going Global**  
**1994 HBO Highlights**

Home Box Office achieved robust 12% EBITDA growth in 1994, to \$257 million from \$230 million in 1993, thanks to the ongoing strength of its core pay-TV businesses, far-reaching marketing campaigns, successful new ventures and a renewed pay-television environment. HBO and Cinemax added 2.3 million subscribers for a total of 27 million—the largest expansion of the company's subscriber base since the pre-VCR era of 1983. Contributing were gains from cable, direct-to-home satellite, wireless and the lodging industry. The company also continued its active expansion into international marketplaces.<sup>1</sup>

### **HBO-Programming - Financial Highlights**

<i>(in millions)</i>	<i>1994</i>	<i>1993</i>
Revenues	\$1,513	\$1,441
EBITDA	257	230

# The Leader in Premium Programming

HBO is the most-watched non-broadcast network, and it regularly outdraws the broadcast networks' primetime lineups in HBO homes (where HBO's promise of a new movie every Saturday night made it the top-rated network on Saturday nights for the fourth straight year). HBO has established itself as the industry leader in award-winning original programming-recognized in 1994 by 15 Emmy Awards, two Peabody Awards and an Academy Award for the documentary *I Am a Promise* (its fourth documentary Oscar in the past five years). In January 1995 HBO received four Golden Globe Awards (more than any of the broadcast networks) and 23 CableACE Awards for 1994 programs (more than the next three networks combined). HBO received 230 honors and awards in 1994 for its pro-gramming, advertising, promotions and marketing excellence.

Among HBO's provocative and critically acclaimed 1994 original films were *The Burning Season*, *State of Emergency*, *White Mile* and *Witch Hunt*. HBO's probing documentaries, such as *Gang War: Bangin' in Little Rock*, also won numerous awards and produced in-creasingly strong ratings. The company continued to create a varied slate of family programming, presenting 218 family-oriented shows in 1994. Many featured important social themes and messages, such as *Going, Going, Almost Gone! Animals in Danger*, presented in association with the World Wildlife Fund. HBO's growing roster of award- winning series includes the "best hour of comedy on TV": the Emmy- and CableACE-winning duo of *The Larry Sanders Show*, in its fourth season, and *Dream On*, now in its sixth year. They were joined in 1994 by the irreverent social commentary of the new Emmy-winning *Dennis Miller Live*. Big-event concerts featured superstars like Barbra Streisand (who headlined the highest-rated music special in HBO history) and Whitney Houston (the first-ever stereo TV transmission from South Africa).



HBO's original programming runs the gamut from drama to comedy to hard-hitting documentaries (clockwise, starting at top): *Witch Hunt*;

artin (on Fox); Gang War; Bangin' in Little Rock; Dream On; The Burning Season; and White Mile.

Comedy—from classic stand-up to ground-breaking series—is a proud tradition at HBO, exemplified by such award-winning programming as *The Larry Sanders Show* starring Garry Shandling (right), now in its fourth season.

---

Highlighted by November's historic championship bout in which 45-year-old George Foreman became the oldest heavyweight champ ever (HBO's highest-rated program since 1990), HBO Sports continued its boxing preeminence in 1994. Boxing and other events distributed by the company's pay-per-view service TVKO generated the highest level of event revenue at retail in the PPV industry for the fourth consecutive year. In 1994 the division produced its 20th anniversary telecast of Wimbledon and extended its agreement to cover the world's most prestigious tennis tournament for another five years. HBO Sports' production *Arthur Ashe: Citizen of the World* aired in September to widespread critical acclaim.

## New Pathways and Consumer Value

With its high-profile programming and marketing expertise, Home Box Office is positioned to take full advantage of pay television's expanding distribution opportunities, such as high-powered, direct-to-home satellite broadcasting, which extends the reach of HBO and Cinemax to virtually every household in America. HBO Direct, the company's direct-broadcast-satellite division, has shown consistent growth, thanks in large part to the power of Home Box Office's brand names and the popularity of multichannel HBO and Cinemax.

The multiple-channel versions of HBO and Cinemax—available to all direct-to-home subscribers and a growing percentage of cable systems—enhance consumer value by offering subscribers multiple channels for the price of one, extending both penetration and retention rates. Another value enhancement, HBO en Español, fueled double-digit growth in HBO's penetration into the Spanish-language market in the U.S.

Cinemax continues as the industry leader in providing subscribers with more films—and more new films—than any other premium service, and is the highest-rated channel on cable after HBO. Together, HBO and Cinemax continue to offer the most films of any pairing of pay-TV services. Multiyear film-licensing agreements with Warner Bros., 20th Century Fox, Sony Pictures, Paramount and Savoy guarantee a steady flow of strong theatrical product

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*George Foreman's stunning knockout of Michael Moorer on November 5, 1994, was HBO's highest-rated program in five years--and a worthy addition to the network's tradition of ring classics, reaching back to the 1975 Ali-Frazier "Thrilla in Manila."*

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## Growth Through Diversification

Building on its success in programming and marketing, Home Box Office has continued to grow its ancillary businesses--such as basic cable, program production for broadcast television, home video and multimedia--and to extend overseas, establishing itself as a growing force in the burgeoning global media industry.

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*Inscape, HBO's joint venture with Warner Music Group and software developer Michael Nash, is releasing cutting-edge CD-ROMs like The Residents' Bad Day on the Midway*

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Comedy Central, Home Box Office's joint-venture basic-cable channel, is now available in 31 million homes. Most of Comedy Central's original programming is produced by HBO Downtown Productions, including three shows that won Emmys in 1994. Basic-cable channel E! Entertainment Television, 49% owned by Time Warner and managed by HBO, expanded to 28 million households and achieved operating profits in 1994. HBO Independent Productions produced three series this season for the Fox network, including *Martin*, now in its third season. HBO Home Video markets a broad range of videos from its library of HBO original productions, made-for-video programs, other non-theatrical product and feature films--including releases covered by a long-term agreement with Savoy Pictures, such as 1994's *A*



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*Bronx Tale and Shadowlands.*

Home Box Office's expertise in creating entertainment software positions it well for the technical challenges and innovations ahead. Investments in interactive multimedia for CD-ROM and other game/entertainment formats include



*Time Warner Cable is the cable company best positioned to enter the new age of telecommunications.*

The Power of Clustering  
The Future is Now  
Near Term and Beyond  
An Explosion of Choice

Time Warner Cable experienced robust internal basic subscriber growth of more than 4%, a 6% increase in pay units, 30% growth in advertising and 11% growth in pay-per-view revenues in 1994. The division continued its aggressive rollout of fiber-optic cable, began a multifaceted entry into the telephone business and launched the Full Service Network(TM) (FSN)—the most powerful and innovative communications system ever introduced to consumers.

Due principally to government rate regulation of the cable industry, Time Warner Cable's overall results were down 4% in 1994. Time Warner Cable posted EBITDA of \$989 million in 1994, down from \$1.035 billion in 1993.

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### **Cable - Financial Highlights**

<i>(in millions)</i>	<i>1994</i>	<i>1993</i>
Revenues	\$2,242	\$2,200
EBITDA	989	1,035

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# The Power of Clustering

Time Warner Cable is the most efficiently clustered of the world's leading cable operators, which positions it strongly for both expanded cable revenues and entry into telephony. With prospects for a pro-competitive approach to telecommunications regulation improving in Washington, Time Warner Cable is poised to bring its technological, packaging and programming strengths to bear on a broader telecommunications marketplace.

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*The Full Service Network offers subscribers unprecedented control, convenience and choice-including the ability to fast-forward, rewind, pause-and shop-at the touch of a button.*

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During 1994 and early 1995 Time Warner Cable and Time Warner Inc. entered into agreements to increase the number of subscribers under their management from 7.5 million to 11.5 million, with three-quarters of them in 34 groups of at least 100,000 (19 of which are above 200,000). These agreements included the acquisitions by Time Warner Inc. of Summit Communications and KBLCOM (the cable systems owned by Houston Industries, including the 50% of Paragon that Time Warner Cable does not already own); the creation of a joint venture, Time Warner Entertainment-Advance/Newhouse, adding systems with 1.4 million subscribers, largely in North Carolina, Florida and New York State; and a merger between Time Warner Inc. and Cablevision Industries, adding about 1.3 million subscribers. All these transactions are expected to close in 1995.

**Time Warner Cable's Largest Clusters  
(after completion of pending transactions)**

<b>Divisions/Clusters</b>	<b>Subscribers (in thousands)</b>
1 New York City	1,026
2 Central Florida	638
3 Tampa Bay, Fla.	512
4 Raleigh/Payetteville, N.C.	358
5 Austin/Waco, Tx.	311
6 Charlotte, N.C.	306
7 San Antonio, Tx.	269
8 Los Angeles, Cal.	262
9 Greensboro, N.C.	252
10 Memphis, Tenn.	249
11 Rochester, N.Y.	245
12 Hawaii	242
13 San Diego, Cal.	213
14 Memphis, Tenn.	211
15 Greater Boston	212
16 Northeast Ohio	206
17 Cincinnati, Ohio	205
18 Milwaukee, Wis.	201
19 Eastern Pennsylvania	201

Time Warner's New York City Cable Group, already the largest cable cluster in the world, reached a significant milestone in 1994 when it connected its one-millionth subscriber. Following the completion of pending transactions, the company's Central Florida system (Orlando) will reach 638,000, and the Tampa Bay system more than 500,000. The benefits of clustering are expected to increase in an environment of competitive telephony and Full Service Network capabilities.

## The Future Is Now

The Full Service Network debuted on December 14, 1994, in Orlando, offering true video-on-demand with full VCR functionality (the ability to fast-forward, rewind and pause), a variety of interactive home-shopping services and video games and an interactive program guide. The FSN, created by Time Warner along with Silicon Graphics, AT&T Network Systems, Scientific-Atlanta and Hewlett-Packard, will be rolled out to 4,000 Orlando households over the course of 1995, and more than a dozen additional services will be introduced this year. They include ShopperVision's "virtual" supermarket and drugstore; HBO on Demand; Time Inc.'s and Time Warner Cable's news-on-demand collaboration, The News Exchange (including local news and information from the Orlando Sentinel); Warner Music Group's The Magic Music Store; and Warner Bros.' Omnio navigation system.

Ongoing research on the Orlando families' use of the Full Service Network will provide Time Warner Cable with invaluable information about consumer preferences, pricing and technological options, and will afford opportunities for journalists and creative artists from every division of Time Warner to explore the many new creative and business possibilities of digital, interactive, broadband networks.

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*New York 1 News, Time Warner Cable of New York City's pioneering 24-hour local cable news channel, saw growth in both ratings and ad revenue in 1994*

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## Near-Term and Beyond

The union of fiber optics and coaxial cable that Time Warner Cable engineers pioneered in 1988 was honored in 1994 with the cable industry's first-ever technical Emmy Award. This architecture is not only paving the way for the Full Service Network, but also improving current performance, thanks to better system reliability, reduced service costs and improved picture quality. The increased capacity of "fiber-rich" systems also opens up many attractive near-term business opportunities, including enhanced pay-per-view (Time Warner already generates the industry's best PPV buy rates), increased multiplexing of premium pay-TV, new product tiers and telephony. Time Warner Cable is in its second year of the most aggressive rollout of fiber optics in the industry.

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*Time Warner Cable won the industry's first Emmy Award for technological achievement in 1994, recognizing the company's trailblazing method for combining fiber optics and coaxial cable.*

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Time Warner Communications, the telephony division of Time Warner Cable, took a number of significant steps in 1994 to enter both the business and residential telephone sectors, including a ground-breaking agreement permit-ting Time Warner Cable's Greater Rochester Cablevision to offer switched business and residential telephone and telecommunications services in that city. Also in Rochetelephony division of Time Warner Cable, took a number of significant steps in 1994 to enter both the business and residential telephone sectors, including a ground-breaking agreement permit-ting Time Warner Cable's Greater Roche

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*Time Warner Cable's broadband power will enable it to create attractive telephone /programming service packages.*

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Time Warner Communications is currently operating in 12 locations using fiber-optic SONET (synchronous optical network) rings to serve businesses and will continue to expand in 1995. The company also applied for permission to enter the local telephone business in Ohio. And Time Warner Communications opened a state-of-the-art National Operations Center in Englewood, Colorado, providing 24-hour management of the company's telephone networks across the country. In both its telephony initiatives and in its plans for the Full Service Network, Time Warner's ability to draw on the expertise and resources of Time Warner Entertainment partner U S WEST has proven invaluable. This partnership remains the premier example of a mutually productive cable-telco relationship.

## An Explosion of Choice

Time Warner Cable continued in 1994 to create new programming options for its subscribers and to enhance existing services. New York 1 News, Time Warner Cable of New York City's innovative and honored 24-hour, all-news channel, which was launched in 1992, achieved steady growth in ratings and advertising revenue during 1994, while continuing to serve as a model for local news operations elsewhere in the U.S. and abroad. The Sega Channel, a new interactive premium service of which Time Warner Entertainment owns 33%, offers owners of Sega Genesis video-game systems the ability to play dozens of popular video games via cable TV for a single monthly charge. Court TV grew its subscriber base from 14 million to 17 million in 1994. And a joint venture with Spiegel launched the Catalog 1 shopping channel, with current plans to focus on online interactive applications and the Full Service Network.

In areas not served by cable, high-power, direct-broadcast satellite services are providing customers with multiple channels of programming. Primestar--a partnership in which Time Warner will own more than 30% after completion of pending system acquisitions--is rapidly expanding its customer base. Time Warner's Primestar customers now are at 100,000.

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*Time Warner Cable's Asian initiatives in 1994 included ventures aimed at bringing cable to Japan, Taiwan and China.*

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Growth opportunities for broadband cable networks are also very promising outside the United States. In 1994 Time Warner Cable announced joint ventures to provide products and services to emerging cable industries in Taiwan, mainland China and Japan. And in January 1995 the Time Warner Entertainment partners--Time Warner, Toshiba, ITOCHU and U S WEST--announced plans to develop new cable systems in Japan.

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## **OTHER INVESTMENTS**

### **COMEDY CENTRAL**

50% owned by Time Warner Entertainment

31 million subscribers

47% increase in net ad revenues over 1993

### **COURTROOM TELEVISION NETWORK**

55% owned

Managed by Time Warner's American  
Lawyer Media, L.P.

17 million subscribers

### **E! ENTERTAINMENT TV**

49% owned

Managed by Home Box Office

28 million subscribers

### **THE SEGA CHANNEL**

33% owned by Time Warner Entertainment

Video-game pay-television channel

### **BLACK ENTERTAINMENT TELEVISION (BET)**

15% owned

40.2 million subscribers

### **THE 3DO COMPANY**

13% owned

Developer of multimedia technology

### **CRYSTAL DYNAMICS**

10% owned by Time Warner Entertainment

Video-game software developer

### **SAVOY PICTURES**

3% owned by Time Warner Entertainment

Independent motion-picture distributor

### **HASBRO**

14% owned

World's largest traditional toy company

### **ATARI CORPORATION**

25% owned

Personal computer and video-game systems

### **CATALOG 1**

50% owned by Time Warner Entertainment

New home-shopping channel with Spiegel,  
Eddie Bauer and others

### **TURNER BROADCASTING SYSTEM**

19.6% owned

Cable News Network (CNN) 60.7 million subscribers

Headline News 54.4 million subscribers  
Turner Network Television (TNT) 60.9 million subscribers  
Superstation TBS 61.9 million subscribers  
The Cartoon Network 11.7 million subscribers

**INTERNATIONAL INVESTMENTS INCLUDE:**

Cable (Hungary, Sweden, Taiwan, Japan, China, France)\*  
Channel [V] (Asia)  
Classic FM Radio (U.K., Netherlands, Finland, Sweden)\*  
HBO Asia\*  
HBO Brasil\*  
HBO Hungary\*  
HBO Ole (Latin America)\*  
Music Choice Europe  
N-TV (Germany)\*  
Sky Network Television (New Zealand)\*  
TV 1000 (Scandinavia)\*  
VIVA (Germany)  
Warner Bros. International Theatres\*  
Warner Bros. Movie World (Australia)\*

\* Time Warner Entertainment investment

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# TIME WARNER *news release*

FOR IMMEDIATE RELEASE

## TIME WARNER AND TIME WARNER ENTERTAINMENT REPORT RECORD COMBINED EBITDA FOR BOTH THE FOURTH QUARTER AND 1994

### Content Businesses--Publishing, Music, Filmed Entertainment and HBO--Post Combined 12% EBITDA Growth in the Quarter and 10% in 1994

NEW YORK, NY, February 7, 1995 -- Time Warner Inc. (Time Warner) and Time Warner Entertainment Company, L.P. (TWE), reported record combined earnings before interest, taxes, depreciation and amortization (EBITDA) of \$2.961 billion on revenues of \$15.905 billion for 1994, compared to EBITDA of \$2.829 billion on revenues of \$14.544 billion for 1993. For the fourth quarter, combined record EBITDA was \$827 million on revenues of \$4.591 billion, compared to EBITDA of \$760 million on revenues of \$4.119 billion in the fourth quarter of 1993. Time Warner's four content businesses--publishing, music, filmed entertainment, and HBO--grew 12% in the quarter and 10% in 1994 as all posted record results for the quarter and the year. While the cable division posted a fourth-quarter EBITDA increase, full-year results were lower due to the effects of government rate regulation. Below are EBITDA and revenues for the fourth quarter and full year (in millions)

	1994	Fourth Quarter 1993	1994	Year 1993
<b>TIME WARNER</b>				
Publishing	\$ 157	\$ 146	\$ 430	\$ 372
Music	251	215	720	643
<b>ENTERTAINMENT GROUP</b>				
Filmed Entertainment	109	96	565	549
Programming-HBO	63	61	257	230
Cable	247	242	989	1,035
<b>Combined EBITDA</b>	<b>\$ 827</b>	<b>\$ 760</b>	<b>\$ 2,961</b>	<b>\$ 2,829</b>
<b>Combined Revenues</b>	<b>\$4,591</b>	<b>\$4,119</b>	<b>\$15,905</b>	<b>\$ 14,544</b>

Commenting on the company's 1994 performance, Chairman and CEO Gerald M. Levin, said "We are pleased that the double-digit growth of our combined content businesses--publishing, music, filmed entertainment, and HBO--continued in 1994 with all posting record results for both the fourth quarter and the year. Looking forward, I expect the strong performance from our content businesses to continue and for cable to reemerge as a

strong growth area for Time Warner."

Separately, Time Warner reported 1994 EBITDA for its wholly-owned Publishing and Music Groups of \$1.150 billion, up 13% on revenues of \$7.396 billion, compared to \$1.015 billion of EBITDA on revenues of \$6.581 billion in 1993. For the fourth quarter, Time Warner's EBITDA totaled \$408 million on revenues of \$2.287 billion, compared to \$361 million of EBITDA on revenues of \$1.960 billion in the year-earlier period. Time Warner also reported \$176 million of pretax income from its equity in the Entertainment Group in 1994, compared to \$281 million for 1993. For the fourth quarter, Time Warner recorded a pretax loss of \$1 million from its equity in the Entertainment Group, compared to \$2 million of income in the year-earlier period.

For the full year 1994, Time Warner reported a loss of \$91 million, compared to \$221 million in 1993. The net loss applicable to common shares (after preferred dividends) was \$104 million, compared to \$339 million in 1993. The loss per common share was \$ .27, compared to \$ .90 in 1993. The 1993 results included both a one-time tax charge and an extraordinary loss totaling

\$127 million or \$ .34 per share.

For the quarter, Time Warner reported net income of \$12 million, compared to \$7 million a year ago. The net income applicable to common shares was \$8 million for the quarter, compared to

\$4 million for the same period of 1993. Net income per common share was \$ .02, compared to \$ .01 in the fourth quarter of 1993.

## PUBLISHING

Fourth-quarter EBITDA for Time Inc., the company's publishing division, was a record

\$157 million, compared to \$146 million a year earlier. For 1994, EBITDA was \$430 million, also a record for continuing operations, up 16%, as compared to \$372 million in 1993. 1994's strong results were driven by growth in magazine advertising, magazine circulation revenues, and the company's book businesses. Improved performances at People, Sports Illustrated, Fortune, Southern Progress Corp., Book-of-the-Month Club and Little, Brown as well as operating margin improvement contributed to the overall results.

## MUSIC

Warner Music Group posted record fourth-quarter EBITDA of \$251 million, up 17%, compared to \$215 million in the fourth quarter 1993. For the full-year, EBITDA was an 11th-straight record \$720 million, up 12%, compared to \$643 million for 1993. Contributing to the year's results were increases in recorded music sales, both in the U.S. and internationally as well as revenue gains from music publishing and direct marketing businesses. Top worldwide-selling artists include All-4-One, Anita Baker, Eric Clapton, Green Day, Luis Miguel, John Michael Montgomery, R.E.M., Stone Temple Pilots, Mariya Takeuchi and The 3 Tenors. In the quarter, Warner Music artists accounted for three of the five nominations for the *Best Album of the Year* Grammy Award.

## ENTERTAINMENT GROUP

### FILMED ENTERTAINMENT

Fourth-quarter EBITDA from the Filmed Entertainment businesses was a record \$109 million, up 14%, versus \$96 million a year earlier. For 1994, EBITDA was a record \$565 million, compared to \$549 million for 1993. Warner Bros. and Six Flags each had record years. For Warner Bros., it was the 12th-straight year of record EBITDA. It was another outstanding year at the domestic box office in 1994, led by the success of *Interview With The Vampire* (\$102 million to date), *Maverick* (\$102 million to date), *The Client* (\$92 million to date), and *Disclosure* (\$77 million to date). Contributing to the year's results were increased revenues from worldwide home video, syndication, and consumer products. Warner Bros. Television's show "ER" is the top-rated new show on network television. Six Flags' improved results were due to increased revenues per visitor and increased

attendance

## HBO

The programming-HBO business had record fourth-quarter EBITDA of \$63 million, compared to \$61 million a year earlier. For 1994, EBITDA was a record \$257 million, up 12%, compared to \$230 million in 1993. The year's results reflect a significant increase in subscribers to both HBO and Cinemax. At year-end, the subscriber count for Home Box Office and Cinemax stood at

27 million, up 2.3 million from 1993, the largest increase for the services since 1983. In January, HBO again dominated the CableACE Awards, winning a total of 23 honors. HBO also received four Golden Globe Awards, more than any of the broadcast networks.

## CABLE

Time Warner Cable's EBITDA was \$247 million in the quarter, versus \$242 million a year earlier. EBITDA for 1994 was \$989 million, compared to \$1,035 billion in 1993. While revenues from pay-TV units, pay-per-view programs, and advertising increased for the year, the increase was more than offset by the impact of the government rate regulation of the cable industry. For the year, the subscriber base of Time Warner Cable grew a healthy 4% to 7.5 million from 7.2 million. After the closing of the three announced transactions with Summit, Advance/Newhouse and KBLCOM, Time Warner Cable will have approximately 10 million customers under its management.

Time Warner Inc. is the world's leading media and entertainment company, with interests in magazine and book publishing, recorded music company, with interests in magazine and book publishing, recorded music and music publishing, filmed entertainment.

####

Attachments:

- (1) Consolidated Income Statement
- (2) Notes

**TIME WARNER INC.**  
**CONSOLIDATED STATEMENT OF OPERATIONS**  
**BY BUSINESS SEGMENT**  
(In millions, except per share amounts)  
(Unaudited)

	Three Months Ended December 31,		Years Ended December 31,	
	1994	1993	1994	1993
Revenues:				
Publishing	\$ 991	\$ 940	\$3,433	\$3,270
unic	1,301	1,024	3,986	3,334
Intersegment elimination	(5)	(4)	(23)	(23)
<b>Total revenues</b>	<b>\$2,287</b>	<b>\$1,960</b>	<b>\$7,396</b>	<b>\$6,581</b>

Operating income before

depreciation and amortization:

Publishing	157	146	430	372
music	251	215	720	643

	408	361	1,150	1,015
Depreciation and amortization	(110)	(108)	(437)	(424)

Operating income	290	253	713	591
------------------	-----	-----	-----	-----

Equity in pretax income (loss) of Entertainment Group, substantially all TWE (1)		2	176	281
--	--	---	-----	-----

Interest and other, net	(210)	(175)	(724)	(718)
Corporate expenses	(19)	(17)	(76)	(73)

Income before income taxes	60	63	89	81
----------------------------	----	----	----	----

Income taxes	(48)	(56)	(180)	(24)
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Income (loss) before extraordinary item	12	7	(91)	(164)
---	----	---	------	-------

Extraordinary loss on retirement of debt, net of \$37 million income tax benefit	-	-	-	(57)
--	---	---	---	------

Net income (loss)	12	7	(91)	(221)
-------------------	----	---	------	-------

Preferred dividend requirements	(4)	(3)	(13)	(118)
---------------------------------	-----	-----	------	-------

Net income (loss) applicable to common shares	\$ 8	\$ 4	\$ (104)	\$ (339)
---	------	------	----------	----------

Income (loss) per common share:

Income (loss) before extraordinary item	\$ 0.02	\$ 0.01	\$ (0.27)	\$ (0.75)
---	---------	---------	-----------	-----------

Net income (loss)	\$ 0.02	\$ 0.01	\$ (0.27)	\$ (0.90)
-------------------	---------	---------	-----------	-----------

Average common shares    379.2      377.2      378.9      374.7

**ENTERTAINMENT GROUP**  
**COMBINED STATEMENT OF OPERATIONS**  
**BY BUSINESS SEGMENT**  
(In millions; unaudited)

	<u>Three Months Ended</u>		<u>Years Ended</u>	
	<u>December 31,</u>		<u>December 31,</u>	
	<u>1994</u>	<u>1993</u>	<u>1994</u>	<u>1993</u>
<b>Revenues:</b>				
Filmed Entertainment	\$1,399	\$1,312	\$5,041	\$4,565
Programming - HBO	391	381	1,513	1,441
Cable	579	551	2,242	2,208
Intersegment elimination	(65)	(85)	(287)	(251)
<b>Total revenues</b>	<b>\$2,304</b>	<b>\$2,159</b>	<b>\$8,509</b>	<b>\$7,963</b>
<b>Operating income before depreciation and amortization:</b>				
Filmed Entertainment	\$ 109	\$ 96	\$ 565	\$ 549
Programming - HBO	63	61	257	230
Cable	<u>247</u>	<u>242</u>	<u>989</u>	<u>1,035</u>
	419	399	1,811	1,814
Depreciation and amortization	<u>(240)</u>	<u>(234)</u>	<u>(959)</u>	<u>(909)</u>
<b>Operating income</b>	<b>179</b>	<b>165</b>	<b>852</b>	<b>905</b>
Interest and other, net	(165)	(148)	(616)	(574)
Corporate services	<u>(15)</u>	<u>(15)</u>	<u>(60)</u>	<u>(60)</u>
Income (loss) before income taxes	(1)	2	176	281
Income taxes	<u>-</u>	<u>(16)</u>	<u>(40)</u>	<u>(64)</u>
Income (loss) before extraordinary item	(1)	(14)	136	217
Extraordinary loss on retirement of debt, net of \$7 million income tax benefit	-	-	-	(10)



Net income (loss)            \$(1)                            \$(14)                            \$136                            \$207

**TIME WARNER INC. AND ENTERTAINMENT GROUP  
NOTES TO STATEMENTS OF OPERATIONS**

**Note 1: Entertainment Group**

The Entertainment Group consists of the Filmed Entertainment, Programming-HBO and Cable businesses, substantially all of which are owned by Time Warner Entertainment Company, L.P. (TWE), a Delaware limited partnership in which subsidiaries of Time Warner are the general partners and subsidiaries of ITOCHU Corporation, Toshiba Corporation and U S WEST, Inc. are the unaffiliated limited partners. The operating results of the Entertainment Group are reported by Time Warner on a deconsolidated basis. No portion of TWE's net income for the years ended December 31, 1994 and 1993 was allocated to the limited partners. Within the Entertainment Group, the revenues and operating results of Filmed Entertainment include the revenues and operating results of Warner Bros. and Six Flags.

**Note 2: Income Taxes**

The relationship between income before income taxes and income tax expense of Time Warner is affected by the amortization of goodwill and certain other financial statement expenses that are not deductible for income tax purposes, and by a charge of \$70 million (\$ 19 per common share) in the third quarter of 1993 to reflect the effect on the company's deferred federal income tax liability of the increase in the corporate tax rate enacted into law in August 1993. Income tax expense of Time Warner includes all income taxes related to its allocable share of partnership income and its equity in the income tax expense of corporate subsidiaries of the Entertainment Group.

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# TIME WARNER

## 1995 ANNUAL REPORT

### Building Global Brands

#### Financial Highlights

Years Ended December 31, (millions, except per share amounts)	1995	1994
<b>EBITDA*</b>		
<b>Time Warner</b>		
Publishing	\$ 476	\$ 430
Music	775	720
Music - other losses**	(85)	-
Cable	90	-
<b>Entertainment Group</b>		
Filmed Entertainment	490	430
Six Flags Theme Parks***	60	135
Broadcasting - The WB Network	(66)	-
Programming - HBO	293	257
Cable	1,275	989
<b>Combined EBITDA</b>	<b>\$3,308</b>	<b>\$2,961</b>
<b>Combined Revenues</b>	<b>\$17,696</b>	<b>\$15,905</b>
<b>Loss before extraordinary item</b>	<b>\$ (124)</b>	<b>\$ (91)</b>
<b>Net loss****</b>	<b>\$ (166)</b>	<b>\$ (91)</b>
<b>Loss per common share, after preferred dividend requirements:</b>		
Loss before extraordinary item	\$ ( .46)	\$ ( .27)
<b>Net loss****</b>	<b>\$ ( .57)</b>	<b>\$ ( .27)</b>

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\* EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) presents business segment operating income before depreciation and amortization expense, including amortization relating to the \$1.4 billion acquisition of Warner Communications Inc. in 1989, the \$1.3 billion acquisition of the minority interest in American Television and Communications Corporation in 1992, and the \$1.4 billion acquisitions of KBLCOM Incorporated and Summit Communications Group, Inc. in 1995 and other business combinations accounted for by the purchase method. Although it is one way Wall Street measures cash flow, EBITDA is not adjusted for all noncash expenses or for working capital, capital expenditures and other investments requirements. EBITDA should be considered in addition to, not as a substitute for, other measures of financial performance and liquidity, as more fully discussed in Management's Discussion and Analysis included elsewhere herein. \*\* Reflects losses related to certain businesses and joint ventures owned by the Music Division which were restructured or closed. \*\*\* Deconsolidated as a result of the sale of a 51% interest in Six Flags effective as of June 23, 1995. \*\*\*\* The net loss for the year ended December 31, 1995 includes an extraordinary loss on the retirement of debt of \$42 million (\$.11 per common share).





# TIME WARNER

1995 ANNUAL REPORT

## Building Global Brands

### DEAR SHAREHOLDERS:

For Time Warner, 1995 was a year of important strategic achievements that will strengthen our growth prospects for years to come.

Understandably, the agreement to acquire the remaining 80% of Turner Broadcasting received the most attention, but all our initiatives were important to Time Warner's future. Thanks to our cable acquisitions, for example, we now have the best-clustered systems in many of the country's top markets. We strengthened our balance sheet and simplified our operating structure by bringing our entertainment properties under one management. With the decision by our international partners, ITOCHU and Toshiba, to become equity holders in Time Warner, we began restructuring our entertainment partnership.

The crowding of so many significant events into a single year shouldn't diminish a sense of their long-term impact. Together, they will help bring superior returns to shareholders. But before we look at these events in more depth, we should also remember that amid the changes, some things stayed the same. First and foremost, the immediate measure of our success continued to be found in the daily decisions of the millions of consumers around the world who turn to our brands and creative output for the best in entertainment and information.



Gerald M. Levin  
Chairman and Chief Executive Officer

**ANOTHER YEAR OF STRONG**

## PERFORMANCE

As a result, Time Warner had another year of outstanding operating performance. Four of our businesses achieved records. Excluding a one-time restructuring charge, Warner Music also posted a record year, its 12th in a row. Three -- Time Inc., Warner Bros. and Home Box Office (HBO) -- turned in double-digit growth. Cable returned to its traditional pattern of double-digit gains in the fourth quarter. The revenue slump inflicted on cable by reregulation, which was a prime factor in the sluggish performance of our stock, is clearly over.

The year ahead promises to be a good one. All our businesses are performing at or near the top of their industries. Their combined operating performance should continue to generate very healthy growth.

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### Management's Discussion and Analysis of Results of Operations and Financial Condition

Time Warner has interests in three fundamental areas of business: Entertainment, consisting principally of interests in recorded music and music publishing, filmed entertainment, broadcasting, theme parks and cable television programming; News and Information, consisting principally of interests in magazine publishing, book publishing and direct marketing; and Telecommunications, consisting principally of interests in cable television systems. Substantially all of Time Warner's interests in filmed entertainment, broadcasting, theme parks, cable television programming and most of its cable television systems are held through the Entertainment Group, consisting principally of TWE, which is not consolidated for financial reporting purposes. TWE manages the telecommunications properties owned by Time Warner and the combined cable television operations are conducted under the name of Time Warner Cable. Capitalized terms are as defined and described in the accompanying consolidated financial statements, or elsewhere herein.

#### Strategic Initiatives

#### Significant Transactions

During 1995, Time Warner and the Entertainment Group embarked on a program to improve their financial condition and increase their overall financial flexibility through the initiation of an asset sales program and significant debt refinancings. Time Warner and the Entertainment Group also pursued significant, strategic initiatives during 1995 through their cable television operations and through a proposed merger of Time Warner and TBS. These initiatives are part of a continuing strategy to further enhance the strength of Time Warner's interests in entertainment and news and information, and to attempt to use existing and acquired cable television systems to establish an enterprise that will be responsible for the overall management and financing of its cable and telecommunications interests. In pursuit of these strategic initiatives, Time Warner and the Entertainment Group announced or completed a number of transactions in 1995 and early 1996 that have had or are expected to have a significant effect on their results of operations and financial condition. Such transactions include:

- The September 1995 announcement of Time Warner's agreement to merge with TBS by acquiring the remaining 80% interest in TBS that it does not already own,
- The acquisitions by Time Warner of Summit, KBLCOM and CVI and related companies, and the formation by TWE of the TWE-Advance/Newhouse Partnership, which together strengthened the geographic clusters of the cable television systems and substantially increased the number of cable subscribers managed by Time Warner Cable (collectively, the "Cable Transactions");
- The exchange of ITOCHU's and Toshiba's interests in TWE for equity interests in Time Warner (the "ITOCHU/Toshiba Transaction");
- The refinancing of approximately \$4 billion of public debt by Time Warner and the execution



- of a new \$8.3 billion credit agreement, under which approximately \$2.7 billion of debt assumed in the Cable Transactions was refinanced by subsidiaries of Time Warner and \$2.6 billion of pre-existing bank debt was refinanced by TWE (the "Debt Refinancings"), and
- The sale by Time Warner and the Entertainment Group of certain assets under an asset sales program, which raised approximately \$1.6 billion on a combined basis for debt reduction, including the sale of 51% of TWE's interest in Six Flags (the "Six Flags Transaction") and the sale or expected sale or transfer of certain unclustered cable television systems owned by TWE (the "Unclustered Cable Transactions").

The nature of these transactions and their impact on the results of operations and financial condition of Time Warner and the Entertainment Group are further discussed below

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#### Telecommunications Strategy

In 1994, Time Warner embarked on a strategy to expand its cable television business, leading to agreements to combine with or acquire cable television systems serving approximately 3.7 million subscribers. This strategy was based on management's expectation that there would be a significant increase in the value of cable television systems related, in part, to a future convergence of the cable and telephone industries which would provide cable companies with an opportunity to operate large geographic clusters of cable television systems for purposes of maximizing the development and distribution of new and improved services on a cost efficient basis, such as increased channel capacity, high speed data transmission and telephony services.

During 1995 and with the acquisition of CVI and related companies in January 1996, Time Warner completed its plans for the expansion of its cable television business, thereby strengthening its geographic clusters of cable television systems as previously envisioned. Along with internal growth, the acquisitions of Summit, KBLCOM and CVI and related companies, as well as the formation of the TWE-Advance/Newhouse Partnership, increased the total number of subscribers under the management of Time Warner Cable to 11.7 million, as compared to 7.5 million subscribers at the end of 1994. Time Warner Cable has also extended its reach of cable television systems to neighborhoods passing 18 million homes or close to 20% of television homes in the U.S. In addition, there are now 35 geographic clusters of cable television systems serving over 100,000 subscribers each, including key markets such as New York City and State, central Florida and North Carolina. Time Warner does not currently plan to make any more significant acquisitions of cable television systems, but instead intends to continue to refine its geographic clusters by exchanging certain unclustered cable television systems for geographically-strategic ones or by selling non-strategic cable television systems as part of the Company's continuing asset sales program. Management continues to believe that the increased size and concentration of its subscriber base will provide for sustained revenue growth from new and improved services, and provide certain economies of scale relating to the upgrade of the technological capabilities of Time Warner Cable's cable television systems.

Management believes that the future convergence of the cable and telephone industries has been substantially confirmed through various events within the industry, including the February 1996 enactment into law of sweeping telecommunications industry reform. Among other features, the Telecommunications Act of 1996 effectively removes regulatory barriers that historically prohibited cable television companies and local and long-distance telephone companies from competing in each other's business. In addition, the new law eliminates most cable rate pricing restrictions in 1999, and earlier under certain circumstances. Time Warner expects that the relaxation of cable rate regulation in 1999, along with permitted cable rate price increases for certain regulated services that went into effect on January 1, 1996 under a separate Time Warner agreement with the Federal Communications Commission (the "FCC"), will provide enhanced pricing flexibility that will help finance its cable and telephony expansion plans.

The next phase of Time Warner's telecommunications strategy is to simplify the structure of its cable and telecommunications properties by bringing such properties together, so far as practicable and on a tax-efficient basis, into an enterprise that will be responsible for the overall management and financing of these interests. The first step of this process was completed in 1995 when ITOCHU

and Toshiba exchanged their interests in TWE for equity interests in Time Warner. The restructuring process depends, among other things, upon successful negotiations with U S WEST and certain creditors, and the receipt of franchise and other regulatory approvals. Accordingly, there can be no assurance that the effort will succeed. In the interim, as contemplated by the TWE-Advance/Newhouse Partnership agreement, Time Warner may transfer certain of its newly-acquired cable systems to the TWE-Advance/Newhouse Partnership on a tax-efficient basis. Such transfers, if they are made, are expected to be structured so that the systems will be transferred subject to a portion of Time Warner's debt, thereby reducing the financial leverage of Time Warner and increasing the under-leveraged capitalization of the TWE- Advance/Newhouse Partnership and consequently, TWE.

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# TIME WARNER

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#### TBS Transaction

With the announcement in September 1995 of Time Warner's plan to merge with TBS, Time Warner has taken a strategic step that would further enhance Time Warner's interests in entertainment and news and information assets while improving the balance between such interests and its interests in the telecommunications business. The addition of TBS' news and entertainment programming networks, film and cartoon libraries, film production companies and sports franchises is expected to complement virtually all of Time Warner's business interests and expand the emphasis on growth through Time Warner's interests in its entertainment and news and information businesses.

The TBS Transaction provides for the merger of each of Time Warner and TBS with separate subsidiaries of a holding company ("New Time Warner") that will combine, for financial reporting purposes, the consolidated net assets and operating results of Time Warner and TBS. Based on TBS' financial position and results of operations as of and for the year ended December 31, 1995, and giving pro forma effect to the TBS Transaction as if it had occurred on December 31, 1995 for balance sheet purposes and at the beginning of the year for statement of operations purposes, the incremental effect on Time Warner reflected in the combined pro forma financial statements of New Time Warner would have been (i) an increase in shareholder's equity of approximately \$7.3 billion, principally due to the issuance by New Time Warner of approximately 177.8 million shares of common stock, (ii) an increase in long-term debt of approximately \$2.5 billion due to the assumption of TBS' debt, (iii) an increase in goodwill of approximately \$7.9 billion as a result of a preliminary allocation of the excess cost over the net book value of assets acquired, (iv) an increase in revenues of \$3.4 billion, (v) an increase in EBITDA (as defined below) of \$524 million, (vi) an increase in depreciation and amortization of \$377 million, including approximately \$200 million of noncash amortization of goodwill, (vii) an increase in operating income of \$147 million, (viii) an increase in net loss of \$111 million and (ix) a reduction in net loss per common share of \$ .12 per common share resulting from the dilutive effect of issuing 177.8 million shares of common stock.

The TBS Transaction is subject to customary closing conditions, including the approval of the shareholders of TBS and of Time Warner, all necessary approvals of the FCC and appropriate antitrust approvals. There can be no assurance that all these approvals can be obtained or, in the case of governmental approvals, if obtained, will not be conditioned upon changes to the terms of the merger agreement or related agreements.

#### Use of EBITDA

The following comparative discussion of the results of operations and financial condition of Time Warner and the Entertainment Group includes, among other factors, an analysis of changes in the operating income of the business segments before depreciation and amortization ("EBITDA") in order to eliminate the effect on the operating performance of the music, filmed entertainment and cable businesses of significant amounts of amortization of intangible assets recognized in the \$14 billion acquisition of WCI in 1989, the \$1.3 billion acquisition of the ATC minority interest in 1992, the \$1.4 billion acquisitions of KBLCOM and Summit in 1995 and other business combinations accounted for by the purchase method, including the \$904 million acquisition of CVI and related companies in January 1996 and the proposed TBS merger with respect to certain discussions on a

pro forma basis. Financial analysts generally consider EBITDA to be an important measure of comparative operating performance for the businesses of Time Warner and the Entertainment Group, and when used in comparison to debt levels or the coverage of interest expense, as a measure of liquidity. However, EBITDA should be considered in addition to, not as a substitute for, operating costs.

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### RESULTS OF OPERATIONS

1995 vs. 1994

Time Warner had revenues of \$8.067 billion, a loss of \$124 million (\$ .46 per common share) before an extraordinary loss on the retirement of debt and a net loss of \$166 million (\$ .57 per common share) in 1995, compared to revenues of \$7.396 billion and a net loss of \$91 million (\$ .27 per common share) in 1994.

The increase in Time Warner's net loss in 1995 was principally related to a \$42 million extraordinary loss on the retirement of debt (\$.11 per common share) and \$85 million in pretax losses (\$52 million after taxes and \$.13 per common share) related to certain businesses and joint ventures owned by the Music Division which were restructured or closed. As discussed more fully below, the increase in Time Warner's net loss in 1995 from such losses was principally mitigated by an overall increase in the fundamental operating income of Time Warner's business segments and increased income from its equity in the pretax income of the Entertainment Group, offset in part by a decrease in investment-related income and higher interest expense on approximately \$1.3 billion of debt assumed in the cable acquisitions. The increase in Time Warner's net loss per common share in 1995 also related to an increase in preferred dividend requirements to \$52 million from \$13 million in 1994 as a result of the preferred stock issued in connection with the 1995 cable acquisitions and the ITOCHU/Toshiba Transaction.

Time Warner's equity in the pretax income of the Entertainment Group was \$256 million in 1995, compared to \$176 million in 1994. As discussed more fully below, the Entertainment Group's operating results in 1995 reflect an overall increase in operating income generated by its business segments (including the contribution by the TWE-Advance/Newhouse Partnership) and an increase in investment-related income resulting from gains on the sale of certain unclustered cable systems and other investments, offset in part by minority interest expense related to the consolidation of the operating results of the TWE-Advance/Newhouse Partnership effective as of April 1, 1995.

On a pro forma basis, giving effect to (i) the Cable Transactions, (ii) the ITOCHU/Toshiba Transaction, (iii) the Debt Refinancings, (iv) the Six Flags Transaction and (v) the Unclustered Cable Transactions, as if each of such transactions had occurred at the beginning of the periods, Time Warner would have reported for the years ended December 31, 1995 and 1994, revenues of \$8.742 billion and \$8.217 billion, depreciation and amortization of \$935 million and \$906 million, operating income of \$600 million and \$653 million, equity in the pretax income of the Entertainment Group of \$286 million and \$205 million, a loss before extraordinary item of \$255 million and \$266 million (\$1.02 and \$1.07 per common share) and a net loss of \$297 million and \$266 million (\$1.13 and \$1.07 per common share), respectively. The 1995 to 1994 comparison of pro forma results are similarly affected by any underlying historical trends that are unrelated to the transactions given pro forma effect to therein, such as the \$85 million in pretax Music Division losses discussed above. The increase in pro forma over historical losses before extraordinary items for each period is principally the result of approximately \$230 million in annualized noncash amortization of certain intangible assets recognized in the cable acquisitions which is not fully offset by the pro forma effects of other improved net operating results, a component of which is the pro forma benefit from the net addition of over \$400 million in annualized EBITDA.

On a pro forma basis, giving effect to (i) the formation of the TWE-Advance/Newhouse



Partnership, (ii) the refinancing of approximately \$2.6 billion of pre-existing bank debt, (iii) the consolidation of Paragon, (iv) the Six Flags Transaction and (v) the Unclustered Cable Transactions, as if each of such transactions had occurred at the beginning of the periods, the Entertainment Group would have reported for the years ended December 31, 1995 and 1994, revenues of \$9.686 billion and \$8.778 billion, depreciation and amortization of \$1.078 billion and \$1.038 billion, operating income of \$994 million and \$923 million, income before extraordinary item of \$203 million and \$171 million and net income of \$179 million and

\$171 million, respectively. The 1995 to 1994 comparison of pro forma results are similarly affected by any underlying historical trends that are unrelated to the transactions given pro forma effect to therein. The increase in pro forma over historical net income for each period principally results from the pro forma effects of a full year contribution by the TWE-Advance/Newhouse Partnership, and interest savings associated with the refinancing of TWE's bank debt and lower debt levels resulting from asset sales.

The relationship between income before income taxes and income tax expense of Time Warner is principally affected by the amortization of goodwill and certain other financial statement expenses that are not deductible for income tax purposes. Income tax expense of Time Warner includes all income taxes related to its allocable share of partnership income and its equity in the income tax expense of corporate subsidiaries of the Entertainment Group.

EBITDA and operating income for Time Warner and the Entertainment Group in 1995 and 1994 are as follows:

Year Ended (millions)	EBITDA		Operating Income	
	1995	1994	1995	1994
<b>Time Warner</b>				
Publishing	\$ 476	\$ 430	\$ 381	\$ 347
Music*	690	720	321	366
Cable	90	-	(5)	-
<b>Total</b>	<b>\$1,256</b>	<b>\$1,150</b>	<b>\$697</b>	<b>\$713</b>
<b>Entertainment Group</b>				
Filmed Entertainment	\$490	\$430	\$253	\$219
Six Flags Theme Parks	60	135	29	56
Broadcasting - The WB Network	(66)	-	(66)	-
Programming - HBO	293	257	274	237
Cable	1,275	989	502	341
<b>Total</b>	<b>\$2,052</b>	<b>\$1,811</b>	<b>\$992</b>	<b>\$852</b>

\* Includes pretax losses of \$85 million recorded in 1995 related to certain businesses and joint ventures owned by the Music Division which were restructured or closed.

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## Building Global Brands

TIME WARNER  
Publishing

Revenues increased to \$3.722 billion, compared to \$3.433 billion in 1994. EBITDA increased to \$476 million from \$430 million. Depreciation and amortization amounted to \$95 million in 1995 and \$83 million in 1994. Operating income increased to \$381 million from \$347 million. Revenues benefited from increases in magazine circulation, advertising and book revenues. Contributing to the revenue gain were increases achieved by People, Sports Illustrated, Fortune and book publisher Oxmoor House. EBITDA and operating income increased as a result of the revenue gains, offset in part by significantly higher postal and paper costs as a result of price increases.

### Music

Revenues increased to \$4.196 billion, compared to \$3.986 billion in 1994. EBITDA decreased to \$690 million from \$720 million. Depreciation and amortization, including amortization related to the purchase of WCI, amounted to \$369 million in 1995 and \$354 million in 1994. Operating income decreased to \$321 million from \$366 million. Operating results were adversely affected by \$85 million in losses recorded in 1995 that related to certain businesses and joint ventures owned by the Music Division which were restructured or closed. Revenues for 1995 were negatively affected by certain reclassifications relating to third party, pressing and distribution arrangements and changes in the Music Division's ownership interests in certain investments and subsidiaries that resulted in changes from the consolidation to the equity method of accounting. Excluding the effects from such reclassifications and changes, revenues from the fundamental business increased by approximately 6%, principally as a result of increases in both domestic and international recorded music revenues and increased music publishing revenues. Domestic and international recorded music revenues benefited from a number of popular releases and an increase in the percentage of compact disc to total unit sales. Excluding the \$85 million in losses, EBITDA increased, and operating income benefited, principally from the revenue gains and interest income on the resolution of a recorded music tax matter, offset in part by expenses incurred in connection with the settlement of certain employment contracts and lower results from direct marketing activities attributable to higher amortization of member acquisition costs.

The losses relating to certain businesses and joint ventures that were restructured or closed are primarily related to Warner Music Enterprises, one of the Company's direct marketing efforts, and the write off of its related direct mail order assets that were not recoverable due to the closure of this business. Such closure was substantially completed in 1995 and will not require any significant, future cash outlays. The activities that will not be continued have not been material to historical operating results and are not expected to significantly affect the results of future operations.

### Cable

As a result of Time Warner's acquisitions of KBLCOM and Summit in 1995, cable operating results for 1995 included revenues of \$172 million, EBITDA of \$90 million, depreciation and amortization of \$95 million and an operating loss of \$5 million. Moderate operating losses are expected to continue in 1996 because of the full year effect of approximately \$230 million of noncash amortization of certain intangible assets recognized in Time Warner's acquisitions of KBLCOM and Summit in 1995, and CVI and related companies in 1996.

### Interest and Other, Net

Interest and other, net, increased to \$877 million in 1995, compared to \$724 million in 1994. Interest expense increased to \$877 million, compared to \$769 million, principally as a result of approximately \$1.3 billion of debt assumed in the cable acquisitions and higher short-term, floating-rates of interest paid on \$2.6 billion notional amount of interest rate swap contracts. Other income, net, was immaterial in 1995, compared to \$45 million in 1994, principally because of a decrease in investment-related income. Investment-related income in both periods consisted of gains on the sale of certain assets, including the sale of an interest in QVC, Inc. in 1995, which were offset by losses from reductions in the carrying value of certain investments taken in each period.

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ENTERTAINMENT GROUP

### Filmed Entertainment

Revenues increased to \$5.078 billion, compared to \$4.484 billion in 1994. EBITDA increased to \$490 million from \$430 million. Depreciation and amortization, including amortization related to the purchase of WCI, amounted to \$237 million in 1995 and \$211 million in 1994. Operating income increased to \$253 million from \$219 million. Revenues benefited from increases in worldwide theatrical, home video, consumer products and television distribution operations. Worldwide theatrical and domestic home video revenues in 1995 were led by the success of *Batman Forever*. EBITDA and operating income benefited from the revenue gains and increased income from licensing operations.

### Six Flags Theme Parks

As a result of TWE's sale of 51% of its interest in Six Flags, the operating results of Six Flags have been deconsolidated effective as of June 23, 1995 and TWE's remaining 49% interest in Six Flags is accounted for under the equity method of accounting. Accordingly, revenues decreased to \$227 million, compared to \$557 million in 1994. EBITDA decreased to \$60 million from \$135 million. Depreciation and amortization amounted to \$31 million in 1995 and \$79 million in 1994. Operating income decreased to \$29 million from \$56 million.

### Broadcasting - The WB Network

The WB Network was launched in January 1995, and generated \$66 million of operating losses on \$33 million of revenues. The operating loss was mitigated by a favorable legal settlement, as well as by funding from a limited partner admitted as of August 1995. Due to the start-up nature of this new national broadcast operation, losses are expected to continue.

### Programming - HBO

Revenues increased to \$1.607 billion, compared to \$1.513 billion in 1994. EBITDA increased to \$293 million from \$257 million. Depreciation and amortization amounted to \$19 million in 1995 and \$20 million in 1994. Operating income increased to \$274 million from \$237 million. Revenues benefited primarily from an increase in subscriptions to 29.7 million from 27 million at the end of 1994, as well as from higher pay-TV rates. EBITDA and operating income improved principally as a result of the revenue gains.

### Cable

Revenues increased to \$3.094 billion, compared to \$2.242 billion in 1994. EBITDA increased to \$1.275 billion from \$989 million. Depreciation and amortization, including amortization related to the purchase of WCI and the acquisition of the ATC minority interest, amounted to \$773 million in 1995 and \$649 million in 1994. Operating income increased to \$502 million from \$340 million. Revenues and operating results benefited from the formation of the TWE-Advance/Newhouse Partnership on April 1, 1995 and the consolidation of Paragon effective as of July 6, 1995. Excluding such effects, revenues benefited from an aggregate increase in basic cable and Primestar-related, direct broadcast satellite subscribers that approached 6% and increases in

nonregulated revenues, including pay-TV, pay-per-view and advertising. Excluding the positive contributions from the TWE-Advance/Newhouse Partnership and the consolidation of Paragon, EBITDA and operating income increased as a result of the revenue gains, offset in part by the full year impact of the second round of cable rate regulations that went into effect in July 1994, higher start-up costs for telephony operations and, with respect to operating income only, higher depreciation and amortization relating to increased capital spending.

#### Interest and Other, Net

Interest and other, net, decreased to \$539 million in 1995, compared to \$616 million in 1994. Interest expense increased to \$579 million, compared to \$567 million in 1994, principally as a result of higher short-term, floating-rates of interest paid on borrowings under TWE's former and existing bank credit agreements, offset in part by interest savings in the last quarter of 1995 on lower debt levels related to management's asset sales program. There was other income, net, of \$40 million in 1995, compared to other expense, net, of \$49 million in 1994, principally because of an increase in investment-related income related to gains on the sale of certain unclustered cable systems and other investments.

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# TIME WARNER

## 1994 ANNUAL REPORT

### Building Global Brands

1994 vs. 1993

Time Warner had revenues of \$7.396 billion and a net loss of \$91 million (\$.27 per common share) in 1994, compared to revenues of \$6.581 billion and a net loss of \$221 million (\$.90 per common share) in 1993. Included in the 1993 results is an extraordinary loss on the retirement of debt of \$57 million (\$.15 per common share) and a one-time tax charge of \$70 million (\$.19 per common share) that resulted from the effect on the Company's deferred income tax liability of the increase in the corporate income tax rate enacted in August 1993.

As discussed more fully below, the improvement in Time Warner's net loss in 1994 reflected an overall increase in operating income generated by its business segments and an increase in investment related income, offset in part by higher interest expense and lower income from Time Warner's equity in the pretax income of the Entertainment Group. The improvement in Time Warner's 1994 net loss also related to the absence of the extraordinary loss and one-time tax charge that were recorded in 1993. The improvement in Time Warner's net loss per common share in 1994 further resulted from a \$105 million reduction in preferred dividend requirements relating to Time Warner's 1993 redemption or exchange of \$5.6 billion of preferred stock for debt.

Time Warner's equity in the pretax income of the Entertainment Group was \$176 million in 1994, compared to \$281 million in 1993. As discussed more fully below, the Entertainment Group's operating results in 1994 reflected an overall decrease in operating income generated by its business segments, principally relating to lower Cable results due to cable rate regulation, and an increase in investment-related and foreign currency contract losses, offset in part by an increase in interest income.

EBITDA and operating income for Time Warner and the Entertainment Group in 1994 and 1993 are as follows:

Year Ended (millions)	EBITDA		Operating Income	
	1994	1993	1994	1993
<b>Time Warner</b>				
Publishing	\$430	\$372	\$347	\$295
Music	720	643	366	296
<b>Total</b>	<b>\$1,150</b>	<b>\$1,015</b>	<b>\$713</b>	<b>\$591</b>
<b>Entertainment Group</b>				
Filmed Entertainment	\$430	\$427	\$219	\$233
Six Flags Theme Parks	135	122	56	53
Programming - HBO Cable	257	230	237	213

Cable 989 1,035 340 406

Total \$1,911 \$1,814 \$852 \$905

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# TIME WARNER

## 1995 ANNUAL REPORT

### Building Global Brands

#### TIME WARNER

##### Publishing

Revenues increased to \$3.433 billion, compared to \$3.270 billion in 1993. EBITDA increased to \$430 million from \$372 million. Depreciation and amortization amounted to \$83 million in 1994 and \$77 million in 1993. Operating income increased to \$347 million from \$295 million. Revenues benefited principally from increases in magazine advertising and circulation revenues, which were aided in part by several special issues during 1994. Significant revenue gains were achieved by *People*, *Sports Illustrated* and *Southern Living*. EBITDA, operating income and operating margins improved principally as a result of the revenue gains and continued cost containment.

##### Music

Revenues increased to \$3.986 billion, compared to \$3.334 billion in 1993. EBITDA increased to \$720 million from \$643 million. Depreciation and amortization, including amortization related to the purchase of WCI, amounted to \$354 million in 1994 and \$347 million in 1993. Operating income increased to \$366 million from \$296 million. The revenue growth resulted from increases in both domestic and international recorded music revenues, which benefited from a number of popular releases during the year and an increase in the percentage of compact disc to total unit sales, and increased music publishing revenues. EBITDA and operating income benefited from these revenue gains and increased results from direct marketing activities attributable to new members and lower amortization of member acquisition costs, offset in part by costs associated with the reorganization of the domestic music companies and continuing investment in new business ventures.

##### Interest and Other, Net

Interest and other, net, increased to \$724 million in 1994, compared to \$718 million in 1993. Interest expense increased to \$769 million from \$698 million as a result of a full twelve months of interest on the debt issued during the first three months of 1993 to redeem or exchange preferred stock, offset in part by savings from lower-cost debt used to fund the redemption of certain notes and debentures in 1993. There was other income, net, of \$45 million in 1994, compared to other expense, net, of \$20 million in 1993, principally because of an increase in investment-related income, including an increase in the amortization of the excess of the Time Warner General Partners' interest in the net assets of TWE over the net book value of their investment in TWE to reflect U S WEST as a partner for a full year. Investment-related income was reduced in part in both years by adjustments to the carrying value of certain investments, expenses in connection with the settlement of certain employment contracts and losses on foreign exchange contracts used to hedge foreign exchange risk.

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# TIME WARNER

1995 ANNUAL REPORT

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ENTERTAINMENT GROUP

### Filmed Entertainment

Revenues increased to \$4.484 billion, compared to \$4.032 billion in 1993. EBITDA increased to \$430 million from \$427 million. Depreciation and amortization, including amortization related to the purchase of WCI, amounted to \$211 million in 1994 and \$194 million in 1993. Operating income decreased to \$219 million from \$233 million. Worldwide home video, syndication and consumer products revenues increased at Warner Bros., offset in part by lower worldwide theatrical revenues. EBITDA and operating income margins decreased principally as a result of lower theatrical results in comparison to the exceptionally strong theatrical results in 1993.

### Six Flags Theme Parks

Revenues increased to \$557 million, compared to \$533 million in 1993. EBITDA increased to \$135 million from \$122 million. Depreciation and amortization amounted to \$79 million in 1994 and \$69 million in 1993. Operating income increased to \$56 million from \$53 million. Revenues increased as a result of overall attendance growth and higher revenues per visitor. EBITDA and operating income improved principally as a result of the revenue gains.

### Programming - HBO

Revenues increased to \$1.513 billion, compared to \$1.441 billion in 1993. EBITDA increased to \$257 million from \$230 million. Depreciation and amortization amounted to \$20 million in 1994 and \$17 million in 1993. Operating income increased to \$237 million from \$213 million. Revenues benefited from an increase in subscriptions and higher pay-TV rates. EBITDA, operating income and operating margins improved principally as a result of the revenue gains.

### Cable

Revenues increased to \$2.242 billion, compared to \$2.208 billion in 1993. EBITDA decreased to \$989 million from \$1.035 billion. Depreciation and amortization, including amortization related to the purchase of WCI and the acquisition of the ATC minority interest, amounted to \$649 million in 1994 and \$629 million in 1993. Operating income decreased to \$340 million from \$406 million. Revenues and operating results in 1994 were adversely affected by two rounds of cable rate regulation that in general reduced the rates cable operators are allowed to charge for regulated services, the first of which went into effect in September 1993 and the second of which went into effect in July 1994. The unfavorable effects of rate regulation were offset in part by an increase in subscribers and nonregulated revenues. Actions that were undertaken to mitigate the impact of rate regulation included a number of cost containment measures and a continued emphasis on near and long-term strategies to increase revenues from unregulated services.

### Interest and Other, Net

Interest and other, net, increased to \$616 million in 1994, compared to \$564 million in 1993. Interest expense decreased to \$567 million, compared with \$580 million in 1993. There was other expense, net, of \$49 million in 1994, compared to other income, net, of \$16 million in 1993. Investment-related and foreign currency contract losses in 1994 exceeded an increase in interest

income on higher cash balances and the interest-bearing note receivable from U S WEST. In 1993, other income, net, benefited from a gain on the sale of certain assets and other investment-related income, which more than offset investment losses.

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# TIME WARNER

1995 ANNUAL REPORT

## Building Global Brands

### FINANCIAL CONDITION AND LIQUIDITY

December 31, 1995

#### TIME WARNER

##### 1995 Financial Condition

Time Warner had \$9.9 billion of debt, \$949 million of mandatorily redeemable preferred securities of subsidiaries, \$1.2 billion of cash and equivalents (net debt of \$8.7 billion), and \$3.7 billion of shareholders' equity at December 31, 1995, compared to \$9.2 billion of debt, \$282 million of cash and equivalents (net debt of \$8.9 billion), and \$1.1 billion of shareholders' equity at December 31, 1994. The increase in debt principally reflects the assumption of approximately \$1.3 billion of debt related to the Cable Transactions, offset in part by debt reductions using proceeds raised from the asset sales program, including proceeds from the issuance of the PERCS which monetized Time Warner's 14% investment in Hasbro. The increase in mandatorily redeemable preferred securities of subsidiaries reflects the issuance in 1995 of the PERCS and Preferred Trust Securities, the proceeds of which were used to reduce certain indebtedness of Time Warner. The noncurrent cash and equivalents consist of the net proceeds received from the issuance of the Preferred Trust Securities in December 1995, which were used in the redemption of the 8.75% Convertible Debentures in early 1996. The increase in shareholders' equity reflects the issuance in 1995 of approximately 2.5 million shares of common stock and approximately 29.3 million shares of preferred stock in connection with the ITOCHU/Toshiba Transaction and the acquisitions of KBL.COM and Summit. On a combined basis (Time Warner and the Entertainment Group together), there was \$14.7 billion of net debt at December 31, 1995, compared to \$15 billion of net debt at the beginning of the year.

##### Investment in TWE

Time Warner's investment in TWE at December 31, 1995 consists of 74.49% of TWE's pro rata priority capital and residual equity capital, and 100% of TWE's senior priority capital and junior priority capital. Such priority capital interests provide Time Warner, and with respect to the pro rata priority capital only, U S West, with certain priority claims to the net partnership income of TWE and distributions of TWE partnership capital, including certain priority distributions of partnership capital in the event of liquidation or dissolution of TWE. Each level of priority capital interest provides for an annual rate of return equal to or exceeding 8%, including an above-market 13.25% annual rate of return (11.25% to the extent concurrently distributed) related to Time Warner's junior priority capital interest, which represents Cumulative Priority Capital of \$4.6 billion at December 31, 1995. While the TWE partnership agreement contemplates the reinvestment of significant partnership cash flows in the form of capital expenditures and otherwise provides for certain other restrictions that are expected to limit cash distributions on partnership interests for the foreseeable future, Time Warner's \$1.4 billion senior priority capital interest and, to the extent not previously distributed, partnership income allocated thereto (based on an 8% annual rate of return) is required to be distributed to Time Warner in three annual installments beginning on July 1, 1997. In 1995, Time Warner received a \$366 million cash distribution from TWE representing the priority capital return allocated to its senior priority capital interest through June 30, 1995.

## Credit Agreement Refinancings

In connection with the Cable Transactions, TWI Cable, TWE and the TWE-Advance/Newhouse Partnership executed a five-year revolving credit facility in June 1995. The New Credit Agreement enabled such entities to refinance certain indebtedness assumed in the Cable Transactions, to refinance TWE's indebtedness under a pre-existing bank credit agreement and to finance the ongoing working capital, capital expenditure and other corporate needs of each borrower.

The New Credit Agreement permits borrowings in an aggregate amount of up to \$8.3 billion, with no scheduled reductions in credit availability prior to maturity. Borrowings are limited to \$4 billion in the case of TWI Cable, \$5 billion in the case of the TWE-Advance/Newhouse Partnership and \$8.3 billion in the case of TWE, subject in each case to certain limitations and adjustments. Such borrowings bear interest at specific rates for each of the three borrowers, generally equal to LIBOR plus a margin initially ranging from 50 to 87.5 basis points, which margin will vary based on the credit rating or financial leverage of the applicable borrower. Unused credit is available for general business purposes and to support any commercial paper borrowings. Each borrower is required to pay a commitment fee initially ranging from 2% to 35% per annum on the unused portion of its commitment. TWI Cable may also be required to pay an annual facility fee equal to 187.5% of the entire amount of its commitment, depending on the level of its financial leverage in any given year. The New Credit Agreement contains certain covenants for each borrower relating to, among other things, additional indebtedness, liens on assets, cash flow coverage and leverage ratios, and loans, advances, distributions and other cash payments or transfers of assets from the borrowers to their respective partners or affiliates.

In July 1995, TWI Cable borrowed approximately \$1.2 billion under the New Credit Agreement to refinance certain indebtedness assumed or incurred in the acquisition of KBLCOM, and TWE borrowed approximately \$2.6 billion to repay and terminate its pre-existing bank credit agreement. An additional \$1.5 billion was borrowed by TWI Cable under the New Credit Agreement in January 1996 to refinance certain indebtedness assumed or incurred in the acquisition of CVI and related companies.

## Public Debt Refinancings

In 1995 and early 1996, Time Warner refinanced approximately \$4 billion of its public debt, thereby increasing its financial flexibility through lowering interest rates, extending debt maturities and eliminating potential dilution from the conversion of its 8.75% Convertible Debentures into 46.6 million shares of common stock. The outstanding 8.75% Convertible Debentures were redeemed in two tranches: \$1 billion principal amount in September 1995 for \$1.06 billion (including redemption premiums and accrued interest) and the remaining \$1.2 billion principal amount in February 1996 for \$1.28 billion (including redemption premiums and accrued interest). The September 1995 redemption was financed with proceeds from a \$500 million issuance of 7.75% ten-year notes in June 1995, proceeds from a \$374 million issuance of the PERCS in August 1995 and available cash and equivalents. The February 1996 redemption was financed with proceeds raised from a \$575 million issuance of the Preferred Trust Securities in December 1995 and proceeds from a \$750 million issuance of certain debentures in January 1996. In connection therewith, Time Warner recognized an extraordinary loss of \$26 million in February 1996.

In August 1995, Time Warner redeemed all of its \$1.8 billion principal amount of outstanding Reset Notes in exchange for new securities, consisting of approximately \$454 million aggregate principal amount of Floating Rate Notes due August 15, 2000, approximately \$272 million aggregate principal amount of 7.975% Notes due August 15, 2004, approximately \$545 million aggregate principal amount of 8.11% Debentures due August 15, 2006, and approximately \$545 million aggregate principal amount of 8.18% Debentures due August 15, 2007.

## Asset Sales

As part of a continuing strategy to enhance the financial position and credit statistics of Time Warner and the Entertainment Group, an asset sales program was initiated in 1995. Including the sale of 51% of TWE's interest in Six Flags in June 1995, the sale of an interest in QVC, Inc. in February 1995, the sale or expected sale of certain unclustered cable systems and the proceeds raised from the monetization of Time Warner's investment in Hasbro in August 1995, Time Warner and the Entertainment Group on a combined basis have completed or entered into transactions that raised approximately \$1.6 billion for debt reduction, all of which were completed in 1995 except for certain transactions aggregating approximately \$170 million which are expected to close in 1996.

## Credit Statistics

The combination of asset sales and debt refinancings is intended to strengthen the financial position of Time Warner and the Entertainment Group and, when taken together with EBITDA growth, is expected to continue the improvement of Time Warner's overall credit statistics. These credit statistics consist of commonly-used liquidity measures such as leverage and coverage ratios. The leverage ratio represents the ratio of total debt, less cash ("Net debt") to total business segment EBITDA, less corporate expenses ("Adjusted EBITDA"). The coverage ratio represents the ratio of Adjusted EBITDA to total interest expense and/or preferred dividends. Those ratios, on a pro forma basis for 1995 and on an historical basis for 1994 and 1993, are as set forth below for each of Time Warner and Time Warner and the Entertainment Group combined. Certain rating agencies and other credit analysts place more emphasis on the combined ratios while others place more emphasis on the Time Warner stand-alone ratios. It should be understood, however, that the assets of the Entertainment Group are not freely available to fund the cash needs of Time Warner.

		Pro Forma*		Historical
<b>Time Warner</b>		1995	1994	1993
Net debt/Adjusted EBITDA		7.0x	8.3x	9.8x
Adjusted EBITDA/Interest*		1.6x	1.4x	1.3x
Adjusted EBITDA/Interest and preferred dividends**		1.3x	1.4x	1.2x
<b>Time Warner and Entertainment Group combined</b>				
Net Debt/Adjusted EBITDA		4.7x	5.3x	5.6x
Adjusted EBITDA/Interest		2.4x	5.3x	5.6x
Adjusted EBITDA/Interest and preferred dividends***		2.1x	2.1x	1.9x

\* Pro forma ratios for 1995 give effect to the Cable Transactions, the ITOCHU/Toshiba Transaction, the Debt Refinancings, the Six Flags Transaction and the Unclustered Cable Transactions, and with respect to Time Warner and the Entertainment Group combined only, the consolidation of Paragon, as if each of such transactions occurred at the beginning of 1995.



Although not reflected therein, the TBS Transaction is not expected to significantly affect the pro forma ratios presented above. Historical ratios for 1995 are not meaningful and have not been presented because they reflect the operating results of acquired or disposed entities for only a portion of the year in comparison to year-end net debt levels.

\*\* Excludes interest of \$28 million in 1995 and \$12 million in 1994 which was paid to TWE in connection with borrowings under Time Warner's \$400 million credit agreement with TWE.

\*\*\* Includes preferred dividends of \$11 million in 1995 in connection with Company-obligated mandatorily redeemable preferred securities of subsidiaries and on a pro forma basis, an incremental \$91 million of preferred dividends related to the preferred stock issued in the Cable Transactions and the ITOCHU/Toshiba Transaction.

### Cash Flows

During 1995, Time Warner's cash provided by operations amounted to \$1.051 billion and reflected \$1.256 billion of EBITDA from its Publishing, Music and Cable businesses, \$1.063 billion of net distributions from TWE and \$35 million from the securitization of receivables, less \$659 million of interest payments, \$278 million of income taxes, \$74 million of corporate expenses and \$292 million related to an increase in other working capital requirements, balance sheet accounts and noncash items. Cash provided by operations of \$473 million in 1994 reflected \$1.150 billion of EBITDA from the Publishing

Cash used by investing activities, excluding investment proceeds, increased to \$647 million in 1995, compared to \$351 million in 1994, principally as a result of higher investment spending by Time Warner's business segments. As a result of management's asset sales program, investment proceeds increased to \$376 million in 1995, compared to \$118 million in 1994.

Cash provided by financing activities was \$123 million in 1995, compared to cash used by financing activities of \$158 million in 1994, principally as a result of the receipt of proceeds from the issuance of the Preferred Trust Securities in December 1995, offset in part by the use of available cash and equivalents to redeem a portion of the 8.75% Convertible Debentures in September 1995. In addition, cash dividends paid increased to \$171 million in 1995, compared to \$142 million in 1994.

The assets and cash flows of TWE are restricted by the TWE partnership agreement and are unavailable to Time Warner except through the payment of certain fees, reimbursements, cash distributions and loans, which are subject to limitations. Under the New Credit Agreement, TWE and TWI Cable are permitted to incur additional indebtedness to make loans, advances, distributions and other cash payments to Time Warner, subject to their respective compliance with the cash flow coverage and leverage ratio covenants contained therein.

Management believes that Time Warner's operating cash flow, cash and marketable securities and additional borrowing capacity are sufficient to fund its capital and liquidity needs for the foreseeable future without distributions and loans from TWE above those permitted by existing agreements.

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# TIME WARNER

## 1995 ANNUAL REPORT

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#### ENTERTAINMENT GROUP

#### 1995 Financial Condition

The financial condition of the Entertainment Group, principally TWE, at December 31, 1995 was affected by the formation of the TWE-Advance/Newhouse Partnership, the Six Flags Transaction and the consolidation of Paragon. The Entertainment Group had \$6.2 billion of debt, \$1.4 billion of Time Warner General Partners' senior priority capital and \$6.6 billion of partners' capital (net of the \$169 million uncollected portion of the note receivable from U.S. WEST) at December 31, 1995, compared to \$7.2 billion of debt, \$1.7 billion of Time Warner General Partners' senior priority capital and \$6.5 billion of partners' capital at December 31, 1994. The \$1 billion reduction in debt resulted principally from the Six Flags Transaction. In addition, principally as a result of the payment of over \$1 billion of distributions to Time Warner in 1995, cash and equivalents decreased to \$209 million at December 31, 1995, compared to \$1.1 billion at December 31, 1994, reducing the debt-net-of-cash amounts for the Entertainment Group to \$6 billion and \$6.1 billion, respectively.

#### Credit Statistics

Principally as a result of the formation of the TWE-Advance/Newhouse Partnership and the Six Flags Transaction, the Entertainment Group's leverage and coverage ratios improved in 1995 on a pro forma basis, as set forth below:

	Pro Forma* 1995	Historical 1994 1993
Net debt/Adjusted EBITDA	3.0x	3.5x 3.3x
Adjusted EBITDA/Interest	3.8x	3.1x 3.0x

\* Pro forma ratios for 1995 give effect to the formation of the TWE-Advance/Newhouse Partnership, the refinancing of approximately \$2.6 billion of pre-existing bank debt, the consolidation of Paragon, the Six Flags Transaction and the Unclassified Cable Transactions, as if each of such transactions had occurred at the beginning of 1995. Historical ratios for 1995 are not meaningful and have not been presented because they reflect the operating results of acquired or disposed entities for only a portion of the year in comparison to year-end net debt levels.

Such ratios may be adversely affected upon the transfer of certain of Time Warner's newly-acquired cable systems to the TWE-Advance/Newhouse Partnership, which, if completed, is expected to be structured so that the systems will be transferred subject to a portion of Time Warner's debt, thereby reducing the financial leverage of Time Warner and increasing the under-leveraged capitalization of the TWE-Advance/Newhouse Partnership and consequently, TWE.

#### Cash Flows

In 1995, the Entertainment Group's cash provided by operations amounted to \$1.495 billion and reflected \$2.052 billion of EBITDA from the Filmed Entertainment, Six Flags Theme Parks, Broadcasting-The WB Network, Programming-HBO and Cable businesses and \$159 million related to a reduction in working capital requirements, other balance sheet accounts and noncash items, less \$577 million of interest payments, \$75 million of income taxes and \$64 million of corporate expenses. Cash provided by operations of \$1.341 billion in 1994 reflected \$1.811 billion of business segment EBITDA and \$180 million related to a reduction in working capital requirements, other balance sheet accounts and noncash items, less \$521 million of interest payments, \$69 million of income taxes and \$60 million of corporate expenses.

Cash used by investing activities decreased to \$750 million in 1995, compared to \$1.770 billion in 1994, principally as a result of a \$1.1 billion increase in investment proceeds relating to management's asset sales program. Capital expenditures increased to \$1.653 billion in 1995, compared to \$1.235 billion in 1994, principally as a result of higher capital spending by the Cable Division.

Cash used by financing activities was \$1.607 billion in 1995, compared to cash provided by financing activities of \$162 million in 1994, principally as a result of an approximate \$1 billion reduction in debt in 1995 and a \$943 million increase in distributions paid to Time Warner, offset in part by a \$368 million increase in collections on the note receivable from U S WEST that were used to partially finance the capital spending requirements of the Cable Division.

Management believes that TWE's operating cash flow, cash and equivalents, collections on the U S WEST Note and additional borrowing capacity are sufficient to fund its capital and liquidity needs for the foreseeable future.

### Cable Capital Spending

Since the beginning of 1994, Time Warner Cable has been engaged in a plan to upgrade the technological capability and reliability of its cable television systems and develop new services, which it believes will position the business for sustained, long-term growth. Capital spending by Time Warner Cable, including the cable operations of both Time Warner and TWE, amounted to \$1.349 billion in 1995, compared to \$778 million in 1994, and was financed in part through collections on the note receivable from U S WEST of \$602 million in 1995 and \$234 million in 1994. Cable capital spending for 1996 is budgeted to be approximately \$1.6 billion and is expected to be funded principally by cable operating cash flow and \$169 million of collections on the remaining portion of the note receivable from U S WEST. In exchange for certain flexibility in establishing cable rate pricing structures for regulated services that went into effect on January 1, 1996 and consistent with Time Warner Cable's long-term strategic plan, Time Warner Cable has agreed with the FCC to invest a total of \$4 billion in capital costs in connection with the upgrade of its cable infrastructure, which is expected to be substantially completed over the next five years. The agreement with the FCC covers all of the cable operations of Time Warner Cable, including the owned or managed cable television systems of Time Warner, TWE and the TWE-Advance/Newhouse Partnership. Management expects to continue to finance such level of investment principally through the growth in cable operating cash flow derived from increases in subscribers and cable rates, borrowings under the New Credit Agreement and the development of new revenue streams from expanded programming options, high speed data transmission, telephony and other services.

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# TIME WARNER

## 1995 ANNUAL REPORT

### Building Global Brands

## Off-Balance Sheet Assets

As discussed below, Time Warner believes that the value of certain off-balance sheet assets should be considered, along with other factors discussed elsewhere herein, in evaluating the Company's financial condition and prospects for future results of operations, including its ability to fund its capital and liquidity needs.

### Intangible Assets

As a creator and distributor of branded information and entertainment copyrights, Time Warner and the Entertainment Group have a significant amount of internally-generated intangible assets whose value is not fully reflected in their respective consolidated balance sheets. Such intangible assets extend across Time Warner's principal business interests, but are best exemplified by Time Warner's collection of copyrighted music product, its interests in Warner Bros.' and HBO's copyrighted film and television product libraries, and the creation or extension of brands, as in the case of Time Inc.'s new magazine titles or The WB Network. Generally accepted accounting principles do not recognize the value of such assets, except at the time they may be acquired in a business combination accounted for by the purchase method of accounting.

Because Time Warner owns the copyrights to such creative material, it continually generates revenue through the sale of such products across different media and in new and existing markets. The value of film and television-related copyrighted product and trademarks is continually realized by the licensing of films and television series to secondary markets and the licensing of trademarks, such as the Looney Tunes characters and Batman, to the retail industry and other markets. In addition, technological advances, such as the introduction of the compact disc and home videocassette in the 1980's and potentially the digital versatile disc in the future, have historically generated significant revenue opportunities through the repackaging and sale of such copyrighted products under the new technological format. Accordingly, such intangible assets have significant off-balance sheet asset value that is not fully reflected in the consolidated balance sheets of Time Warner or the Entertainment Group.

### Warner Bros. Backlog

Warner Bros.' backlog, representing the amount of future revenue not yet recorded from cash contracts for the licensing of theatrical and television product for pay cable, network, basic cable and syndicated television exhibition, amounted to \$1.056 billion at December 31, 1995, compared to \$852 million at December 31, 1994 (including amounts relating to HBO of \$175 million at each date). Because such contracts are for the licensing of theatrical and television product which have already been produced, the recognition of revenue is principally only dependent upon the commencement of the availability period for telecast under the terms of the related licensing agreement. In addition, cash licensing fees are collected periodically over the term of the related licensing agreements. Accordingly, the portion of backlog for which cash advances have not already been received has significant off-balance sheet asset value as a source of future funding. The backlog excludes advertising barter contracts, which are also expected to result in the future realization of cash through the sale of advertising spots received under such contracts.

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# TIME WARNER

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### Building Global Brands

## INTEREST RATE AND FOREIGN CURRENCY RISK MANAGEMENT

### Interest Rate Swap Contracts

Time Warner uses interest rate swap contracts to adjust the proportion of total debt that is subject to variable and fixed interest rates. At December 31, 1995, Time Warner had interest rate swap contracts to pay floating-rates of interest (average six-month LIBOR rate of 5.9%) and receive fixed-rates of interest (average rate of 5.4%) on \$2.6 billion notional amount of indebtedness, which resulted in approximately 43% of Time Warner's underlying debt, and 41% of the debt of Time Warner and the Entertainment Group combined, being subject to variable interest rates. The notional amount of outstanding

contracts at December 31, 1995 by year of maturity, along with the related average fixed-rates of interest to be received and the average floating-rates of interest to be paid, are as follows: 1996-\$300 million (receive-4.6%, pay-5.9%), 1998-\$700 million (receive-5.5%, pay-5.8%), 1999-\$1.2 billion (receive-5.5%, pay-5.9%), and 2000-\$400 million (receive-5.5%, pay-5.9%). At December 31, 1994, Time Warner had interest rate swap contracts on \$2.9 billion notional amount of indebtedness.

Based on the level of interest rates prevailing at December 31, 1995, the fair value of Time Warner's fixed-rate debt exceeded its carrying value by \$407 million and it would have cost \$9 million to terminate the related interest rate swap contracts, which combined is the equivalent of an unrealized loss of \$416 million. Based on Time Warner's fixed-rate debt and related interest rate swap contracts outstanding at December 31, 1995, each 25 basis point increase or decrease in the level of interest rates prevailing at December 31, 1995 would result in a net reduction or increase in the combined unrealized loss of approximately \$185 million, respectively, including respective costs or savings of \$16 million to terminate the related interest rate swap contracts. Based on the level of interest rates prevailing at December 31, 1994, the fair value of Time Warner's fixed-rate debt was \$572 million less than its carrying value and it would have cost \$236 million to terminate its interest rate swap contracts, which combined was the equivalent of an unrealized gain of \$336 million. Unrealized gains or losses on debt or interest rate swap contracts are not recognized unless the debt is retired or the contracts are terminated prior to their maturity.

Although changes in the unrealized gains or losses on interest rate swap contracts and debt do not result in the realization or expenditure of cash unless the contracts are terminated or the debt is retired, each 25 basis point increase or decrease in the level of interest rates related to Time Warner's variable-rate debt and interest rate swap contracts would respectively increase or decrease Time Warner's annual interest expense and related cash payments by approximately \$12 million, including \$7 million related to interest rate swap contracts.

### Foreign Exchange Contracts

Time Warner uses foreign exchange contracts primarily to hedge the risk that unremitted or future royalties and license fees owed to Time Warner or TWE 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. As part of its overall strategy to manage the level of exposure to

the risk of foreign currency exchange rate fluctuations, Time Warner hedges a portion of its and TWE's combined foreign currency exposures anticipated over the ensuing twelve month period. At December 31, 1995, Time Warner has effectively hedged approximately half of the combined estimated foreign currency exposures that principally relate to anticipated cash flows to be remitted to the U.S. over the ensuing twelve month period, using foreign exchange contracts that generally have maturities of three months or less, which are generally rolled over to provide continuing coverage throughout the year. Time Warner often closes foreign exchange sale contracts by purchasing an offsetting purchase contract. At December 31, 1995, Time Warner had contracts for the sale of \$504 million and the purchase of \$140 million of foreign currencies at fixed rates, primarily English pounds (29% of net contract value), German marks (19%), Canadian dollars (16%), French francs (16%) and Japanese yen (5%), compared to contracts for the sale of \$551 million and the purchase of \$109 million of foreign currencies at December 31, 1994.

Unrealized gains or losses related to foreign exchange contracts are recorded in income as the market value of such contracts change, accordingly, the carrying value of foreign exchange contracts approximates market value. The carrying value of foreign exchange contracts was not material at December 31, 1995 and 1994. No cash is required to be received or paid with respect to the realization of such gains and losses until the related foreign exchange contracts are settled, generally at their

respective maturity dates. In 1995 and 1994, Time Warner had \$20 million and \$33 million, respectively, and TWE had \$11 million and \$20 million, respectively, of net losses on foreign exchange contracts, which were or are expected to be offset by corresponding increases in the dollar value of foreign currency royalties and license fee payments that have been or are anticipated to be received in cash from the sale of U.S. copyrighted products abroad. Time Warner reimburses or is reimbursed by TWE for contract gains and losses related to TWE's foreign currency exposure. Foreign currency contracts are placed with a number of major financial institutions in order to minimize credit risk.

Based on the foreign exchange contracts outstanding at December 31, 1995, each 5% devaluation of the U.S. dollar as compared to the level of foreign exchange rates for currencies under contract at December 31, 1995 would result in approximately \$25 million of unrealized losses and \$7 million of unrealized gains on foreign exchange contracts involving foreign currency sales and purchases, respectively. Conversely, a 5% appreciation of the U.S. dollar would result in \$25 million of unrealized gains and \$7 million of unrealized losses, respectively. At December 31, 1995, none of Time Warner's foreign exchange purchase contracts relates to TWE's foreign currency exposure. However, with regard to the \$25 million of unrealized losses or gains on foreign exchange sale contracts, Time Warner would be reimbursed by TWE, or would reimburse TWE, respectively, for approximately \$6 million related to TWE's foreign currency exposure. Consistent with the nature of the economic hedge provided by such foreign exchange contracts, such unrealized gains or losses would be offset by corresponding decreases or increases, respectively, in the dollar value of future foreign currency royalty and license fee payments that would be received in cash within the ensuing twelve month period from the sale of U.S. copyrighted products abroad.

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# TIME WARNER

## 1995 ANNUAL REPORT

### Building Global Brands

#### Consolidated Balance Sheet

December 31, (millions, except per share amounts)	1995	1994
<b>ASSETS</b>		
<b>Current assets</b>		
Cash and equivalents	\$ 628	\$ 282
Receivables, less allowances of \$786 and \$768	1,755	1,439
Inventories	443	370
Prepaid expenses	894	726
<b>Total current assets</b>	<b>3,720</b>	<b>2,817</b>
Cash and equivalents segregated for redemption of long-term debt	557	-
Investments in and amounts due to and from Entertainment Group	5,734	5,350
Other Investments	2,389	1,555
Land and buildings	431	412
Cable television equipment	361	-
Furniture, fixtures and other equipment	1,196	998
<b>Less accumulated depreciation</b>	<b>1,988</b>	<b>1,410</b>
	(869)	(657)
Property, plant and equipment	1,119	753
Music catalogues, contracts and copyrights	1,140	1,207
Cable television franchises	1,696	-
Goodwill	5,213	4,630
Other assets	564	404
<b>Total assets</b>	<b>\$22,132</b>	<b>\$16,716</b>

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# TIME WARNER

1995 ANNUAL REPORT

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### Consolidated Balance Sheet

December 31, (millions, except per share amounts)	1995	1994
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable	\$ 672	\$ 648
Royalties payable	755	731
Debt due within one year	34	355
Other current liabilities	1,566	1,238
<b>Total current liabilities</b>	<b>3,027</b>	<b>2,972</b>
Long-term debt	9,907	8,839
Deferred income taxes	3,420	2,700
Unearned portion of paid subscriptions	654	631
Company-obligated mandatorily redeemable preferred securities of subsidiaries holding solely subordinated notes and debentures of the Company *	949	-
<b>Shareholder's equity</b>		
Furniture, fixtures and other equipment	1,196	998
Preferred stock, \$1 par value, 250 million shares authorized, 29.7 million and 962 thousand shares outstanding, \$2.994 billion and \$140 million liquidation preference	30	1
Common stock, \$1 par value, 750 million shares authorized, 387.7 million and 379.3 million shares outstanding	388	379
Paid-in capital	388	379
Unrealized gains on certain marketable securities	116	130
Accumulated deficit	(2,289)	(1,950)
<b>Total shareholders' equity</b>	<b>3,667</b>	<b>1,148</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$22,132</b>	<b>\$16,716</b>

\* Includes \$374 million of preferred securities that are redeemable for cash or, at Time Warner's option, approximately

12.1 million shares of Hasbro, Inc. common stock owned by Time Warner (Note 8).

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# TIME WARNER

## 1995 ANNUAL REPORT

### Building Global Brands

#### Consolidated Statement of Operations

Years ended December 31, (millions, except per share amounts)	1995	1994	1993
<b>Revenues*</b>	\$8,067	\$7,396	\$6,581
Cost of revenues **, **	4,682	4,307	3,780
Selling, general and administrative **, **	2,688	2,376	2,210
<b>Operating expenses</b>	7,370	6,683	5,990
Business segment operating income	697	713	591
Equity in pretax income of Entertainment Group*	256	176	281
Interest and other, net*	(877)	(724)	(718)
Corporate expenses*	(74)	(76)	(73)
Income before income taxes	2	89	81
Income taxes	(126)	(180)	(245)
Loss before extraordinary item	(124)	(91)	(164)
Extraordinary loss on retirement of debt, net of \$26 million and \$37 million income tax benefit in 1995 and 1993, respectively	(42)	-	(57)
<b>Net loss</b>	(166)	(91)	(221)
Preferred dividend requirements	(52)	(13)	(118)
<b>Net loss applicable to common shares</b>	\$(218)	\$(104)	\$(339)
<b>Loss per common share</b>			
Loss before extraordinary item	\$(.46)	\$(.27)	\$(.75)
Net loss	\$(.57)	\$(.27)	\$(.90)
<b>Average common shares</b>	383.8	378.9	374.7

\* Includes the following income (expenses) resulting from transactions with the Entertainment Group and other related companies for the years ended December 31, 1995, 1994, and 1993, respectively: revenues-\$211 million, \$203 million and \$170 million; cost of revenues-\$108 million, \$(109) million and \$(87) million; selling, general and administrative-\$46 million, \$47 million and \$59 million; equity in pretax income of Entertainment Group-\$95 million, \$(120) million and \$(115) million; interest and other, net-\$27 million, \$13 million and \$(4) million; and corporate expenses-\$64 million, \$60 million and \$60 million.

\*\* Includes depreciation and amortization expense of: \$ 559 \$ 437 \$ 424

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# TIME WARNER

1995 ANNUAL REPORT

## Building Global Brands

### Consolidated Statement of Cash Flows

<i>Years Ended December 31, (millions)</i>	1995	1994	1993
<b>Operations</b>			
Net loss	\$ (166)	\$ (91)	\$ (221)
Adjustments for noncash and nonoperating items			
Extraordinary loss on retirement of debt	42	-	57
One-time tax charge*	-	-	70
Depreciation and amortization	559	437	424
Noncash interest expense	176	219	185
Excess (deficiency) of distributions over equity in pretax income of Entertainment Group	807	(56)	(261)
Equity in income of other investee companies, net of distributions	(16)	(17)	-
Changes in operating assets and liabilities:			
Receivables	(68)	(47)	(71)
Inventories	(52)	(38)	20
Accounts payable and other liabilities	160	324	200
Other balance sheet changes	(391)	(258)	(152)
<b>Cash provided by operations</b>	<b>1,051</b>	<b>473</b>	<b>257</b>
<b>Investing Activities</b>			
Investments and acquisitions	(381)	(187)	(175)
Capital expenditures	(266)	(164)	(198)
Investment proceeds	376	118	103
<b>Cash used by investing activities</b>	<b>(271)</b>	<b>(233)</b>	<b>(270)</b>
<b>Financing Activities</b>			
Borrowings	2,023	582	4,714
Debt repayments	(2,693)	(626)	(1,599)
Issuance of Company-obligated mandatorily redeemable preferred securities of subsidiaries	949	-	-
Redemption of old Series D preferred stock	-	-	(3,499)
Dividends paid	(171)	(142)	(299)
Stock option and dividend reinvestment plans	106	34	92

Other, principally financing costs	(91)	(6)	(143)
Cash provided (used) by financing activities	123	(158)	(729)
<b>Increase (Decrease) in Cash and Equivalents</b>	<b>903</b>	<b>82</b>	<b>(742)</b>
<b>Cash and Equivalents at Beginning of Period</b>	<b>282</b>	<b>200</b>	<b>942</b>
<b>Cash and Equivalents at End of Period**</b>	<b>\$1,185</b>	<b>\$ 282</b>	<b>\$200</b>

\* Reflects a \$70 million increase in Time Warner's deferred income tax liability as a result of new tax law enacted in 1993

\*\* Includes current and noncurrent cash and equivalents at December 31, 1995

See accompanying notes.

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# TIME WARNER

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## Consolidated Statement of Shareholders' Equity

<i>(millions, except per share amounts)</i>	<i>Preferred Stock</i>	<i>Common Stock</i>	<i>Paid-In Capital</i>	<i>Unrealized Gains</i>	<i>Accumulated Deficit</i>	<i>Total</i>
<b>BALANCE AT DECEMBER 31, 1992</b>	\$ 129	\$ 372	\$8,606	\$ -	\$ (940)	\$8,167
Net Loss					(221)	(221)
Dividends on common stock-\$\$.31 per share					(116)	(116)
Dividends on Series B preferred stock-\$9.28 per share		4	4		(13)	(9)
Dividends on old Series C and D preferred stock to dates of redemption or exchange					(106)	(106)
Exchange of old Series C preferred stock and redemption of old Series D preferred stock	(128)		(6,240)		(311)	(6,679)
Unrealized gains on certain marketable equity investments at adoption of FAS 115				205		205
Shares issued pursuant to stock option and dividend		4	116			120

reinvestment plans						
Other		2	51		(44)	9
<b>BALANCE AT DECEMBER 31, 1993</b>	1	378	2,537	205	(1,751)	1,370
Net Loss					(91)	(91)
Dividends on common stock-\$ .35 per share (\$.09 per share per quarter effective for the second quarter of 1994)					(133)	(133)
Dividends on Series B preferred stock-\$9.28 per share			4		(13)	(9)
Unrealized losses on certain marketable equity investments				(75)		(75)
Shares issued pursuant to stock option and dividend reinvestment plans		1	53			54
Other			(6)		38	32
<b>BALANCE AT DECEMBER 31, 1994</b>	1	379	2,588	130	(1,950)	1,148
Net Loss					(166)	(166)
Dividends on common stock-\$ .36 per share					(138)	(138)
Dividends on Series B preferred stock-\$6.40 per share			3		(8)	(5)
Dividends on						

new Series C, D, G, H and I preferred stock-\$3.75 per share per year effective from the respective dates of issuance					(44)	(44)
Issuance of common and preferred stock in the KBLCOM and Summit acquisitions	14	3	1,367			1,384
Issuance of preferred stock in the ITOCHU/Toshiba transaction	15		1,335			1,350
Unrealized losses on certain marketable equity investments				(14)		(14)
Shares issued pursuant to stock option and dividend reinvestment plans		4	122			126
Other		2	7		17	26
<b>BALANCE AT DECEMBER 31, 1995</b>	<b>\$ 30</b>	<b>\$ 388</b>	<b>\$5,422</b>	<b>\$ 116</b>	<b>\$(2,289)</b>	<b>\$3,667</b>

See accompanying notes.

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# TIME WARNER

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## Building Global Brands

### Notes to Consolidated Financial Statements

#### 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

##### Description of Business

Time Warner Inc. ("Time Warner" or the "Company") is the world's leading media company, whose principal business objective is to create and distribute branded information and entertainment copyrights throughout the world. Time Warner has interests in three fundamental areas of business: Entertainment, consisting principally of interests in recorded music and music publishing, filmed entertainment, broadcasting, theme parks and cable television programming, News and Information, consisting principally of interests in magazine publishing, book publishing and direct marketing, and Telecommunications, consisting principally of interests in cable television systems. Substantially all of Time Warner's interests in filmed entertainment, broadcasting, theme parks, cable television programming and most of its cable television systems are held through Time Warner Entertainment Company, L.P. ("TWE"), a partnership in which Time Warner owns a 74.49% residual equity interest and certain priority capital interests senior thereto. Time Warner does not consolidate TWE and certain related companies (the "Entertainment Group") for financial reporting purposes because of certain limited partnership approval rights related to TWE's interest in certain cable television systems.

Each of the business interests within Entertainment, News and Information and Telecommunications is important to management's objective of increasing shareholder value through the creation, extension and distribution of recognizable brands and copyrights throughout the world. Such brands and copyrights include (1) copyrighted music from many of the world's leading recording artists that is produced and distributed by a family of established record labels such as Warner Bros. Records, the Atlantic and Elektra Entertainment Groups and Warner Music International, (2) the unique and extensive film and tele-vision libraries of Warner Bros. and trademarks such as the Looney Tunes characters and Batman, (3) The WB Network, a new national broadcasting network launched in 1995 as an extension of the Warner Bros. brand and as an additional distribution outlet for Warner Bros.' collection of children cartoons and television programming, (4) Six Flags, the largest regional theme park operator in the United States, in which TWE owns a 49% interest, (5) HBO and Cinemax, the leading pay television services, (6) magazine franchises such as Time, People and Sports Illustrated and direct marketing brands such as Time Life Inc. and Book-of-the-Month Club and (7) Time Warner Cable, the second largest operator of cable television systems in the U.S.

The operating results of Time Warner's various business interests are presented herein as an indication of financial performance (Note 13). Except for start-up losses incurred in an effort to create value in a branded national broadcasting network, Time Warner's principal business interests generate significant operating income and cash flow from operations. The cash flow from operations generated by such business interests is significantly greater than their operating income due to significant amounts of noncash amortization of intangible assets recognized in various acquisitions accounted for by the purchase method of accounting. Noncash amortization of intangible assets recorded by Time Warner's business interests, including the unconsolidated business interests of the Entertainment Group, amounted to \$822 million in 1995, \$782 million in 1994 and \$768 million in 1993.

## **Basis of Consolidation and Accounting or Investments**

The consolidated financial statements include 100% of the assets, liabilities, revenues, expenses, income, loss and cash flows of Time Warner and all companies in which Time Warner has a controlling voting interest ("subsidiaries"), as if Time Warner and its subsidiaries were a single company. Significant intercompany accounts and transactions between the consolidated companies have been eliminated.

The Entertainment Group and investments in certain other companies in which Time Warner has significant influence but less than a controlling voting interest, are accounted for using the equity method. Under the equity method, only Time Warner's investment in and amounts due to and from the equity investee are included in the consolidated balance sheet, only Time Warner's share of the investee's earnings is included in the consolidated operating results, and only the dividends, cash distributions, loans or other cash received from the investee, less any additional cash investment, loan repayments or other cash paid to the investee are included in the consolidated cash flows.

In accordance with Financial Accounting Standards Board ("FASB") Statement No. 115, "Accounting for Certain Investments in Debt and Equity Securities," ("FAS 115") investments in companies in which Time Warner does not have the controlling interest or an ownership and voting interest so large as to exert significant influence are accounted for at market value if the investments are publicly traded and there are no resale restrictions, or at cost, if the sale of a publicly-traded investment is restricted or if the investment is not publicly traded. Unrealized gains and losses on investments accounted for at market value are reported net-of-tax in a separate component of shareholders' equity until the investment is sold, at which time the realized gain or loss is included in income. Dividends and other distributions of earnings from both market value and cost method investments are included in income when declared.

The effect of any changes in Time Warner's ownership interests resulting from the issuance of equity capital by consolidated subsidiaries or equity investees to unaffiliated parties is included in income.

### **Foreign Currency**

The financial position and operating results of substantially all foreign operations are consolidated 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, which have not been material, are included in accumulated deficit. Foreign currency transaction gains and losses, which have not been material, are included in operating results.

### **Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and footnotes thereto. Actual results could differ from those estimates.

Significant estimates inherent in the preparation of the accompanying consolidated financial statements include management's forecast of anticipated revenues from the sale of future and existing music and publishing-related products in order to evaluate the ultimate recoverability of accounts receivables and artist and author advances recorded as assets in the consolidated balance sheet. Accounts receivables and sales in the music and publishing industries are subject to customers' rights to return unsold items. Management periodically reviews such estimates and it is reasonably possible that management's assessment of recoverability of accounts receivables and

individual artist and author advances may change based on actual results and other factors

### **Revenues and Costs**

The unearned portion of paid subscriptions is deferred until magazines are delivered to subscribers. Upon each delivery, a proportionate share of the gross subscription price is included in revenues.

Inventories of magazines, books, cassettes and compact discs are stated at the lower of cost or estimated realizable value. Cost is determined using first-in, first-out; last-in, first-out, and average cost methods. In accordance with industry practice, certain products (such as magazines, books, compact discs and cassettes) are sold to customers with the right to return unsold items. Revenues from such sales represent gross sales less a provision for future returns. Returned goods included in inventory are valued at estimated realizable value but not in excess of cost.

A significant portion of cable system revenues are derived from subscriber fees, which are recorded as revenue in the period the service is provided.

### **Advertising**

Advertising costs are expensed upon the first exhibition of the advertisement, except for certain direct-response advertising, for which the costs are capitalized and amortized over the expected period of future benefits. Direct-response advertising principally consists of product promotional mailings, broadcast advertising, catalogs and other promotional costs incurred in the Company's direct-marketing businesses. Deferred advertising costs are generally amortized over periods of up to three years subsequent to the promotional event using straight-line or accelerated methods, with a significant portion of such costs amortized in twelve months or less. Deferred advertising costs for Time Warner amounted to \$195 million and \$175 million at December 31, 1995 and 1994, respectively. Advertising expense for Time Warner amounted to \$1.045 billion in 1995, \$931 million in 1994 and \$831 million in 1993.

### **Cash and Equivalents**

Cash equivalents consist of commercial paper and other investments that are readily convertible into cash, and have original maturities of three months or less. Noncurrent cash and equivalents at December 31, 1995 consist of net proceeds received from the issuance of Preferred Trust Securities in December 1995, which were segregated for the redemption of the 8.75% Convertible Debentures in February 1996 (Notes 6 and 8).

### **Property, Plant and Equipment**

Property, plant and equipment are stated at cost. Additions to cable property, plant and equipment generally include material, labor, overhead and interest. Depreciation is provided generally on the straight-line method over useful lives ranging up to twenty-five years for buildings and improvements and up to fifteen years for furniture, fixtures, cable television equipment and other equipment.

In March 1995, the FASB issued Statement of Financial Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," ("FAS 121") effective for fiscal years beginning after December 15, 1995. The new rules establish standards for the recognition and measurement of impairment losses on long-lived assets and certain intangible assets. Time Warner expects that the adoption of FAS 121 will not have a material effect on its financial statements.

### **Intangible Assets**

As a creator and distributor of branded information and entertainment copyrights, Time Warner has a significant and growing amount of intangible assets, including goodwill, cable television franchises and music catalogues, contracts and copyrights. In accordance with generally accepted accounting principles, Time Warner does not recognize the fair value of internally-generated intangible assets. Costs incurred to create and produce copyrighted product, such as compact discs and cassettes, are generally either expensed as incurred, or capitalized as tangible assets as in the case of cash advances and inventoriable product costs. However, accounting recognition is not given to any increasing asset value that may be associated with the collection of the underlying copyrighted material. Additionally, costs incurred to create or extend brands, such as magazine titles, generally result in losses over an extended development period and are recognized as a reduction of income as incurred, while any corresponding brand value created is not recognized as an intangible asset in the consolidated balance sheet. On the other hand, intangible assets acquired in business combinations accounted for by the purchase method of accounting are capitalized and amortized over their expected useful life as a noncash charge against future results of operations. Accordingly, the intangible assets reported in the consolidated balance sheet do not reflect the fair value of Time Warner's internally-generated intangible assets, but rather are limited to intangible assets resulting from certain acquired entertainment copyrights. Time Warner has a significant and growing amount of intangible assets, including goodwill, cable televi

Time Warner amortizes goodwill over periods up to forty years using the straight-line method. Cable tele-vision franchises, music catalogues, contracts and copyrights, and other intangible assets are amortized over periods up to twenty years using the straight-line method. In 1995, 1994 and 1993, amortization of goodwill amounted to \$175 million, \$158 million and \$148 million, respectively; amortization of music copyrights, artists' contracts and record catalogues amounted to \$118 million, \$115 million and \$113 million, respectively; amortization of other intangible assets amounted to \$43 million, \$31 million and \$31 million, respectively; and amortization of cable television franchises amounted to \$42 million in 1995. Accumulated amortization of intangible assets at December 31, 1995 and 1994 amounted to \$1.845 billion and \$1.505 billion, respectively.

Time Warner separately reviews the carrying value of acquired intangible assets for each acquired entity on a quarterly basis to determine whether an impairment may exist. Time Warner considers relevant cash flow and profitability information, including estimated future operating results, trends and other available information, in assessing whether the carrying value of intangible assets can be recovered. Upon a determination that the carrying value of intangible assets will not be recovered from the undiscounted future cash flows of the acquired business, the carrying value of such intangible assets would be considered impaired and will be reduced by a charge to operations in the amount of the impairment. Impairment is measured as any deficiency in estimated undiscounted future cash flows of the acquired business to recover the carrying value related to the intangible assets.

### Income Taxes

Income taxes are provided using the liability method prescribed by FASB Statement No. 109, "Accounting for Income Taxes." Under the liability method, deferred income taxes reflect tax carryforwards and the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial statement and income tax purposes, as determined under enacted tax laws and rates. The financial effect of changes in tax laws or rates is accounted for in the period of enactment.

Realization of the net operating loss and investment tax credit carryforwards, which were acquired in acquisitions, are accounted for as a reduction of goodwill.

The principal operations of the Entertainment Group are conducted by partnerships. Income tax

expense includes all income taxes related to Time Warner's allocable share of partnership income and its equity in the income tax expense of corporate subsidiaries of the partnerships.

### Stock Options

In accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," compensation cost for stock options is recognized in income based on the excess, if any, of the quoted market price of the stock at the grant date of the award or other measurement date over the amount an employee must pay to acquire the stock. The exercise price for stock options granted to employees equals or exceeds the fair market value of Time Warner common stock at the date of grant, thereby resulting in no recognition of compensation expense by Time Warner.

### Loss Per Common Share

Loss per common share is based upon the net loss applicable to common shares after preferred dividend requirements and upon the weighted average of common shares outstanding during the period. The conversion of securities convertible into common stock and the exercise of stock options were not assumed in the calculations of loss per common share because the effect would have been antidilutive.

### Reclassifications

Certain reclassifications have been made to the prior years' financial statements to conform to the 1995 presentation.

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## 2. ENTERTAINMENT GROUP

Time Warner's investment in and amounts due to and from the Entertainment Group at December 31, 1995 and 1994 consist of the following:

<i>December 31, (millions)</i>	<i>1995</i>	<i>1994</i>
	\$	\$
Investment in TWE	6,179	5,284
Income tax and stock option related distributions due from TWE	122	423
Credit agreement debt due to TWE	(400)	(400)
Other liabilities due to TWE, principally related to home video distribution	(354)	(266)
Other receivables due from TWE	76-	
<b>Investments in and amounts due to and from TWE</b>	<b>5,623</b>	<b>5,041</b>
Investment in other Entertainment Group companies	111	309
<b>Total</b>	<b>\$5,734</b>	<b>\$5,350</b>

TWE is a Delaware limited partnership that was capitalized on June 30, 1992 to own and operate substantially all of the Filmed Entertainment, Programming-HBO and Cable businesses previously owned by subsidiaries of Time Warner. Certain Time Warner subsidiaries are the general partners of TWE ("Time Warner General Partners"). Time Warner acquired the aggregate 11.22% limited partnership interests previously held by subsidiaries of each of ITOCHU Corporation ("ITOCHU") and Toshiba Corporation ("Toshiba") in 1995 for an aggregate cost of \$1.36 billion, consisting of 15 million shares of convertible preferred stock (Series G Preferred Stock, Series H Preferred Stock and Series I Preferred Stock) and \$10 million in cash (the "ITOCHU/Toshiba Transaction"). The ITOCHU/Toshiba Transaction was accounted for by the purchase method of accounting for business combinations.

After the ITOCHU/Toshiba Transaction, Time Warner and certain of its wholly-owned subsidiaries collectively own 74.49% of the pro rata priority capital and residual equity interests in TWE, and certain additional senior and junior priority capital interests. The remaining 25.51% pro rata priority capital and residual equity limited partnership interests are held by a subsidiary of U S WEST, Inc. ("U S WEST"), which acquired such interests in 1993 for \$1.532 billion of cash and a \$1.021 billion 4.4% note (the "U S WEST Note").

Each partner's interest in TWE consists of the initial priority capital and residual equity amounts that



were assigned to that partner or its predecessor based on the estimated fair value of the net assets each contributed to the partnership, as adjusted for the fair value of certain assets distributed by TWE to the Time Warner General Partners in 1993 which were not subsequently reacquired by TWE in 1995 ("Contributed Capital"), plus, with respect to the priority capital interests only, any undistributed priority capital return. The priority capital return consists of net partnership income allocated to date in accordance with the provisions of the TWE partnership agreement and the right to be allocated additional partnership income which, together with any previously allocated net partnership income, provides for the various priority capital rates of return specified in the table below. The sum of Contributed Capital and the undistributed priority capital return is referred to as "Cumulative Priority Capital." Cumulative Priority Capital is not necessarily indicative of the fair value of the underlying priority capital interests principally due to above-market rates of return on certain priority capital interests as compared to securities of comparable credit risk and maturity, such as the 13.25% rate of return on the junior priority capital interest owned by subsidiaries of Time Warner. Furthermore, the ultimate realization of Cumulative Priority Capital could be affected by the fair value of TWE, which is subject to fluctuation.

A summary of the priority of Contributed Capital, Time Warner's ownership of Contributed Capital and Cumulative Priority Capital at December 31, 1995 and priority capital rates of return thereon is set forth below:

<i>Priority of Contributed Capital (billions)</i>	<i>Contributed Capital*</i>	<i>Cumulative Priority Capital</i>	<i>Priority Capital Rates of Return** (% per annum compounded quarterly)</i>	<i>% Owned by Time Warner</i>
Senior priority capital	\$1.4	\$1.4***	8.00%	100.00%
Pro rata priority capital	5.6	8.7	13.00%****	74.49%
Junior priority capital	2.9	4.6	13.25%*****	100.00%
Residual equity capital	3.3	3.3*****	.....	74.49%

\* Excludes partnership income or loss allocated thereto.

\*\* Income allocations related to priority capital rates of return are based on partnership income after any special tax allocations.

\*\*\* Net of \$366 million of partnership income distributed in 1995 representing the priority capital return thereon through June 30, 1995.

\*\*\*\* 11.00% to the extent concurrently distributed.

\*\*\*\*\* 11.25% to the extent concurrently distributed.

\*\*\*\*\* Residual equity capital is not entitled to stated priority rates of return and, as such, its Cumulative Priority Capital is equal to its Contributed Capital. However, in the case of certain events such as the liquidation or dissolution of residual equity capital is entitled to any excess of the fair value of the net assets of TWE over the aggregate amount of Cumulative Priority Capital and special tax allocations. The residual equity Contributed Capital has priority over the priority returns on junior and pro rata priority capital.



Because Contributed Capital is based on the fair value of the net assets that each partner contributed to the partnership, the aggregate of such amounts is significantly higher than TWE's partners' capital as reflected in the consolidated financial statements, which is based on the historical cost of the contributed net assets. For purposes of allocating partnership income or loss to the partners, partnership income or loss is based on the fair value of the net assets contributed to the partnership and results in significantly less partnership income, or results in partnership losses, in contrast to the net income reported by TWE for financial statement purposes, which is also based on the historical cost of contributed net assets.

Under the TWE partnership agreement, partnership income, to the extent earned, is first allocated to the partners so that the economic burden of the income tax consequences of partnership operations is borne as though the partnership were taxed as a corporation ("special tax allocations"), then to the senior priority, pro rata priority and junior priority capital interests, in order of priority, at rates of return ranging from 8% to 13.25% per annum, and finally to the residual equity interests. Partnership losses generally are allocated first to eliminate prior allocations of partnership income to, and then to reduce the Contributed Capital of, the residual equity, junior priority capital and pro rata priority capital interests, in that order, then to reduce the Time Warner General Partners' senior priority capital, including partnership income allocated thereto, and finally to reduce any special tax allocations. To the extent partnership income is insufficient to satisfy all special allocations in a particular accounting period, the right to receive additional partnership income necessary to provide for the various priority capital rates of return is carried forward until satisfied out of future partnership income, including any partnership income that may result from any liquidation or dissolution of TWE.

The TWE partnership agreement provides, under certain circumstances, for the distribution of partnership income allocated to the senior priority capital owned by the Time Warner General Partners. Pursuant to such provision, \$366 million of partnership income was distributed to the Time Warner General Partners in 1995. The senior priority capital and, to the extent not previously distributed, partnership income allocated thereto is required to be distributed in three annual installments beginning on July 1, 1997. The junior priority capital owned by subsidiaries of Time Warner may be increased if certain operating performance targets are achieved over a five-year period ending on December 31, 1996 and a ten-year period ending on December 31, 2001. Although satisfaction of the ten-year operating performance target is indeterminable at this time, it is not expected that the five-year target will be attained.

TWE reported net income of \$73 million, \$161 million and \$198 million in 1995, 1994 and 1993, respectively, no portion of which was allocated to the limited partners. Time Warner did not recognize a gain when TWE was capitalized. TWE recorded the assets contributed by the Time Warner General Partners at Time Warner's historical cost. The excess of the Time Warner General Partners' interest in the net assets of TWE over the net book value of their investment in TWE is being amortized to income over a twenty year period.

U S WEST has an option to obtain up to an additional 6.33% of pro rata priority capital and residual equity interests, depending on cable operating performance. The option is exercisable between January 1, 1999 and on or about May 31, 2005 at a maximum exercise price of \$1.25 billion to \$1.8 billion, depending on the year of exercise. Either U S WEST or TWE may elect that the exercise price be paid with partnership interests rather than cash.

Each Time Warner General Partner has guaranteed a pro rata portion of approximately \$6 billion of TWE's debt and accrued interest at December 31, 1995, based on the relative fair value of the net assets each Time Warner General Partner contributed to TWE. Such indebtedness is recourse to each Time Warner General Partner only to the extent of its guarantee. In addition to their interests in TWE and the other Entertainment Group companies, the assets of the Time Warner General

Partners include the equivalent of 29.6 million common shares of Turner Broadcasting System, Inc., 12.1 million common shares of Hasbro, Inc., 43.7 million common shares of Time Warner, and substantially all the assets of Time Warner's music business. There are no restrictions on the ability of the Time Warner General Partner guarantors to transfer assets, other than TWE assets, to parties that are not guarantors.

Set forth below is summarized financial information of the Entertainment Group, which reflects the consolidation by TWE of the TWE-Advance/Newhouse Partnership effective as of April 1, 1995 (Note 4), the deconsolidation of Six Flags Entertainment Corporation ("Six Flags") effective as of June 23, 1995 and the consolidation of Paragon Communications ("Paragon") effective as of July 6, 1995.

## TIME WARNER ENTERTAINMENT GROUP

### Operating Statement Information

<i>Years Ended</i>				
<i>December 31,</i>		<i>1995</i>	<i>1994</i>	<i>1993</i>
<i>(millions)</i>				
Revenues	\$9,029	\$8,509	\$7,963	
Depreciation and amortization	1,060	959	909	
Business segment operating income	992	852	905	
Interest and other, net	539	616	564	
Minority interest	133	-	-	
Income before income taxes	256	176	281	
Income before extraordinary item	170	136	217	
Net income	146	136	207	

### Cash Flow Information

<i>Years Ended</i>				
<i>December 31,</i>		<i>1995</i>	<i>1994</i>	<i>1993</i>
<i>(millions)</i>				
Cash provided by operations	\$1,495	\$1,341	\$1,276	
Capital expenditures	(1,657)	(1,235)	(613)	
Investments and acquisitions	(217)	(186)	(368)	
Investment proceeds	1,120	51	184	
Loan to Time Warner	-	(400)	-	
Borrowings	2,484	1,001	3,075	
Debt repayments	(3,596)	(953)	(3,734)	

Collection on note receivable from US WEST	602	234	16
Capital contributions	-	-	1,532
Capital distributions (1063)	(120)	(20)	
Increase (decrease) in cash and equivalents	(862)	(267)	1,302

#### Balance Sheet Information

<i>December 31, (millions)</i>	<i>1995</i>	<i>1994</i>
Cash and equivalents	\$209	\$1,071
Total current assets	2,909	3,571
Total assets	18,960	18,992
Total current liabilities	3,230	2,953
Long-term debt	6,137	7,160
Minority interests	726	-
Time Warner General partners' senior priority capital, consisting of \$1.364 billion Contributed Capital plus an undistributed priority return Partner' capital, before deduction of the USWEST Note	1,426	1,663
USWEST Note	169	771

The assets and cash flows of TWE are restricted by the TWE partnership and credit agreements and are unavailable for use by the partners except through the payment of certain fees, reimbursements, cash distributions and loans, which are subject to limitations. At December 31, 1995 and 1994, the Time Warner General Partners had recorded \$122 million and \$89 million, respectively, of stock option related distributions due from TWE, based on closing prices of Time Warner common stock of \$37.875 and \$35.125, respectively. Time Warner is paid when the options are exercised. The Time Warner General Partners also receive tax-related distributions from TWE. The payment of such distributions was previously subject to restrictions until July 1995 and is now made to the Time Warner General Partners on a current basis. At December 31, 1994, the Time Warner General Partners had accrued \$334 million of tax-related distributions due from TWE. During 1995, the Time Warner General Partners received net distributions from TWE in the amount of \$1.063 billion, consisting of \$366 million of TWE partnership income allocated to the Time Warner General Partners' senior priority capital interest, \$680 million of tax-related distributions and \$17 million of stock option related distributions. During 1994 and 1993, the Time Warner General Partners received net distributions from TWE in the amount of \$120 million and \$20 million, respectively, consisting of \$115 million of tax-related distributions and \$5 million of stock option related distributions in 1994, and \$20 million of stock option related distributions in 1993. In addition to the tax, stock option and Time Warner General Partners' senior priority capital distributions, TWE may make other distributions, generally depending on excess cash and credit agreement limitations. The Time Warner General Partners' full share of such distributions may be

deferred if the limited partners do not receive certain threshold amounts by certain dates.

On June 23, 1995, TWE sold 51% of its interest in Six Flags to an investment group led by Boston Ventures for \$204 million and received \$640 million in additional proceeds from Six Flags, representing payment of certain intercompany indebtedness and licensing fees. As a result of the transaction, Six Flags has been deconsolidated and TWE's remaining 49% interest in Six Flags is accounted for under the equity method of accounting. TWE reduced debt by approximately \$850 million in connection with the transaction, and a portion of the income on the transaction has been deferred by TWE principally as a result of its guarantee of certain third-party, zero-coupon indebtedness of Six Flags due in 1999.

In the normal course of conducting their businesses, Time Warner and its subsidiaries and affiliates have had various transactions with TWE and other Entertainment Group companies, generally on terms resulting from negotiation between the affected units that in management's view results in reasonable allocations. In 1995, TWE and certain subsidiaries of Time Warner entered into management services agreements, pursuant to which TWE receives fees for the management of all cable television systems owned by Time Warner. Management fees paid to TWE in 1995 were not material. In addition, Time Warner provides TWE with certain corporate support services for which it received a fee in the amount of \$64 million, \$60 million and \$60 million in 1995, 1994 and 1993, respectively.

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### 3. TBS TRANSACTION

Time Warner has entered into an Amended and Restated Agreement and Plan of Merger dated as of September 22, 1995 (the "Merger Agreement"), which provides for the merger of each of Time Warner and Turner Broadcasting System, Inc. ("TBS") with separate subsidiaries of a holding company ("New Time Warner" and collectively, the "TBS Transaction"). In connection therewith, the issued and outstanding shares of each class of the capital stock of Time Warner will be converted into shares of a substantially identical class of capital stock of New Time Warner. In addition, Time Warner has agreed to enter into certain agreements and related transactions with certain shareholders of TBS, including R. E. Turner and Liberty Media Corporation ("LMC"). The Merger Agreement and certain related agreements provide for the issuance by New Time Warner of approximately 172.8 million shares of common stock, par value \$ 01 per share (including 50.8 million shares of a special class of non-redeemable common stock to be issued to LMC, the "LMC Class Common Stock"), in exchange for the outstanding TBS capital stock, the issuance of approximately 13 million stock options to replace all outstanding TBS options and the assumption of TBS' indebtedness (which approximated \$2.5 billion at December 31, 1995). As part of the TBS Transaction, LMC will receive an additional five million shares of LMC Class Common Stock pursuant to a separate option agreement which, together with the 50.8 million shares received pursuant to the TBS Transaction, will be placed in a voting trust or, in certain circumstances, exchanged for shares of another special class of non-voting, non-redeemable common stock of New Time Warner. The TBS Transaction will be accounted for by the purchase method of accounting for business combinations.

The TBS Transaction is subject to customary closing conditions, including the approval of the shareholders of TBS and of Time Warner, all necessary approvals of the Federal Communications Commission and appropriate antitrust approvals. There can be no assurance that all these approvals can be obtained or, in the case of governmental approvals, if obtained, will not be conditioned upon changes to the terms of the Merger Agreement or the related agreements.

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### 4. CABLE TRANSACTIONS

On April 1, 1995, TWE formed a cable television joint venture with the Advance/Newhouse Partnership ("Advance/Newhouse") to which Advance/Newhouse and TWE contributed cable television systems (or interests therein) serving approximately 4.5 million subscribers, as well as certain foreign cable investments and programming investments that included Advance/Newhouse's 10% interest in Primestar Partners, L.P. ("Primestar"). TWE owns a two-thirds equity interest in the TWE-Advance/Newhouse Partnership and is the managing partner. TWE consolidates the partnership and the one-third equity interest owned by Advance/Newhouse is reflected in TWE's consolidated financial statements as minority interest. In accordance with the partnership agreement, Advance/Newhouse can require TWE to purchase its equity interest for fair market value at specified intervals following the death of both of its principal shareholders. Beginning in the third year, either partner can initiate a dissolution in which TWE would receive two-thirds and Advance/Newhouse would receive one-third of the partnership's net assets. The assets contributed by TWE and Advance/Newhouse to the partnership were recorded at their predecessor's historical cost. No gain was recognized by TWE upon the capitalization of the partnership.

On May 2, 1995, Time Warner acquired Summit Communications Group, Inc. ("Summit"), which owned cable television systems serving approximately 162,000 subscribers, in exchange for the issuance of approximately 1.6 million shares of common stock and approximately 3.3 million shares of a new convertible preferred stock ("Series C Preferred Stock") and the assumption of \$140 million of indebtedness. The acquisition was accounted for by the purchase method of accounting for business combinations; accordingly, the cost to acquire Summit of approximately \$351 million was allocated to the net assets acquired in proportion to estimates of their respective fair values, as follows: cable television franchises-\$372 million; goodwill-\$146 million; other current and noncurrent assets-\$144 million; long-term debt-\$140 million; deferred income taxes-\$166 million; and other current liabilities-\$5 million.

On July 6, 1995, Time Warner acquired KBLCOM Incorporated ("KBLCOM"), which owned cable television systems serving approximately 700,000 subscribers and a 50% interest in Paragon, which owned cable television systems serving an additional 972,000 subscribers. The other 50% interest in Paragon was already owned by TWE. To acquire KBLCOM, Time Warner issued 1 million shares of common stock and 1.1 million shares of a new convertible preferred stock ("Series D Preferred Stock") and assumed or incurred approximately \$1.2 billion of indebtedness. The acquisition was accounted for by the purchase method of accounting for business combinations; accordingly, the cost to acquire KBLCOM of approximately \$1.033 billion was allocated to the net assets acquired in proportion to their respective fair values, as follows: investments-\$950 million; cable television franchises-\$1.366 billion; goodwill-\$586 million; other current and noncurrent assets-\$289 million; long-term debt-\$1.213 billion; deferred income taxes-\$895 million; and other current liabilities-\$50 million.

On January 4, 1996, Time Warner acquired Cablevision Industries Corporation ("CVI") and related companies that owned cable television systems serving approximately 1.3 million subscribers, in exchange for the issuance of approximately 2.9 million shares of common stock and approximately 6.5 million shares of new convertible preferred stock ("Series E Preferred Stock" and "Series F Preferred Stock") and the assumption or incurrence of approximately \$2 billion of indebtedness.



The acquisition is not reflected in the accompanying consolidated financial statements. The acquisition will be accounted for by the purchase method of accounting for business combinations, accordingly, the cost to acquire CVI and related companies of \$904 million is expected to be preliminarily allocated to the net assets acquired in proportion to estimates of their respective fair values, as follows: cable television franchises-\$2.390 billion, goodwill-\$688 million, other current and noncurrent assets-\$481 million, long-term debt-\$1.766 billion, deferred income taxes-\$731 million, and other current and noncurrent liabilities-\$158 million.

The accompanying consolidated statement of operations includes the operating results of each business from the respective closing date of each transaction. On a pro forma basis, giving effect to (i) all of the aforementioned cable transactions, (ii) the ITOCHU/Toshiba Transaction, (iii) Time Warner's and TWE's debt refinancings and (iv) the sale of 51% of TWE's interest in Six Flags and the sale or expected sale or transfer of certain unclustered cable television systems owned by TWE, as if each of such transactions had occurred at the beginning of the periods, Time Warner would have reported for the years ended December 31, 1995 and 1994, revenues of \$8.742 billion and \$8.217 billion, depreciation and amortization of \$935 million and \$906 million, operating income of \$656 million and \$653 million, equity in the pretax income of the Entertainment Group of \$286 million and \$205 million, a loss before extraordinary item of \$255 million and \$266 million (\$1.02 and \$1.07 per common share) and a net loss of \$297 million and \$266 million (\$1.13 and \$1.07 per common share), respectively.

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#### 5. OTHER INVESTMENTS

Time Warner's other investments consist of

<i>December 31, (millions)</i>	<i>1995</i>	<i>1995</i>
Equity method investments*	\$1,898	\$985
Market value method investments	375	435
Cost method investments	116	135
<b>Total</b>	<b>\$2,389</b>	<b>\$1,555</b>

\* Equity method investments include Time Warner's investment in TBS which was carried at \$541 million at December 31, 1995. Time Warner has agreed to acquire the remaining interest in TBS that it does not already own (Note 3).

Market value method investments include the fair value of 12.1 million shares of common stock of Hasbro, Inc. ("Hasbro"). Notwithstanding the market value per share, such shares can be used, at Time Warner's option, to fully satisfy either its obligations with respect to the zero coupon exchangeable notes due 2012 (Note 6) or the Company-obligated mandatorily redeemable preferred securities of a subsidiary due 1997 (Note 8). Because the issuance of the mandatorily redeemable preferred securities provides Time Warner with protection against the risk of depreciation of the market price of Hasbro common stock and the zero coupon exchangeable notes limit Time Warner's ability to share in the appreciation of the market price of Hasbro common stock, the combination thereof has effectively monetized Time Warner's investment in Hasbro.

In addition to TWE and its equity investees, companies accounted for using the equity method include TBS (currently 19.6% owned), CinAmerica Theatres, L.P. (50% owned) and The Columbia House Company partnerships (50% owned) and other music joint ventures (generally 50% owned). A summary of combined financial information as reported by the equity investees of Time Warner is set forth below:

<i>Years Ended December 31 (millions)</i>	<i>1995</i>	<i>1994</i>	<i>1993</i>
Revenues	\$5,123	\$4,444	\$3,363
Depreciation and amortization	219	182	140
Operating income	547	584	450
Income before extraordinary items and cumulative effect of a change in accounting principle	188	281	201
Net income (loss)	188	256	(135)

Current assets	2,272	2,113	1,586
Total assets	5,851	5,194	4,111
Current liabilities	1,318	1,136	755
Long-term debt	3,826	3,730	2,606
Total liabilities	5,886	5,423	3,992
Total shareholders' equity or partners' capital	(35)	(229)	119

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### 6. LONG-TERM DEBT

Long-term debt consists of

<i>December 31, (millions)</i>	<i>1995</i>	<i>1994</i>
7.45% Notes due February 1, 1998	\$500	\$500
7.95% Notes due February 1, 2000	500	500
Floating rate notes due August 15, 2000 (6.8% interest rate)	454	-
Redeemable reset notes due August 15, 2000 (8.7% yield)	-	1,719
7.975% Notes due August 15, 2004	272	-
7.75% Notes due June 15, 2005	497	-
8.11% Debentures due August 15, 2006	545	-
8.18% Debentures due August 15, 2007	545	-
Zero coupon exchangeable notes due December 17, 2012 (6.25% yield)	581	547
Zero coupon convertible notes due June 22, 2013 (5% yield)	1,019	970
9.125% Debentures due January 15, 2013	1,000	1,000
8.75% Convertible subordinated debentures due January 10, 2015	1,226	2,226
8.75% Debentures due April 1, 2017	248	248
9.15% Debentures due February 1, 2023	1,000	1,000
Credit agreement debt due to TWE (6.8% and 6.7% interest rates)	400	400

#### Time Warner Cable Subsidiaries

New Credit Agreement (6.8% interest rate)	1,265	-
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Summit 10.5% Debentures due April 15, 2005	140	-
Other	115	129
Subtotal	10,307	9,239
Reclassification of debt due to TWE to amounts due to the Entertainment Group	(400)	(400)
Total	\$9,907	\$8,839

### Debt Refinancings

During 1995 and early 1996, in response to favorable market conditions, Time Warner refinanced approximately \$4 billion of its public debt and, in conjunction with the cable acquisitions, entered into a new credit agreement under which it refinanced approximately \$2.7 billion of debt assumed in the acquisitions, as more fully described below.

In June 1995, a wholly-owned subsidiary of Time Warner ("TWI Cable"), TWE and the TWE-Advance/Newhouse Partnership executed a five-year revolving credit facility (the "New Credit Agreement"). The New Credit Agreement enabled such entities to refinance certain indebtedness assumed in the cable acquisitions, to refinance TWE's indebtedness under a pre-existing bank credit agreement and to finance the ongoing working capital, capital expenditure and other corporate needs of each borrower.

The New Credit Agreement permits borrowings in an aggregate amount of up to \$8.3 billion, with no scheduled reductions in credit availability prior to maturity. Borrowings are limited to \$4 billion in the case of TWI Cable, \$5 billion in the case of the TWE-Advance/Newhouse Partnership and \$8.3 billion in the case of TWE, subject in each case to certain limitations and adjustments. Such borrowings bear interest at specific rates for each of the three borrowers, generally equal to LIBOR plus a margin initially ranging from 50 to 87.5 basis points, which margin will vary based on the credit rating or financial leverage of the applicable borrower. Unused credit is available for general business purposes and to support any commercial paper borrowings. Each borrower is required to pay a commitment fee initially ranging from .2% to .35% per annum on the unused portion of its commitment. TWI Cable may also be required to pay an annual facility fee equal to .1875% of the entire amount of its commitment, depending on the level of its financial leverage in any given year. The New Credit Agreement contains certain covenants for each borrower relating to, among other things, additional indebtedness; liens on assets; cash flow coverage and leverage ratios; and loans, advances, distributions and other cash payments or transfers of assets from the borrowers to their respective partners or affiliates. Principally as a result of such restrictions, restricted net assets of consolidated subsidiaries of Time Warner amounted to approximately \$950 million at December 31, 1995.

In July 1995, TWI Cable borrowed approximately \$1.2 billion under the New Credit Agreement to refinance certain indebtedness assumed or incurred in the acquisition of KBLCOM. An additional \$1.5 billion was borrowed by TWI Cable under the New Credit Agreement in January 1996 to refinance certain indebtedness assumed or incurred in the acquisition of CVI and related companies.

In August 1995, Time Warner redeemed all of its \$1.8 billion principal amount of outstanding Redeemable Reset Notes due August 15, 2002 (the "Reset Notes") in exchange for new securities, consisting of approximately \$454 million aggregate principal amount of Floating Rate Notes due August 15, 2000, approximately \$272 million aggregate principal amount of 7.975% Notes due August 15, 2004, approximately \$545 million aggregate principal amount of 8.11% Debentures due

August 15, 2006, and approximately \$545 million aggregate principal amount of 8.18% Debentures due August 15, 2007

Through periodic redemptions, Time Warner has fully redeemed its \$3.1 billion principal amount of 8.75% Convertible Subordinated Debentures due 2015 (the "8.75% Convertible Debentures"), which were issued in April 1993 in exchange for the old Series C preferred stock that was issued in Time Warner's 1989 acquisition of Warner Communications Inc. ("WCI") (Note 9). Time Warner first redeemed \$900 million principal amount of 8.75% Convertible Debentures in July 1993. In September 1995, Time Warner redeemed approximately \$1 billion principal amount of such debentures for \$1.06 billion (including redemption premiums and accrued interest) and, in February 1996, Time Warner redeemed the remaining \$1.2 billion principal amount of 8.75% Convertible Debentures for \$1.28 billion (including redemption premiums and accrued interest). The September 1995 redemption was financed with proceeds from a \$500 million issuance of 7.75% ten-year notes in June 1995, proceeds from a \$374 million issuance of Company-obligated mandatorily redeemable preferred securities of a subsidiary in August 1995 and available cash and equivalents. The February 1996 redemption was financed with proceeds from a \$575 million issuance of Company-obligated mandatorily redeemable preferred securities of a subsidiary in December 1995 and proceeds from a \$750 million issuance in January 1996 of (i) \$400 million principal amount of 6.85% thirty-year debentures, which are putable by the holders thereof in year seven, (ii) \$200 million principal amount of 8.3% forty-year discount debentures, which do not pay cash interest for the first twenty years, (iii) \$166 million principal amount of 7.48% twelve-year debentures and (iv) \$150 million principal amount of 8.05% twenty-year debentures. See Note 8 for a description of the mandatorily redeemable preferred securities issued in connection with such redemptions.

An extraordinary loss of \$57 million was incurred in 1993, principally in connection with the redemption of \$900 million of 8.75% Convertible Debentures and \$529 million of WCI senior and subordinated debentures. An extraordinary loss of \$42 million was recognized in 1995 in connection with the September 1995 redemption of the 8.75% Convertible Debentures and the write-off by TWE of deferred financing costs related to its former bank credit agreement. In addition, Time Warner recognized an extraordinary loss of \$26 million in February 1996 in connection with the redemption of the remaining outstanding portion of the 8.75% Convertible Debentures.

### Zero Coupon Notes

Time Warner's zero coupon notes do not pay interest until maturity. The zero coupon exchangeable notes due December 17, 2012 are exchangeable at any time by the holders into an aggregate of 12.1 million shares of common stock of Hasbro, Inc. ("Hasbro") at the rate of 7.301 shares for each \$1,000 principal amount of notes, subject to Time Warner's right to pay in whole or in part with cash instead of Hasbro common stock. Time Warner can elect to redeem the notes any time after December 17, 1997, and holders can elect to have the notes redeemed prior thereto in the event of a change of control, at the issue price plus accrued interest. Holders also can elect to have the notes redeemed at the issue price plus accrued interest on December 17, 1997, 2002 and 2007, subject to Time Warner's right to pay in whole or in part with Hasbro common stock instead of cash. The equivalent conversion price of Hasbro common stock at the first date of redemption is \$54.41 per share, and will be adjusted thereafter in proportion to changes in the accrued original issue discount of each note. The 12.1 million shares of Hasbro common stock owned by Time Warner can be used by the Company, at its election, to satisfy its obligations under such notes or its obligations under certain mandatorily redeemable preferred securities of a subsidiary (Note 8). Unamortized original issue discount on the zero coupon exchangeable notes due 2012 was \$1.070 billion and \$1.104 billion at December 31, 1995 and 1994, respectively.

The zero coupon convertible notes due June 22, 2013 are convertible at any time by the holders into an aggregate of 18.7 million shares of Time Warner common stock at the rate of 7.759 shares for

each \$1,000 principal amount of notes. Time Warner can elect to redeem the notes any time after June 22, 1998, and holders can elect to have the notes redeemed prior thereto in the event of a change in control, at the issue price plus accrued interest. Holders also can elect to have the notes redeemed at the issue price plus accrued interest on June 22, 1998, 2003 and 2008, subject to Time Warner's right to pay in whole or in part with Time Warner common stock instead of cash. The equivalent conversion price of Time Warner common stock at the first date of redemption is \$61.44 per share, and will be adjusted thereafter in proportion to changes in the accrued original issue discount of each note. Unamortized original issue discount on the zero coupon convertible notes due 2013 was \$1.396 billion and \$1.445 billion at December 31, 1995 and 1994, respectively.

### TWE-Related Obligations

Time Warner and TWE entered into a credit agreement in 1994 that allows Time Warner to borrow up to \$400 million from TWE through September 15, 2000. Outstanding borrowings from TWE bear interest at LIBOR plus 1% per annum. Time Warner borrowed \$400 million in 1994 under the credit agreement, and used the proceeds therefrom principally to repay certain of its notes at their maturity. In addition, each Time Warner General Partner has guaranteed a pro rata portion of approximately \$6 billion of TWE's debt and accrued interest at December 31, 1995, as more fully described in Note 2.

### Interest Expense and Maturities

At December 31, 1995, Time Warner had interest rate swap contracts to pay floating-rates of interest and receive fixed-rates of interest on \$2.6 billion notional amount of indebtedness, which resulted in approximately 43% of Time Warner's underlying debt being subject to variable interest rates (Note 12).

Interest expense amounted to \$877 million in 1995, \$769 million in 1994 and \$698 million in 1993, including \$28 million in 1995 and \$12 million in 1994 which was paid to TWE in connection with borrowings under Time Warner's \$400 million credit agreement with TWE. The weighted average interest rate on Time Warner's total debt, including the effect of interest rate swap contracts, was 7.9% and 8.1% at December 31, 1995 and 1994, respectively.

Annual repayments of long-term debt for the five years subsequent to December 31, 1995 consist of \$500 million due in 1998 and \$2.219 billion due in 2000. Such repayments exclude the aggregate repurchase or redemption prices of \$656 million in 1997 and \$1.151 billion in 1998 relating to the zero coupon exchangeable notes and zero coupon convertible notes, respectively, in the years in which the holders of such debt may first exercise their redemption options.

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#### 7. INCOME TAXES

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

<i>Years Ended December 31, (millions)</i>	<i>1995</i>	<i>1994</i>	<i>1993</i>
Domestic	\$(203)	\$(78)	\$(57)
Foreign	205	167	138
<b>Total</b>	<b>\$2</b>	<b>\$ 89</b>	<b>\$ 81</b>

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

<i>Years Ended December 31, (millions)</i>	<i>1995</i>	<i>1994</i>	<i>1993</i>
<b>Federal:</b>			
Current*	\$ 42	\$ 66	\$ 45
Deferred**	(167)	(81)	11
<b>Foreign:</b>			
Current***	215	194	168
Deferred	8	(45)	(11)
<b>State and Local:</b>			
Current	78	79	86
Deferred	(50)	(33)	(54)
<b>Total</b>	<b>\$126</b>	<b>\$180</b>	<b>\$245</b>

\* Includes utilization of tax carryforwards of \$101 million in 1995, \$48 million in 1994 and \$136 million in 1993. Excludes current tax benefits of \$9 million in 1995, \$11 million in 1994 and \$14 million in 1993 resulting from the exercise of stock options and vesting of restricted stock awards, which were credited directly to paid-in-capital, and current tax benefits of \$3 million in 1995 and \$6 million in 1993 resulting from the retirement of debt, which reduced the extraordinary losses in such years.

\*\*Includes \$70 million unusual charge in 1993 to increase deferred tax liability for increase in tax rate.

\*\*\* Includes foreign withholding taxes of \$102 million in 1995, \$74 million in 1994 and \$79 million in 1993.

The differences between income taxes expected at the U.S. federal statutory income tax rate and income taxes provided are as set forth below. The relationship between income before income taxes and income tax expense is most affected by the amortization of goodwill and certain other financial statement expenses that are not deductible for income tax purposes and by a \$70 million charge in 1993 to adjust the deferred income tax liability for the increase in the U.S. federal statutory rate from 34% to 35% enacted into law that year.

<i>Years Ended December 31, (millions)</i>	<i>1995</i>	<i>1994</i>	<i>1993</i>
--	-------------	-------------	-------------



Taxes on income at U.S. federal statutory rate	\$1	\$31	\$28
State and local taxes, net	18	30	21
Nondeductible goodwill amortization	100	97	96
Other nondeductible expenses	10	10	11
Charge to increase deferred tax liability for increase in tax rate	-	-	70
Foreign income taxed at different rates, net of U.S. foreign tax credits	3	1	13
Other	(6)	11	6
<b>Total</b>	<b>\$</b>	<b>\$180</b>	<b>\$</b>
	126		245

Significant components of Time Warner's net deferred tax liabilities are as follows:

<i>Years Ended December 31, (millions)</i>	<i>1995</i>	<i>1994</i>
Assets acquired in business combinations	\$2,963	\$2,276
Depreciation and amortization	829	619
Unrealized appreciation of certain marketable securities	81	91
Other	390	460
<b>Deferred tax liabilities</b>	<b>4,263</b>	<b>3,446</b>
Tax carryforwards	296	264
Accrued liabilities	228	206
Receivable allowances and return reserves	211	200
Other	108	76
<b>Deferred tax assets</b>	<b>843</b>	<b>746</b>
<b>Net deferred tax liabilities</b>	<b>\$3,420</b>	<b>\$2,700</b>

U.S. income and foreign withholding taxes have not been recorded on permanently reinvested earnings of foreign subsidiaries aggregating approximately \$760 million at December 31, 1995. Determination of the amount of unrecognized deferred U.S. income tax liability with respect to such earnings is not practicable. If such earnings are repatriated, additional U.S. income and foreign withholding taxes are substantially expected to be offset by the accompanying foreign tax credits.

U.S. federal tax carryforwards at December 31, 1995 consisted of \$328 million of net operating losses, \$152 million of investment tax credits and \$30 million of alternative minimum tax credits. The utilization of certain carryforwards is subject to limitations under U.S. federal income tax laws. Except for the alternative minimum tax credits which do not expire, the other U.S. federal tax carryforwards expire in varying amounts as follows for income tax reporting purposes:

<i>(millions)</i>	<i>Net Operating Losses</i>	<i>Carryforwards</i>
		<i>Investment Tax Credits</i>
1997	\$ -	\$ 2
1998	-	7
1999	14	19
2000	-	99
Thereafter up to 2008	314	99
	\$ 328	\$ 152

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#### 8. MANDATORILY REDEEMABLE PREFERRED SECURITIES

In August 1995, Time Warner issued approximately 12.1 million Company-obligated mandatorily redeemable preferred securities of a wholly-owned subsidiary ("PERCS") for aggregate gross proceeds of \$374 million. The sole assets of the subsidiary that is the obligor on the PERCS are \$385 million principal amount of 4% subordinated notes of Time Warner due December 23, 1997. Cumulative cash distributions are payable on the PERCS at an annual rate of 4%. The PERCS are mandatorily redeemable on December 23, 1997, for an amount per PERCS equal to the lesser of \$54.41, and the market value of a share of common stock of Hasbro on December 17, 1997, payable in cash or, at Time Warner's option, Hasbro common stock. Time Warner has the right to redeem the PERCS at any time prior to December 23, 1997, at an amount per PERCS equal to \$54.41 (or in certain limited circumstances the lesser of such amount and the market value of a share of Hasbro common stock at the time of redemption) plus accrued and unpaid distributions thereon and a declining premium, payable in cash or, at Time Warner's option, Hasbro common stock.

In December 1995, Time Warner issued approximately 23 million Company-obligated mandatorily redeemable preferred securities of a wholly-owned subsidiary ("Preferred Trust Securities") for aggregate gross proceeds of \$575 million. The sole assets of the subsidiary that is the obligor on the Preferred Trust Securities are \$592 million principal amount of 8 7/8% subordinated debentures of Time Warner due December 31, 2025. Cumulative cash distributions are payable on the Preferred Trust Securities at an annual rate of 8 7/8%. Cash distributions may be deferred at the election of Time Warner for any period not exceeding 20 consecutive quarters. The Preferred Trust Securities are mandatorily redeemable for cash on December 31, 2025, and Time Warner has the right to redeem the Preferred Trust Securities, in whole or in part, on or after December 31, 2000, or in other certain circumstances, in each case at an amount per Preferred Trust Security equal to \$25 plus accrued and unpaid distributions thereon.

Time Warner has certain obligations relating to the PERCS and the Preferred Trust Securities which amount to a full and unconditional guaranty of each subsidiary's obligations with respect thereto.

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### 9. CAPITAL STOCK

The outstanding capital stock of Time Warner at December 31, 1995 consisted of 29.7 million shares of preferred stock and 387.7 million shares of common stock (net of 45.7 million shares of common stock in treasury, as to which 43.7 million were held by the Time Warner General Partners). At January 31, 1996, including each brokerage house that holds shares of Time Warner common stock as one shareholder but excluding the number of shareholders whose shares are beneficially held by such brokerage houses, there were approximately 25,000 holders of record of Time Warner common stock.

During 1995, Time Warner issued approximately 29.3 million shares of convertible preferred stock in connection with the ITOCHU/Toshiba Transaction and its acquisitions of KBLCOM and Summit, and in January 1996, Time Warner issued an additional 6.5 million shares of convertible preferred stock in connection with its acquisition of CVI and related companies. Set forth below is a summary of the principal terms of Time Warner's outstanding issues of preferred stock:

<i>Description (millions)</i>	<i>Shares outstanding</i>	<i>Number of shares of common stock issuable upon conversion</i>	<i>Earliest exchange date</i>	<i>Earliest redemption date</i>
Series B Preferred Stock	4	-	-	At any time
Series C Preferred Stock	3.3	6.8	5/2/98	5/2/00
Series D Preferred Stock	11.0	22.9	7/6/99	7/6/00
Series G Preferred Stock	6.2	12.9	9/5/99	9/5/99
Series H Preferred Stock	1.8	3.7	9/5/00	9/5/99
Series I Preferred Stock	7.0	14.6	10/2/99	10/2/99
Series outstanding at December	29.7	60.9		

31, 1995				
Series E				
Preferred				
Stock issued	3.3	6.8	1/4/01	1/4/01
in January				
1996				
Series F				
Preferred				
Stock issued	3.2	6.7	1/4/00	1/4/01
in January				
1996				
<hr/>				
Total shares				
outstanding				
at January	36.2	74.4		
31, 1996				
<hr/>				

Each share of Series B Preferred Stock: (1) is entitled to a liquidation preference of \$145 per share, (2) is not convertible, (3) entitles the holder thereof to receive an annual dividend equal to \$4.35 per share beginning in June 1995, and \$9.28 per share prior thereto, (4) does not generally entitle the holder thereof to vote, except in certain limited circumstances, and (5) is redeemable, in whole or in part, by Time Warner and the holders thereof in exchange for cash or shares of any class or series of publicly-traded Time Warner stock, at Time Warner's option, equal in value to the liquidation value of the Series B Preferred Stock plus a premium of 2% of liquidation value for each year after May 31, 1995 to the redemption date.

The principal terms of each series of convertible preferred stock issued in 1995 and 1996 (the Series C Preferred Stock, the Series D Preferred Stock, the Series E Preferred Stock, the Series F Preferred Stock, the Series G Preferred Stock, the Series H Preferred Stock and the Series I Preferred Stock, and collectively, the "Convertible Preferred Stock") are similar in nature, unless otherwise noted below. Each share of Convertible Preferred Stock: (1) is entitled to a liquidation preference of \$100 per share, (2) is immediately convertible into 2.08264 shares of Time Warner common stock at a conversion price of \$48 per share (based on its liquidation value), except that shares of the Series H Preferred Stock are generally not convertible until September 5, 2000, (3) entitles the holder thereof (i) to receive for a four year period from the date of issuance (or a five year period with respect to the Series C and Series E Preferred Stock) an annual dividend per share equal to the greater of \$3.75 and an amount equal to the dividends paid on the Time Warner common stock into which each share may be converted and (ii) to the extent that any of such shares of preferred stock remain outstanding at the end of the period in which the minimum \$3.75 per share dividend is to be paid, the holders thereafter will receive dividends equal to the dividends paid on shares of Time Warner common stock multiplied by the number of shares into which their shares of preferred stock are convertible and (4) except for the Series H Preferred Stock which is generally not entitled to vote, entitles the holder thereof to vote with the common stockholders on all matters on which the common stockholders are entitled to vote, and each share of such Convertible Preferred Stock is entitled to two votes on any such matter.

Time Warner has the right to exchange each series of Convertible Preferred Stock for Time Warner common stock at the stated conversion price at any time on or after the respective exchange date. The Series C Preferred Stock is exchangeable by the holder beginning after the third year from its date of issuance and by Time Warner after the fourth year at the stated conversion price plus a declining premium in years four and five and no premium thereafter. In addition, Time Warner has the right to redeem each series of Convertible Preferred Stock, in whole or in part, for cash at the

liquidation value plus accrued dividends, at any time on or after the respective redemption date.

Pursuant to a shareholder rights plan adopted in January 1994, Time Warner distributed one right per common share which currently becomes exercisable in certain events involving the acquisition of 15% or more of the then outstanding common stock of Time Warner. Upon the occurrence of such an event, each right entitles its holder to purchase for \$150 the economic equivalent of common stock of Time Warner, or in certain circumstances, of the acquirer, worth twice as much. In connection with the plan, 4 million shares of preferred stock were reserved. The rights expire on January 20, 2004. In connection with the TBS Transaction, Time Warner expects to amend the shareholder rights plan principally to change the basis for determining if an acquisition of 15% or more of Time Warner common stock has occurred to a fully-diluted basis.

In 1993, Time Warner redeemed or exchanged \$6.4 billion of Series C and Series D preferred stock ("old Series C and Series D preferred stock") that were issued in Time Warner's 1989 acquisition of WCI. The cash redemption of the old Series D preferred stock was financed principally by the proceeds from the issuance of long-term notes and debentures. The old Series C preferred stock was exchanged for the 8.75% Convertible Debentures.

At December 31, 1995, Time Warner had reserved 172.6 million shares of common stock for the conversion of its Convertible Preferred Stock, zero coupon convertible notes and other convertible securities, and for the exercise of outstanding options to purchase shares of common stock, excluding 25.7 million shares related to the 8.75% Convertible Debentures which were redeemed in February 1996 (Note 6).

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#### 10. STOCK OPTION PLANS

Options to purchase Time Warner common stock under various stock option plans have been granted to employees of Time Warner and TWE at, or in excess of, fair market value at the date of grant. Generally, the options become exercisable over a three-year vesting period and expire ten years from the date of grant.

A summary of stock option activity under all plans is as follows:

	<i>Thousands of shares</i>	<i>Exercise price per share</i>
Balance at January 1, 1995	77,611	\$ 8-48
Granted	5,096	34-45
Exercised	(3,721)	8-40
Cancelled	(367)	17-45
Balanced at December 31, 1995	78,619	\$ 17-48

<i>December 31, (thousands)</i>	<i>1995</i>	<i>1994</i>
Exercisable	66,242	63,106
Available for future grants	7,884	8,849

For options exercised by employees of TWE, Time Warner is reimbursed for the amount by which the market value of Time Warner common stock on the exercise date exceeds the exercise price, or the greater of the exercise price or \$27.75 for options granted prior to the TWE capitalization on June 30, 1992. There were 28.5 million options held by employees of TWE at December 31, 1995, 21.8 million of which were exercisable. There were 1.3 million options exercised in 1994 and 4.8 million options exercised in 1993, at prices ranging from \$8-\$36 per share in each year.

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### 11. BENEFIT PLANS

Time Warner and its subsidiaries have defined benefit pension plans covering substantially all domestic employees. Pension benefits are based on formulas that reflect the employees' years of service and compensation levels during their employment period. Qualifying plans are funded in accordance with government pension and income tax regulations. Plan assets are invested in equity and fixed income securities.

Pension expense included the following:

<i>Years ended December 31, (millions)</i>	1995	1994	1993
Service Cost	\$ 29	\$ 34	\$ 25
Interest cost	53	50	45
Actual return on plan assets	(137)	(2)	(52)
Net amortization and deferral	89	(45)	10
<b>Total</b>	<b>\$ 34</b>	<b>\$ 37</b>	<b>\$ 28</b>

The status of funded pension plans is as follows:

<i>December 31, (millions)</i>	1995	1994
Accumulated benefit obligation (89% vested)	\$ 544	\$ 394
Effect of future salary increases	192	132
Projected benefit obligation	736	526
Plan assets at fair value	643	495
Projected benefit obligation in excess of plan assets	(93)	(31)
Unamortized actuarial losses	94	49
Unamortized plan changes	2	(7)
Other	(10)	(8)
Prepaid (accrued) pension expense	\$ (7)	\$ 3

The following assumptions were used in accounting for pension plans:

	1995	1994	1993
Weighted average discount rate	7.25%	8.5%	7.5%

Return on plan assets	9%	9%	9%
Rate of increase in compensation	6%	6%	6%

Employees of Time Warner's operations in foreign countries participate to varying degrees in local pension plans, which in the aggregate are not significant.

Time Warner also has an employee stock ownership plan, 401(k) savings plans and other savings and profit sharing plans, as to which the expense amounted to \$51 million in 1995, \$51 million in 1994 and \$46 million in 1993. Contributions to the 401(k) and other savings plans are based upon a percentage of the employees' elected contributions. Contributions to the employee stock ownership and profit sharing plans are generally determined by management and approved by the board of directors of the participating companies.

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## 12. FINANCIAL INSTRUMENTS

The carrying value of Time Warner's financial instruments approximates fair value, except for differences with respect to long-term, fixed-rate debt and related interest rate swap contracts and certain differences related to cost method investments and other financial instruments which are not significant. The fair value of financial instruments, such as long-term debt and investments, is generally determined by reference to market values resulting from trading on a national securities exchange or in an over-the-counter market. In cases where quoted market prices are not available, such as for derivative financial instruments, fair value is based on estimates using present value or other valuation techniques.

### Interest Rate Risk Management

Interest rate swap contracts are used to adjust the proportion of total debt that is subject to variable and fixed interest rates. Under interest rate swap contracts, the Company either agrees to pay an amount equal to a specified floating-rate of interest times a notional principal amount, and to receive in return an amount equal to a specified fixed-rate of interest times the same notional principal amount or, vice versa, to receive a floating-rate amount and to pay a fixed-rate amount. The notional amounts of the contracts are not exchanged. No other cash payments are made unless the contract is terminated prior to maturity, in which case the amount paid or received in settlement is established by agreement at the time of termination, and usually represents the net present value, at current rates of interest, of the remaining obligations to exchange payments under the terms of the contract. Interest rate swap contracts are entered into with a number of major financial institutions in order to minimize credit risk.

The net amounts paid or payable, or received or receivable, through the end of the accounting period are included in interest expense. Because interest rate swap contracts are used to modify the interest characteristics of Time Warner's outstanding debt from a fixed to a floating-rate basis or, vice versa, unrealized gains or losses on interest rate swap contracts are not recognized in income unless the contracts are terminated prior to their maturity. Gains or losses on any contracts terminated early are deferred and amortized to income over the remaining average life of the terminated contracts.

At December 31, 1995, Time Warner had interest rate swap contracts to pay floating-rates of interest (average six-month LIBOR rate of 5.9%) and receive fixed-rates of interest (average rate of 5.4%) on \$2.6 billion notional amount of indebtedness, which resulted in approximately 43% of Time Warner's underlying debt being subject to variable interest rates. The notional amount of outstanding contracts by year of maturity at December 31, 1995 is as follows: 1996-\$300 million, 1998-\$700 million, 1999-\$1.2 billion, and 2000-\$400 million. At December 31, 1994, Time Warner had interest rate swap contracts on \$2.9 billion notional amount of indebtedness.

Based on the level of interest rates prevailing at December 31, 1995, the fair value of Time Warner's fixed-rate debt exceeded its carrying value by \$407 million and it would have cost \$9 million to terminate the related interest rate swap contracts, which combined is the equivalent of an unrealized loss of \$416 million. Based on Time Warner's fixed-rate debt and related interest rate swap contracts outstanding at December 31, 1995, each 25 basis point increase or decrease in the level of

interest rates prevailing at December 31, 1995 would result in a net reduction or increase in the combined unrealized loss of approximately \$185 million, respectively, including respective costs or savings of \$16 million to terminate the related interest rate swap contracts. Based on the level of interest rates prevailing at December 31, 1994, the fair value of Time Warner's fixed-rate debt was \$572 million less than its carrying value and it would have cost \$236 million to terminate its interest rate swap contracts, which combined was the equivalent of an unrealized gain of \$336 million.

Although changes in the unrealized gains or losses on interest rate swap contracts and debt do not result in the realization or expenditure of cash unless the contracts are terminated or the debt is retired, each 25 basis point increase or decrease in the level of interest rates related to Time Warner's variable-rate debt and interest rate swap contracts would respectively increase or decrease Time Warner's annual interest expense and related cash payments by approximately \$12 million, including \$7 million related to interest rate swap contracts.

### **Foreign Exchange Risk Management**

Foreign exchange contracts are used primarily by Time Warner to hedge the risk that unremitted or future royalties and license fees owed to Time Warner or TWE 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. As part of its overall strategy to manage the level of exposure to the risk of foreign currency exchange rate fluctuations, Time Warner hedges a portion of its and TWE's combined foreign currency exposures anticipated over the ensuing twelve month period. At December 31, 1995, Time Warner has effectively hedged approximately half of the combined estimated foreign currency exposures that principally relate to anticipated cash flows to be remitted to the U.S. over the ensuing twelve month period, using foreign exchange contracts that generally have maturities of three months or less, which are generally rolled over to provide continuing coverage throughout the year. Time Warner often closes foreign exchange sale contracts by purchasing an offsetting purchase contract. At December 31, 1995, Time Warner had contracts for the sale of \$504 million and the purchase of \$140 million of foreign currencies at fixed rates, primarily English pounds (29% of net contract value), German marks (19%), Canadian dollars (16%), French francs (16%) and Japanese yen (5%), compared to contracts for the sale of \$551 million and the purchase of \$109 million of foreign currencies at December 31, 1994.

Unrealized gains or losses related to foreign exchange contracts are recorded in income as the market value of such contracts change; accordingly, the carrying value of foreign exchange contracts approximates market value. The carrying value of foreign exchange contracts was not material at December 31, 1995 and 1994 and is included in other current liabilities. No cash is required to be received or paid with respect to the realization of such gains and losses until the related foreign exchange contracts are settled, generally at their respective maturity dates. In 1995 and 1994, Time Warner had \$20 million and \$33 million, respectively, and TWE had \$11 million and \$20 million, respectively, of net losses on foreign exchange contracts, which were or are expected to be offset by corresponding increases in the dollar value of foreign currency royalties and license fee payments that have been or are anticipated to be received in cash from the sale of U.S. copyrighted products abroad. Time Warner reimburses or is reimbursed by TWE for contract gains and losses related to TWE's foreign currency exposure. Foreign currency contracts are placed with a number of major financial institutions in order to minimize credit risk.

Based on the foreign exchange contracts outstanding at December 31, 1995, each 5% devaluation of the U.S. dollar as compared to the level of foreign exchange rates for currencies under contract at December 31, 1995 would result in approximately \$25 million of unrealized losses and \$7 million of unrealized gains on foreign exchange contracts involving foreign currency sales and purchases, respectively. Conversely, a 5% appreciation of the U.S. dollar would result in \$25 million of unrealized gains and \$7 million of unrealized losses, respectively. At December 31, 1995, none of

Time Warner's foreign exchange purchase contracts relates to TWE's foreign currency exposure. However, with regard to the \$25 million of unrealized losses or gains on foreign exchange sale contracts, Time Warner would be reimbursed by TWE, or would reimburse TWE, respectively, for approximately \$6 million related to TWE's foreign currency exposure. Consistent with the nature of the economic hedge provided by such foreign exchange contracts, such unrealized gains or losses would be offset by corresponding decreases or increases, respectively, in the dollar value of future foreign currency royalty and license fee payments that would be received in cash within the ensuing twelve month period from the sale of U S copyrighted products abroad.

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#### 13. SEGMENT INFORMATION

Time Warner's businesses are conducted in three fundamental areas: Entertainment, consisting principally of interests in recorded music and music publishing, filmed entertainment, broadcasting, theme parks and cable television programming; News and Information, consisting principally of interests in magazine publishing, book publishing and direct marketing, and Telecommunications, consisting principally of interests in cable television systems. Time Warner's interests in filmed entertainment, broadcasting, theme parks, cable television programming and most of its telecommunications business are held by the Entertainment Group, which is not consolidated for financial reporting purposes.

Information as to the operations of Time Warner and the Entertainment Group in different business segments is set forth below. Cable business segment information for Time Warner reflects the 1995 acquisitions of KBLCOM and Summit. Cable business segment information for the Entertainment Group reflects the consolidation by TWE of the TWE-Advance/Newhouse Partnership effective as of April 1, 1995 and Paragon effective as of July 6, 1995. The operating results of Six Flags have been deconsolidated effective as of June 23, 1995 and results prior to that date are reported separately to facilitate comparability.

<i>Years Ended</i>				
<i>December 31,</i>		<i>1995</i>	<i>1994</i>	<i>1993</i>
<i>(millions)</i>				
<b>REVENUES</b>				
<b>Time Warner</b>				
Publishing	\$3,722	\$3,433	\$3,270	
Music	4,196	3,986	3,334	
Cable	172	-	-	
Intersegment elimination	(23)	(23)	(23)	
<b>Total</b>	<b>\$8,067</b>	<b>\$7,396</b>	<b>\$5,581</b>	
<b>Entertainment Group</b>				
Filmed Entertainment	\$5,078	\$4,484	\$4,032	
Six Flags Theme parks	227	557	533	
Broadcasting-the WB Network	33	-	-	
Programming-HBO	1,607	1,513	1,441	
Cable	3,094	2,242	2,208	
Intersegment elimination	(410)	(287)	(251)	
<b>Total</b>				



<b>Total</b>	<b>\$9,629</b>	<b>\$8,509</b>	<b>\$7,963</b>
--------------	----------------	----------------	----------------

<i>Years Ended December 31, (millions)</i>	<i>1995</i>	<i>1994</i>	<i>1993</i>
--	-------------	-------------	-------------

**OPERATING INCOME**

**Time Warner**

Publishing	\$381	\$347	\$295
Music*	321	366	296
Cable	(5)	-	-

<b>Total</b>	<b>\$697</b>	<b>\$</b>	<b>\$</b>
		713	591

**Entertainment Group**

Filmed Entertainment	\$	\$	\$
	253	219	233
Six Flags Theme parks	29	56	53
Broadcasting-the WB Network	(66)	-	-
Programming-HBO	274	237	213
Cable	502	340	406

<b>Total</b>	<b>\$992</b>	<b>\$852</b>	<b>\$905</b>
--------------	--------------	--------------	--------------

<i>Years Ended December 31, (millions)</i>	<i>1995</i>	<i>1994</i>	<i>1993</i>
--	-------------	-------------	-------------

**DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT**

**Time Warner**

Publishing	\$ 59	\$ 47	\$ 45
Music	95	86	87
Cable	27	-	-

<b>Total</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
	181	133	132

**Entertainment Group**

Filmed Entertainment	\$	\$ 76	\$ 51
	113		
Six Flags Theme parks	20	51	41
Broadcasting-the WB Network	-	-	-
Programming-HBO	18	14	14
Cable	465	340	327

<b>Total</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
	616	481	433



*Years Ended December  
31, (millions)*      1995 1994 1993

**AMORTIZATION OF  
INTANGIBLE  
ASSETS**

**Time Warner**

Publishing	\$ 36	\$ 36	\$ 32
Music	274	268	260
Cable	68	-	-
<b>Total</b>	<b>\$378</b>	<b>\$ 304</b>	<b>\$ 292</b>

**Entertainment Group**

Filmed Entertainment	\$ 124	\$ 135	\$ 143
Six Flags Theme Parks	11	28	28
Broadcasting-the WB Network	-	-	-
Programming-HBO	1	6	3
Cable	308	309	302
<b>Total</b>	<b>\$444</b>	<b>\$478</b>	<b>\$476</b>

Information as to the assets and capital expenditures of Time Warner and the Entertainment Group is as follows:

*Years Ended  
December 31,  
(millions)*      1995    1994    1993

**ASSETS**

**Time Warner**

Publishing	\$ 2,175	\$ 2,013	\$ 1,897
Music	7,828	7,672	7,401
Cable	3,875	-	-
<b>Entertainment Group*</b>	<b>5,734</b>	<b>5,350</b>	<b>5,627</b>
<b>Corporate**</b>	<b>2,520</b>	<b>1,681</b>	<b>1,967</b>

<b>Total</b>	<b>\$ 22,132</b>	<b>\$ 16,716</b>	<b>\$ 16,892</b>
--------------	------------------	------------------	------------------

**Entertainment  
Group**

Filmed Entertainment	\$ 7,389	\$ 7,184	\$ 6,719
Six Flags Theme parks	-	814	848
Broadcasting-the WB Network	63	-	-
Programming-HBO	935	911	875

Cable	9,842	8,303	8,102
Corporate**	731	1,780	1,658
<b>Total</b>	<b>\$13,960</b>	<b>\$18,992</b>	<b>\$18,202</b>

\* Entertainment Group assets represent Time Warner's investment in and amounts due to and from the Entertainment Group

\*\* Consists principally of cash, cash equivalents and other investments

*Years Ended December  
31. (millions)*      1995   1994   1993

**CAPITAL  
EXPENDITURES**

**Time Warner**

Publishing	\$ 70	\$ 50	\$ 41
Music	121	108	91
Cable	56	-	-
Corporate	19	6	66
<b>Total</b>	<b>\$ 266</b>	<b>\$ 164</b>	<b>\$ 198</b>

**Entertainment Group**

Filmed Entertainment	\$ 294	\$ 395	\$ 210
Six Flags Theme Parks	43	46	34
Broadcasting-the WB Network	-	-	-
Programming-HBO	20	14	16
Cable*	1,293	778	353
Corporate	3	2	-
<b>Total</b>	<b>\$ 1,653</b>	<b>\$ 1,235</b>	<b>\$ 613</b>

*Years Ended  
December 31.  
(millions)*      1995   1994   1993

**Revenues**

United States*	\$ 5,447	\$ 4,944	\$ 4,414
Europe	1,552	1,445	1,296
Pacific Rim	775	724	583
Rest of World	293	283	288
<b>Total</b>	<b>\$ 8,067</b>	<b>\$ 7,396</b>	<b>\$ 6,581</b>

**Operating  
Income**

United States	\$ 457	\$ 494	\$ 436
Europe	158	108	102
Pacific Rim	57	74	28

Rest of World	25	37	25
<b>Total</b>	<b>\$ 697</b>	<b>\$ 713</b>	<b>\$ 591</b>
<b>Assets</b>			
United States	\$19,301	\$13,961	\$14,328
Europe	1,797	1,717	1,635
Pacific Rim	628	636	514
Rest of World	406	402	415
<b>Total</b>	<b>\$22,132</b>	<b>\$16,716</b>	<b>\$16,892</b>

\* Time Warner's revenues do not include the revenues of the Entertainment Group, which had export revenues of \$1.982 billion in 1995, \$1.693 billion in 1994 and \$1.650 billion in 1993, principally from the sale of Filmed Entertainment products abroad.

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#### 14. COMMITMENTS AND CONTINGENCIES

Total rent expense amounted to \$174 million in 1995, \$157 million in 1994 and \$163 million in 1993. The minimum rental commitments under noncancellable long-term operating leases are: 1996-\$147 million; 1997-\$133 million; 1998-\$139 million; 1999-\$130 million; 2000-\$123 million and after 2000-\$923 million.

Minimum commitments and guarantees under certain licensing, artists and other agreements aggregated approximately \$2.9 billion at December 31, 1995, which are payable principally over a five-year period. Such amounts do not include the Time Warner General Partner guarantees of approximately \$6 billion of TWE debt.

Pending legal proceedings are substantially limited to litigation incidental to the businesses of Time Warner, alleged damages in connection with class action lawsuits and pending litigation with U S WEST. In the opinion of counsel and management, the ultimate resolution of these matters will not have a material effect on the financial statements of Time Warner.

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#### 15. ADDITIONAL FINANCIAL INFORMATION

Additional financial information with respect to cash flows is as follows

<i>Years Ended December 31, (millions)</i>	<i>1995</i>	<i>1994</i>	<i>1993</i>
Cash payments made for interest	\$ 659	\$ 539	\$ 330
Cash payments made for income taxes	302	389	234
Tax-related distributions received from TWE	680	115	-
Income tax refunds received	24	50	52

During the years ended December 31, 1995 and 1994, Time Warner realized \$35 million and \$179 million, respectively, from the securitization of receivables. Noncash investing and financing activities in 1995 included the \$1.4 billion acquisitions of KBLCOM and Summit in exchange for capital stock (Note 4), the \$1.36 billion acquisition of ITOCHU's and Toshiba's interests in TWE in exchange for capital stock and \$10 million in cash (Note 2) and the \$1.8 billion redemption of Time Warner's Reset Notes in exchange for other debt securities (Note 6). Noncash financing activities in 1993 included the issuance of approximately \$3.1 billion of debentures in exchange for the old Series C preferred stock (Note 9).

Other current liabilities consist of:

<i>December 31, (millions)</i>	<i>1995</i>	<i>1994</i>
Accrued expenses	\$ 972	\$ 794
Accrued compensation	337	308
Accrued income taxes	173	81
Deferred revenues	84	55
<b>Total \$ 1,566</b>	<b>\$ 1,238</b>	

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**Report of Management**

The accompanying consolidated financial statements have been prepared by management in conformity with generally accepted accounting principles, and necessarily include some amounts that are based on management's best estimates and judgments.

Time Warner maintains a system of internal accounting controls designed to provide management with reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly. The concept of reasonable assurance is based on the recognition that the cost of a system of internal control should not exceed the benefits derived and that the evaluation of those factors requires estimates and judgments by management. Further, because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected. Nevertheless, management believes that a high level of internal control is maintained by Time Warner through the selection and training of qualified personnel, the establishment and communication of accounting and business policies, and its internal audit program.

The Audit Committee of the Board of Directors, composed solely of directors who are not employees of Time Warner, meets periodically with management and with Time Warner's internal auditors and independent auditors to review matters relating to the quality of financial reporting and internal accounting control, and the nature, extent and results of their audits. Time Warner's internal auditors and independent auditors have free access to the Audit Committee.

**GERALD M. LEVIN**

Chairman and  
Chief Executive Officer

**RICHARD D. PARSONS**

President

**RICHARD J. BRESSLER**

Senior Vice President  
and Chief Financial Officer

**Report of Independent Auditors**

**THE BOARD OF DIRECTORS AND SHAREHOLDERS**

**TIME WARNER INC.**

We have audited the accompanying consolidated balance sheet of Time Warner Inc. ("Time Warner") as of December 31, 1995 and 1994, and the related consolidated statements of operations, cash flows and shareholders' equity for each of the three years in the period ended December 31, 1995. These financial statements are the responsibility of Time Warner's management. Our

responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Time Warner at December 31, 1995 and 1994, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1995, in conformity with generally accepted accounting principles.

**ERNST & YOUNG**  
New York, New York

February 6, 1996

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**Selected Financial Information**

The selected financial information for each of the five years in the period ended December 31, 1995 set forth below has been derived from and should be read in conjunction with the financial statements and other financial information presented elsewhere herein. Capitalized terms are as defined and described in such consolidated financial statements, or elsewhere herein. The selected historical financial information for all periods after 1992 reflects the deconsolidation of the Entertainment Group, principally TWE, effective January 1, 1993.

The selected historical financial information for 1995 reflects the issuance of 29.3 million shares of convertible preferred stock having an aggregate liquidation preference of \$2.926 billion in connection with (i) the acquisitions of KBL.COM and Summit and (ii) the exchange by Toshiba and ITOCHU of their direct and indirect interests in TWE. The selected historical financial information for 1993 reflects the issuance of \$6.1 billion of long-term debt and the use of \$5 billion of cash and equivalents for the exchange or redemption of preferred stock having an aggregate liquidation preference of \$6.4 billion. The selected historical financial information for 1992 reflects the capitalization of TWE on June 30, 1992 and associated refinancings, and the acquisition of the 18.7% minority interest in ATC as of June 30, 1992, using the purchase method of accounting for business combinations.

Per common share amounts and average common shares have been restated to give effect to the



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### Quarterly Financial Information (Unaudited)

(millions, except per share amounts)

Quarter	Revenues	Operating Income of Business Segments	Equity in Pretax Income (Loss) of Entertainment Group	Net Income (Loss)	Net Income (loss) Applicable to Common Shares **	Dividends Per Common Share	Average Common Shares	Common Stock		
								High	Low	
<b>1995</b>										
1st	\$1,817	\$ 138	\$ 22	\$ (47)	\$ (50)	\$ (0.13)	\$ 0.09	379.5	\$ 39 1/4	\$ 33 5/8
2nd	1,907	184	84	(8)	(13)	(0.03)	0.09	381.4	43 1/2	34 1/4
3rd*	1,981	21	129	(144)	(160)	(0.41)	0.09	386.5	45 5/8	38 7/8
4th	2,362	354	21	33	5	0.01	0.09	387.5	41 1/4	35 3/4
Year*	8,067	697	256	(166)	(218)	(0.57)	0.36	383.8	45 5/8	33 5/8
<b>1994</b>										
1st	\$1,558	\$ 112	\$ 45	\$ (51)	\$ (54)	\$ (0.14)	0.08	378.6	\$44 1/4	\$ 35 5/8
2nd	1,666	170	66	(20)	(23)	(0.06)	0.09	378.8	40 5/8	34 1/2
3rd	1,884	141	66	(32)	(35)	(0.09)	0.09	379.1	38 3/4	34
4th	2,287	290	(1)	12	8	0.02	0.09	379.2	37 3/4	31 1/2
Year	7,396	713	176	(91)	(104)	(0.27)	0.35	378.9	44 1/4	31 1/2

\* Business segment operating income for the third quarter of 1995 includes \$85 million in losses relating to certain businesses and joint ventures owned by the Music Division which were restructured or closed. The net loss for the third quarter of 1995 includes an extraordinary loss on the retirement of debt of \$42 million (\$ 11 per common share)

\*\* After preferred dividend requirements.

\*\*\* Per common share amounts for the quarters and full years have been calculated separately. Accordingly, quarterly amounts may be calculated separately. Accordingly, quarterly amounts may not add to the annual amount because of differences in

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### Corporate Management Group

**GERALD M. LEVIN**  
*Chairman and  
Chief Executive Officer*

**PETER R. HAJE**  
*Executive Vice President,  
General Counsel and Secretary*

**TOD R. HULLIN**  
*Senior Vice President*

**TIMOTHY A. BOGGS**  
*Senior Vice President*

**RICHARD D. PARSONS**  
*President*

**RICHARD J. BRESSLER**  
*Senior Vice President and  
Chief Financial Officer*

**PHILIP R. LOCHNER JR.**  
*Senior Vice President*

### Board of Directors

**GERALD M. LEVIN**  
*Chairman and  
Chief Executive Officer,  
Time Warner Inc.*

**EDWARD S.  
FINKELSTEIN**  
*Chairman,  
Finkelstein Associates,  
Inc.*

**HENRY LUCE III**  
*Chairman and CEO,  
The Henry Luce  
Foundation Inc.*

**DONALD S. PERKINS**  
*Former Chairman,  
Jewel Companies, Inc.*

**RICHARD D.  
PARSONS**  
*President,  
Time Warner Inc.*

**BEVERLY SILLS  
GREENOUGH**  
*Chairman,  
Lincoln Center for  
the Performing Arts*

**REUBEN MARK**  
*Chairman and CEO,  
Colgate-Palmolive Company*

**RAYMOND S.  
TROUBH**  
*Financial consultant and  
director of various  
companies*

**MERV ADELSON**  
*Chairman,  
East-West Capital  
Associates*

**AMBASSADOR CARLA A.  
HILLS**  
*Chairman and CEO,  
Hills & Company, and  
former United States Trade  
Representative*

**MICHAEL A. MILES**  
*Former Chairman and  
CEO,  
Philip Morris  
Companies Inc.*

**FRANCIS T. VINCENT  
JR.**  
*Chairman,  
Vincent Enterprises*

**LAWRENCE B.  
BUTTENWIESER**  
*Partner,  
Rosenman & Colin*

**DAVID T. KEARNS**  
*Retired Chairman and  
CEO,  
Xerox Corporation*

**J. RICHARD MUNRO**  
*Chairman of the  
Executive/Finance  
Committee of the Board,  
Time Warner Inc.*

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# Operating Officers

## ENTERTAINMENT

### Warner Bros.

#### **ROBERT A. DALY**

*Chairman and Co-CEO*

#### **TERRY S. SEMEL**

*Chairman and Co-CEO*

#### **BARRY M. MEYER**

*Executive Vice President and COO*

#### **RICHARD J. FOX**

*Executive Vice President, International Theatrical Enterprises*

#### **JAMES R. MILLER**

*Executive Vice President, Business and Acquisitions*

#### **SANFORD R. REISENBACH**

*Executive Vice President, Marketing and Planning*

#### **EDWARD A. ROMANO**

*Executive Vice President and CFO*

#### **STEPHEN ROSS**

*Executive Vice President, Special Projects*

#### **JOHN A. SCHULMAN**

*Executive Vice President and General Counsel*

#### Warner Bros. Worldwide Theatrical Production

#### **BRUCE BERMAN**

*President*

#### Warner Bros. Worldwide Theatrical Advertising and Publicity

#### **ROBERT G. FRIEDMAN**

*President*

#### Warner Bros. International Theatrical Distribution

#### **EDWARD E. FRUMKES**

*President*

#### Warner Home Video

#### **WARREN LIEBERFARB**

*President*

#### Warner Bros. Domestic Theatrical Distribution

#### **D. BARRY REARDON**

*President*

Warner Bros. Music

**GARY LE MEL**

*President*

Warner Bros. Domestic Television Production

**TONY JONAS**

*President*

Warner Bros. Domestic Television Distribution

**RICHARD T. ROBERTSON**

*President*

Warner Bros. International Television Distribution

**JEFFREY SCHLESINGER**

*President*

Warner Bros. Domestic Pay-TV, Cable and Network Features

**EDWARD BLEIER**

*President*

Warner Bros. Television Animation

**JEAN MACCURDY**

*President*

Warner Bros. Feature Animation

**MAX HOWARD**

*President*

Warner Bros. International Theatres

**MILLARD OCHS**

*President*

Warner Bros. Worldwide Consumer Products

**DANIEL R. ROMANELLI**

President Warner Bros. Worldwide Licensing

**GEORGE JONES**

President Warner Bros. Worldwide Studio Stores

**PETER STARRETT**

*President*

Warner Bros. International recreation Enterprises

**NICHOLAS WINSLOW**

*President*

Warner Bros. Studios facilities

**GARY CREDLE**

*President*

**Elektra Entertainment Group**

**SYLVIA RHONE**

*Chairman and CEO*



**AARON LEVY**  
*Vice Chairman and COO*

**SEYMOUR STEIN**  
*President*

**DC Comics**

**JENETTE KAHN**  
*President and Editor-In-Chief*

**PAUL LEVITZ**  
*Executive Vice President and Publisher*

**The Atlantic Group**

**AHMET M. ERTEGUN**  
*Co-Chairman and Co-CEO*

**VAL AZZOLI**  
*Co-Chairman and Co-CEO*

Warner Music Group  
**ROBERT A. DALY**  
*Chairman and Co-CEO*

**TERRY S. SEMEL**  
*Chairman and Co-CEO*

**JEROME N. GOLD**  
*Executive Vice President and CFO*

**FRED WISTOW**  
*Executive Vice President and General Counsel*

**Warner Bros. Records**

**RUSS THYRET**  
*Chairman and CEO*

**DAVID ALTSCHUL**  
*Vice Chairman*

**COLIN HODGSON**  
*Executive Vice President and CFO*

**STEVEN BAKER**  
*President, Warner Bros. records*

**HOWIE KLEIN**  
*President, Reprise records*

**Warner Music International**

**RAMON LOPEZ**  
*Chairman and CEO*

**STEPHEN SHRIMPTON**  
*President*

**JAMES CARADINE**  
*Executive Vice President*

**KEN COOPER**  
*Executive Vice President and CFO*

**PETER ANDRY**  
*Warner Classics International*

**ANDRE MIDANI**  
*President, Warner Music Latin America*

**MANFRED ZUMKELLER**  
*President, Warner Music Europe*

**WEA Inc.**

**DAVID MOUNT**  
*Chairman and CEO*

**ELLIS KERN**  
*President and Co-CEO*

**RICK WIETSMA**  
*Executive Vice President and Co-CEO*

**Warner/Chappell Music**

**LESLIE E. BIDER**  
*Chairman and CEO*

**IRA PLANKO**  
*Chief Operating Officer and CFO*

**RICK SHOEMAKER**  
*President*

**Warner Special Products**

**ANTHONY PIPITONE**  
*President and CEO*

**Home Box Office**

**JEFFREY L. BEWKES**  
*Chairman, President and CEO*

**SETH G. ABRAHAM**

*Executive Vice President and President, Time Warner Sports*

**CHRIS ALBRECHT**

*Executive Vice President and President, Original Programming and HBO Independent Productions*

**JOHN K. BILLOCK**

*Executive Vice President and President, HBO Sales and Marketing*

**LARRY P. CARLSON**

*Executive Vice President and President, HBO Satellite Services*

**ROBERT COOPER**

*Executive Vice President and President, HBO Pictures and HBO NYC Productions*

**WILLIAM C. NELSON**

*Executive Vice President and CFO*

**JOHN S. REDPATH JR.**

*Executive Vice President and General Counsel*

**STEPHEN J. SCHEFFER**

*Executive Vice President and President, Film Programming, Video, and Enterprises*

**CURTIS G. VIEBRANZ**

*Executive Vice President and President, HBO International*

**HAROLD AKSELRAD**

*Senior Vice President, Business Affairs*

**DAVID BALDWIN**

*Senior Vice President, Program Planning*

**VINTON H. BAUER**

*Senior Vice President, HBO Direct*

**ALBERT COLLIS JR.**

*Senior Vice President, Information Technology*

**SHELEY D. FISCHER**

*Senior Vice President, Human Resources and Administration*

**ROBERT S. GRASSI**

*Senior Vice President, Affiliate relations*

**LESLIE H. JACOBSON**

*Senior Vice President, Film Programming*

**ERIC KESSLER**

*Senior Vice President, HBO Marketing*

**HENRY MCGEE**

*Senior Vice President and President, HBO Video*

**SHEILA NEVINS**

*Senior Vice President, Documentary and Family Programming*

**RICHARD PLEPLER**

*Senior Vice President, Corporate Communications*

**DOMINIC SERIO**

*Senior Vice President, Studio and Broadcast Operations*

**RICHARD WALTZER**

*Senior Vice President, HBO Pictures*

**ROBERT M. ZITTER**

*Senior Vice President, Technology Operations*

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### Operating Officers

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#### NEWS AND INFORMATION

Time Inc.

**REGINALD K. BRACK, JR.**  
*Chairman*

**SUSAN CAUGHMAN**  
*Senior Vice President,  
Consumer Marketing*

**E. BRUCE HALLETT**  
*President, Time*  
**ANN S. MOORE**  
*President, People*

**TOM ANGELILLO**  
*President and CEO,  
Southern Progress  
Corporation*

**Little, Brown and Company**  
**CHARLES E. HAYWARD**  
*President and CEO*

**Time Life Inc.**  
**GEORGE ARTANDI**  
*President and CEO*  
**Editorial Executives**

**NORMAN PEARLSTINE**  
*Editor-In-Chief, Time  
Warner Inc.*

**DON LOGAN**  
*President and  
CEO*

**JAMES GRAHAM**  
*Senior Vice President,  
Corporate Sales and  
Marketing*

**MICHAEL PEPE**  
*Group Publisher,  
Fortune and Money*

**STEVE SEABOLT**  
*President and  
CEO, Sunset  
Publishing  
Corporation*

**Warner Books,  
Inc.**  
**LAURENCE J. KIRSHBAUM**  
*President and CEO*

**HENRY MULLER**  
*Editorial  
Director*

**JOSEPH A. RIPP**  
*Executive Vice President and  
CFO*

**JIM NELSON**  
*President and CEO,  
Time Publishing  
Ventures*

**MICHAEL J. KLINGENSMITH**  
*Publisher,  
Entertainment Weekly*

**ELIZABETH VALK LONG**  
*Executive Vice  
President*

**DONALD M. ELLIMAN, JR.**  
*President, Sports  
Illustrated*

**EDWARD R. MACCARRICK**  
*Publisher, Life*

**Book-of-the-Month  
Club, Inc.**  
**GEORGE ARTANDI**  
*President and CEO*

**JAMES R. GAINES**  
*Corporate Editor*

**PAUL SAGAN**  
*President and Editor,  
New Media*

**WALTER  
ISAACSON**  
*Managing Editor,  
Time*

**LONDON Y.  
JONES, JR.**  
*Managing Editor,  
People*

**JOHN HUEY III**  
*Managing Editor,  
Fortune*

**FRANK LALLI**  
*Managing Editor,  
Money*

**WILLIAM R.  
COLSON**  
*Managing Editor,  
Sports Illustrated*

**DANIEL  
OKRENT**  
*Managing  
Editor, Life*

**JAMES W.  
SEYMORE JR.**  
*Managing Editor,  
Entertainment Weekly*

#### TELECOMMUNICATIONS

**Time Warner Cable**  
**JOSEPH J. COLLINS**  
*Chairman and CEO*

**JAMES H.  
DOOLITTLE**  
*President and COO*

**TOMMY J.  
HARRIS**  
*Chief Financial  
Officer*

**JAMES P.  
COTTINGHAM**  
*Executive Vice  
President*

**THEODORE J. CUTLER**  
*Executive Vice President*

**CHARLES W.  
ELLIS**  
*Executive Vice  
President*

**JOHN F. GAULT**  
*Executive Vice  
President*

**THOMAS M.  
RUTLEDGE**  
*Executive Vice  
President*

**Time Warner Cable of New  
York City**

**Time Warner  
Cable Ventures**

**Time Warner  
Cable**

**RICHARD AURELIO**  
*President*

**GLENN A. BRITT**  
*President and CEO*

**Programming**  
**E. THAYER  
BIGELOW JR.**  
*President and CEO*

1995 Time Warner Annual Report

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# TIME WARNER

## 1995 ANNUAL REPORT

### Building Global Brands

#### Investor Information

#### COMMON STOCK INFORMATION

##### EXCHANGE LISTINGS

Time Warner (ticker symbol "TWX") is listed on the New York Stock Exchange, the Pacific Stock Exchange and the London Stock Exchange

##### TRANSFER AGENT

Chemical Mellon Shareholder Services, L.L.C.  
85 Challenger Road  
Ridgefield Park, NJ 07660  
(212) 613-7427  
(800)279-1238

##### DIVIDEND REINVESTMENT AND STOCK PURCHASE PLAN

Holders of Time Warner common stock can obtain information about this plan by calling Chemical Mellon Shareholder Services, L.L.C. at (800) 279-1238

##### CORPORATE PUBLICATIONS

Copies of Time Warner's Form 10-K annual report, Annual Report, Quarterly Reports and Social responsibility report are available without charge by writing or calling

##### INDEPENDENT AUDITORS

Ernst & Young LLP

Shareholder Relations

Time Warner Inc  
75 Rockefeller Plaza  
New York, NY 10019  
(212)484-6971

#### FIXED INCOME INFORMATION

##### TIME WARNER INC.

###### Debt Securities

- 7.45% Notes due 1998
- 7.95% Notes due 2000
- Floating Rate Notes due 2000
- 10.75% Senior debentures of Cablevision Industries Inc. due 2002
- 7.975% Notes due 2004
- 7.75% Notes due 2005
- 10.5% Debentures of Summit Communications Group Inc. due 2005
- 8.11% Debentures due 2006
- 8.18% Debentures due 2007
- 9.25% Senior Debentures of Cablevision Industries Inc. due 2008
- 7.48% Debentures due 2008
- Liquid Yield Option Notes due 2012
- Liquid Yield Option Notes due 2013
- 9.1/8% Debentures due 2013
- 8.05% Debentures due 2016
- 8.3/4% Debentures due 2017
- 9.15% Debentures due 2023
- 6.85% Debentures due 2026
- 8.30% Discount Debentures due 2036

###### Mandatorily Redeemable Preferred Securities

- 4% Preferred Exchangeable Redemption Cumulative Securities of Time Warner Financing Trust due 1997
- 8.875% Preferred Trust Securities of Time Warner Capital I due 2025

##### TIME WARNER ENTERTAINMENT COMPANY, L.P.

- 9.5/8% Senior Notes due 2002
- 7.1/4 % Senior Debentures due 2008
- 8.7/8% Senior Notes due 2012
- 10.15% Senior Notes due 2017
- 8.3/8% Senior Debentures due 2023

##### TRUSTEES

- Chemical Bank
- Chemical Bank
- Chemical Bank
- Bankers Trust Company
- Chemical Bank
- Chemical Bank
- Fleet bank
- Chemical Bank
- Chemical Bank
- First National Bank of Boston
- Chemical Bank
- Chemical Bank
- Chemical Bank
- Chemical Bank
- Marine Midland Bank N.A.
- Chemical Bank
- Chemical Bank
- Chemical Bank
- Chemical Bank
- Chemical Bank
- First National Bank of Chicago
- First National Bank of Chicago

##### TRUSTEES

- Bank of New York
- Bank of New York
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# TIME WARNER

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*[Click Here](#) to download a PDF copy of the entire 1996 Time Warner Annual Report.*

*[Click Here](#) to download a PDF copy of the financials only.*



## Financial Highlights

Years Ended December 31, (millions, except per share amounts)	Pro Forma <sup>(a)</sup>		Historical	
	1996	1995	1996	1995
<b>EBITDA<sup>(b)</sup></b>				
<b>Time Warner</b>				
Publishing	\$ 535	\$ 476	\$ 535	\$ 476
Music	744	690 <sup>(c)</sup>	744	690 <sup>(c)</sup>
Cable Networks-TBS	547	502	162	-
Filmed Entertainment-TBS	(108)	48	32	-
Cable	476	425	476	90
Intersegment elimination	(10)	6	5	-
<b>Time Warner EBITDA</b>	<b>\$ 2,184</b>	<b>\$ 2,147</b>	<b>\$ 1,954</b>	<b>\$ 1,256</b>
<b>Entertainment Group</b>				
Filmed Entertainment-Warner Bros.	\$ 546	\$ 490	\$ 546	\$ 490
Six Flags Theme Parks <sup>(d)</sup>	-	-	-	60
Broadcasting-The WB Network	(98)	(66)	(98)	(66)
Cable Networks-HBO	350	293	350	293
Cable	1,536	1,355	1,536	1,275
<b>Entertainment Group EBITDA</b>	<b>\$ 2,334</b>	<b>\$ 2,072</b>	<b>\$ 2,334</b>	<b>\$ 2,052</b>
<b>Combined EBITDA</b>	<b>\$ 4,518</b>	<b>\$ 4,219</b>	<b>\$ 4,288</b>	<b>\$ 3,308</b>
<b>Combined Revenues<sup>(e)</sup></b>	<b>\$ 23,660</b>	<b>\$ 21,840</b>	<b>\$ 20,925</b>	<b>\$ 17,696</b>
<b>Loss before extraordinary item</b>	<b>\$ (284)</b>	<b>\$ (233)</b>	<b>\$ (156)</b>	<b>\$ (124)</b>
<b>Net loss<sup>(f)</sup></b>	<b>\$ (318)</b>	<b>\$ (275)</b>	<b>\$ (191)</b>	<b>\$ (165)</b>
<b>Loss per common share, after preferred dividend requirements:</b>				
Loss before extraordinary item	\$ (1.05)	\$ (.87)	\$ (.95)	\$ (.46)
<b>Net loss</b>	<b>\$ (1.11)</b>	<b>\$ (1.04)</b>	<b>\$ (1.04)</b>	<b>\$ (.57)</b>

(a) Pro forma results give effect to the TBS Transaction, the Cable Transactions, the ITOCHU/Toshiba Transaction, and certain debt refinancings and asset sales, as if such transactions occurred at the beginning of the respective periods. Each of these transactions is more fully discussed in Management's Discussion and Analysis of Results of Operations and Financial Condition included elsewhere herein. The pro forma results are presented for informational purposes only and are not necessarily indicative of the operating results that would have occurred had the transactions actually occurred at the beginning of those periods, nor are they necessarily indicative of future operating results.

(b) EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) presents business segment operating income before depreciation and amortization expense, including amortization relating to the \$14 billion acquisition of Warner Communications Inc. in 1989, the \$1.3 billion acquisition of the minority interest in American Television and Communications Corporation in 1992, the \$2.3 billion acquisitions of KBLCOM Incorporated, Summit Communications Group, Inc. and Cablevision Industries Corporation and related companies in 1995 and 1996, the \$6.2 billion acquisition of Turner Broadcasting System, Inc. in 1996 and other business combinations accounted for by the purchase method. Although it is one Wall Street measures cash flow, EBITDA is not adjusted for all noncash expenses or for working capital, capital expenditures and other investment requirements. EBITDA should be considered in addition to, not as a substitute for, other measures of financial performance and liquidity, as more fully discussed in Management's Discussion and Analysis included elsewhere herein.

(c) Includes \$88 million of losses recorded in 1995 related to certain businesses and joint ventures owned by the Music division which were restructured or closed.

(d) Deconsolidated as a result of the sale of a 31% interest in Six Flags effective as of June 23, 1995.

(e) On a pro forma basis, combined revenues for 1996 and 1995, respectively, consist of \$12,799 billion and \$12,154 billion for Time Warner and \$10,861 billion and \$9,686 billion for the Entertainment Group. On a historical basis, combined revenues for 1996 and 1995, respectively, consist of \$10,064 billion and \$8,067 billion for Time Warner and \$10,861 billion and \$9,829 billion for the Entertainment Group. Time Warner does not consolidate the Entertainment Group for financial reporting purposes.

(f) The net loss for the years ended December 31, 1996 and 1995 includes an extraordinary loss on the retirement of debt of \$35 million and \$42 million, respectively.

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## Management's Discussion and Analysis of Results of Operations and Financial Condition

On October 10, 1996, Time Warner Inc. ("Time Warner" or the "Company"), acquired the remaining 80% interest in Turner Broadcasting System, Inc. ("TBS") that it did not already own. As a result of this transaction, a new parent company with the name "Time Warner Inc." replaced the old parent company of the same name ("Old Time Warner", now known as Time Warner Companies, Inc.), and Old Time Warner and TBS became separate, wholly owned subsidiaries of the new parent company ("New Time Warner"). References herein to "Time Warner" or the "Company" refer to Old Time Warner prior to October 10, 1996 and New Time Warner thereafter.

Time Warner classifies its business interests into four fundamental areas: Entertainment, consisting principally of interests in recorded music and music publishing, filmed entertainment, television production, television broadcasting and theme parks; Cable Networks, consisting principally of interests in cable television programming and sports franchises; Publishing, consisting principally of interests in magazine publishing, book publishing and direct marketing; and Cable, consisting principally of interests in cable television systems. A majority of Time Warner's interests in filmed entertainment, television production, television broadcasting and theme parks, a portion of its interests in cable television programming and a majority of its cable television systems are held through Time Warner Entertainment Company, L.P. ("TWE"). Time Warner owns general and limited partnership interests in TWE consisting of 74.49% of the pro rata priority capital ("Series A Capital") and residual equity capital ("Residual Capital"), and 100% of the senior priority capital ("Senior Capital") and junior priority capital ("Series B Capital"). The remaining 25.51% limited partnership interests in the Series A Capital and Residual Capital of TWE are held by a subsidiary of U.S. WEST, Inc. ("U.S. WEST"). Time Warner does not consolidate TWE and certain related companies (the "Entertainment Group") for financial reporting purposes because of certain limited partnership approval rights related to TWE's interest in certain cable television systems. Capitalized terms are as defined and described in the accompanying consolidated financial statements, or elsewhere herein.

### STRATEGIC INITIATIVES

**Significant Transactions** During the past two years, Time Warner has pursued significant, strategic initiatives that have resulted in the acquisition of TBS and the expansion of Time Warner's interests in the cable television business. These initiatives were part of an ongoing strategy to strengthen Time Warner's interests in entertainment and cable television programming, and to expand the operation of large geographic clusters of cable television systems in an effort to achieve economies of scale in the development and distribution of new and expanded services. Over the same period, management also engaged in a program to improve the combined financial condition of Time Warner and the Entertainment Group, as well as to increase their overall financial flexibility, through the initiation of a debt reduction program and significant debt refinancings.

Management believes its expansion strategy has largely achieved its objectives and intends to sharpen its focus on improving the combined financial condition of Time Warner and the Entertainment Group and increasing their overall financial flexibility through additional initiatives, such as continued debt reduction and implementation of various cost-savings and revenue-enhancing measures designed to augment fundamental business growth.

Consistent with management's strategic direction, Time Warner completed the following transactions in 1996 that have had and are expected to continue to have a significant effect on its results of operations and financial condition:

- The acquisition in October 1996 of the remaining 80% interest in TBS that was not already owned (the "TBS Transaction"). In connection with this transaction, New Time Warner issued or agreed to issue approximately 178.4 million shares of common stock, approximately 14 million stock options and \$67 million of consideration payable, at its election, in either cash or common stock. New Time Warner also assumed approximately \$2.8 billion of indebtedness. The addition of TBS's news and entertainment programming networks, film and animation libraries, film production companies and sports franchises is expected to complement virtually all of Time Warner's business interests.

- The implementation in April 1996 of a program to repurchase, from time to time, up to 15 million shares of Time Warner common stock. This program is supported, in part, by a five-year, \$750 million revolving credit facility which is expected to be repaid principally from the cash proceeds from the future exercise of employee stock options. As of December 31, 1996, Time Warner had acquired approximately 11.4 million shares of its common stock for an aggregate cost of \$456 million.
- The issuance in April 1996 of 1.6 million shares of a new series of exchangeable preferred stock, which currently pays cumulative, non-cash dividends at the rate of 10 1/4% per annum. The approximate \$1.55 billion of net proceeds raised from this transaction were used to reduce debt (the "Preferred Stock Refinancing"). Along with other actions since the initiation of a \$2-\$3 billion debt reduction program in February 1995, including the expected 1997 sale of TWE's interest in E! Entertainment Television, Inc., Time Warner and the Entertainment Group have exceeded their initial goals under this program.
- The redemption in 1996 and early 1997 of approximately \$1.5 billion of convertible debt using proceeds from other financings, which lowered interest rates, staggered debt maturities and eliminated the potential dilution from the conversion of such securities into 31.3 million shares of common stock.
- The acquisition of Cablevision Industries Corporation and related companies ("CVI") on January 4, 1996 (the "CVI Acquisition"), which strengthened Time Warner Cable's geographic clusters of cable television systems and substantially increased the number of cable subscribers managed by Time Warner Cable. Time Warner issued 2.9 million shares of common stock and 6.3 million shares of new convertible preferred stock and assumed or incurred approximately \$2 billion of indebtedness. As of December 31, 1996, Time Warner Cable, which includes the cable operations of both Time Warner and TWE, served approximately 12.3 million subscribers, passing nearly 20% of the television homes in the U.S.

The nature of these transactions and their impact on the results of operations and financial condition of Time Warner and the Entertainment Group are further discussed below.

**TBS Transaction.** In the TBS Transaction, each of Old Time Warner and TBS became separate, wholly owned subsidiaries of New Time Warner, which combines, for financial reporting purposes, the consolidated net assets and operating results of Old Time Warner and TBS. Each issued and outstanding share of each class of capital stock of Old Time Warner was converted into one share of a substantially identical class of capital stock of New Time Warner.

In connection with the TBS Transaction, New Time Warner issued (i) approximately 173.4 million shares of common stock (including 50.8 million shares of LMCN-V Class Common Stock to affiliates of Liberty Media Corporation ("LMC"), a subsidiary of Tele-Communications, Inc.), in exchange for shares of TBS capital stock and (ii) approximately 14 million stock options to replace all outstanding TBS stock options. In addition, New Time Warner agreed to issue to LMC and its affiliates at a later date an additional five million shares of LMCN-V Class Common Stock and \$67 million of consideration payable, at the election of New Time Warner, in cash or additional shares of LMCN-V Class Common Stock. This additional consideration will be issued pursuant to a separate option and non-competition agreement that will provide, if New Time Warner exercises its option, for a subsidiary of LMC to provide certain satellite uplink and distribution services for WTBS, a broadcast television station owned by TBS, if it is converted to a copyright-paid, cable television programming service. The cost to acquire TBS was approximately \$6.2 billion. New Time Warner has also fully and unconditionally guaranteed all of TBS's and Old Time Warner's outstanding publicly traded indebtedness, which amounted to approximately \$1.030 billion and \$7.754 billion, respectively, at December 31, 1996.

As part of the integration of TBS's businesses into Time Warner's operating structure, management is pursuing various cost-saving and revenue-enhancing initiatives. Such initiatives, some of which have already been implemented, include the consolidation of certain duplicative administrative and operational functions (such as transferring the management of TBS's television syndication and home video operations to Warner Bros.), the restructuring of TBS's film production companies,

the planned conversion of WTBS from a broadcast superstation into a copyright paid, cable television programming service; the creation of new basic cable television networks (such as CNN/SI, Time Warner's sports news network) and other revenue-enhancing activities, including the cross-promotion of animation assets, film libraries and children's programming.

In restructuring TBS's film production activities, Time Warner has already phased out all production activities of Turner Pictures and is evaluating alternatives for Castle Rock Entertainment ("Castle Rock") and New Line Cinema ("New Line"). These alternatives range from an equity transaction interest in these studios to a nonrecourse financing transaction.

**Cable Strategy** Over the past two years, Time Warner has combined with or acquired cable television systems serving approximately 3.7 million subscribers (the "Cable Transactions"), which, along with internal growth, has increased the total number of subscribers under the management of Time Warner Cable to 12.3 million from 7.5 million subscribers at the end of 1994. This expansion strategy has also extended Time Warner Cable's reach of cable television systems to neighborhoods passing 19 million homes or close to 20% of television homes in the U.S. In addition, there are now 34 geographic clusters of cable television systems serving over 100,000 subscribers each, including key markets such as New York City, northern New York State, central Florida and North Carolina. Management believes that the improved concentration of its subscriber base will provide for sustained revenue growth from new and expanded services, and provide certain economies of scale relating to the upgrade of the technological capabilities of Time Warner Cable's cable television systems.

Time Warner's current strategy is to restructure its cable television systems, so far as practicable and on a tax-efficient basis, to enable such interests to be self-financed. As part of this strategy, Time Warner is seeking to reduce its economic interest in the cable television business in order to reduce existing debt and its share of future funding requirements related to such cable operations. The primary alternative being pursued is a restructuring of TWE that would decrease Time Warner's cable interests in TWE and increase Time Warner's interests in TWE's entertainment and cable networks. Any TWE restructuring depends, among other things, upon successful negotiations with U.S. WEST and other third parties, a renegotiation of certain credit arrangements, including the 1995 Credit Agreement, and consents or approvals from cable television franchise and other regulatory authorities, in addition to, or in lieu of, a TWE restructuring, other alternatives remain available to Time Warner to advance these goals, some of which would not require U.S. WEST consent but would still require other third party, franchise and regulatory approvals. There is no assurance that any of these efforts will succeed.

**Use of EBITDA** The following comparative discussion of the results of operations and financial condition of Time Warner and the Entertainment Group includes, among other factors, an analysis of changes in the operating income of the business segments before depreciation and amortization ("EBITDA") in order to eliminate the effect on the operating performance of the music, filmed entertainment, cable network and cable businesses of significant amounts of amortization of intangible assets recognized in the \$14 billion acquisition of WCI in 1989, the \$1.3 billion acquisition of the ATC minority interest in 1992, the \$2.3 billion of Cable Acquisitions in 1995 and 1996, the



\$6.2 billion acquisition of TBS in 1996 and other business combinations accounted for by the purchase method. Financial analysts generally consider EBITDA to be an important measure of comparative operating performance for the businesses of Time Warner and the Entertainment Group, and when used in comparison to debt levels or the coverage of interest expense, as a measure of liquidity. However, EBITDA should be considered in addition to, not as a substitute for, operating income, net income, cash flow and other measures of financial performance and liquidity reported in accordance with generally accepted accounting principles.

#### **TRANSACTIONS AFFECTING COMPARABILITY OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION**

In connection with management's strategic initiatives, Time Warner and the Entertainment Group have completed a number of transactions over the past two years which have affected the comparability of each entity's results of operations and financial condition. For Time Warner, these transactions include the TBS Transaction, the Cable Acquisitions, the ITOCHU/Toshiba Transaction, the Preferred Stock Refinancing and certain other debt refinancings (the "TW Transactions"). For the Entertainment Group, these transactions include the formation of the TWE-Advance/Newhouse Partnership, the refinancing of TWE's bank debt and certain asset sales, including the sale of 51% of TWE's interest in Six Flags (the "Entertainment Group Transactions" and, when taken together with the TW Transactions, the "Time Warner Transactions"). Each of these transactions is more fully discussed elsewhere herein.

In order to enhance comparability, the following discussion of results of operations for Time Warner and the Entertainment Group is supplemented, where appropriate, by pro forma

financial information that gives effect to the Time Warner Transactions and the Entertainment Group Transactions, respectively, as if such transactions had occurred at the beginning of the respective periods presented. The pro forma results are presented for informational purposes only and are not necessarily indicative of the operating results that would have occurred had the transactions actually occurred at the beginning of those periods, nor are they necessarily indicative of future operating results.

#### **RESULTS OF OPERATIONS**

As a result of the TBS Transaction, Time Warner now has two new business segments which parallel its previously existing interests in filmed entertainment and cable television programming held through TWE. Time Warner's Cable Networks segment principally consists of TBS's cable television networks and sports operations. These operations include entertainment networks such as TNT, the TBS Superstation, the Cartoon Network and Turner Classic Movies; news networks such as CNN, CNN International and CNN Headline News; and sports franchises consisting of the Atlanta Braves and the Atlanta Hawks. Time Warner's Filmed Entertainment segment principally consists of TBS's film and television production and distribution operations, including New Line, Castle Rock, Hanna-Barbera, Inc. and the former film and television libraries of Metro-Goldwyn-Mayer, Inc. and RKO Pictures, Inc. Because the results of operations of these businesses and Time Warner's cable businesses are not comparable to the prior period, the following discussion of business segments' operating results is presented on both a historical and pro forma basis.

1996 VS. 1995

EBITDA and operating income for Time Warner and the Entertainment Group in 1996 and 1995 are as follows:

Years Ended December 31, (millions)	EBITDA				Operating Income			
	Pro Forma		Historical		Pro Forma		Historical	
	1996	1995	1996	1995	1996	1995	1996	1995
<b>Time Warner:</b>								
Publishing	\$ 535	\$ 476	\$ 535	\$ 476	\$ 418	\$ 381	\$ 418	\$ 381
Music <sup>(1)</sup>	744	690	744	690	361	321	361	321
Cable Networks - TBS	547	502	162	-	297	267	99	-
Filmed Entertainment - TBS	(108)	48	32	-	(202)	(62)	8	-
Cable	476	425	476	90	75	29	75	(5)
Intersegment elimination	(10)	8	8	-	(10)	8	5	-
<b>Total</b>	<b>\$ 2,184</b>	<b>\$ 2,147</b>	<b>\$ 1,954</b>	<b>\$ 1,256</b>	<b>\$ 939</b>	<b>\$ 942</b>	<b>\$ 986</b>	<b>\$ 697</b>
<b>Entertainment Group:</b>								
Filmed Entertainment - Warner Bros.	\$ 546	\$ 490	\$ 546	\$ 490	\$ 254	\$ 253	\$ 254	\$ 253
Six Flags Theme Parks <sup>(2)</sup>	-	-	-	60	-	-	-	29
Broadcasting - The WB Network	(98)	(66)	(98)	(66)	(98)	(66)	(98)	(66)
Cable Networks - HBO	350	293	350	293	328	274	328	274
Cable	1,538	1,355	1,538	1,275	606	533	606	502
<b>Total</b>	<b>\$ 2,334</b>	<b>\$ 2,072</b>	<b>\$ 2,334</b>	<b>\$ 2,052</b>	<b>\$ 1,090</b>	<b>\$ 994</b>	<b>\$ 1,090</b>	<b>\$ 992</b>

(1) Includes pretax losses of \$85 million recorded in 1995 related to certain businesses and joint ventures owned by the Music division which were restructured or closed.  
 (2) Deconsolidated as a result of the sale of a 51% interest in Six Flags effective as of June 23, 1995.

Time Warner had revenues of \$10.064 billion, a loss of \$156 million (\$.95 per common share) before an extraordinary loss on the retirement of debt and a net loss of \$191 million (\$1.04 per common share) in 1996, compared to revenues of \$8.067 billion, a loss of \$124 million (\$.46 per common share) before an extraordinary loss on the retirement of debt and a net loss of \$166 million (\$.57 per common share) in 1995. Time Warner's equity in the pretax income of the Entertainment Group was \$290 million in 1996, compared to \$256 million in 1995.

As discussed more fully below, the increase in Time Warner's historical net loss in 1996 principally resulted from an increase in interest expense relating to approximately \$6.1 billion of debt assumed or incurred in the TBS Transaction and the Cable Acquisitions and a decrease in investment related income primarily relating to lower gains on certain asset sales, which more than offset an overall increase in the operating income of Time Warner's business segments and increased income from its equity in the pretax income of the Entertainment Group. The increase in Time Warner's 1996 historical net loss per common share was further affected by a \$205 million

increase in preferred dividend requirements relating to the preferred stock issued in connection with the Preferred Stock Refinancing, the Cable Acquisitions and the ITOCHU/Toshiba Transaction, offset in part by the dilutive effect from issuing 173.4 million shares of common stock in connection with the TBS Transaction.

Time Warner's historical results of operations include the operating results of each acquired business from the respective closing date of each transaction. On a pro forma basis, giving effect to the Time Warner Transactions as if each of such transactions had occurred at the beginning of 1995, Time Warner would have reported for the years ended December 31, 1996 and 1995, respectively, revenues of \$12.799 billion and \$12.154 billion, EBITDA of \$2.184 billion and \$2.147 billion, operating income of \$939 million and \$942 million, equity in the pretax income of the Entertainment Group of \$290 million and \$286 million, a loss before extraordinary item of \$284 million and \$233 million (\$1.05 and \$.97 per common share) and a net loss of \$319 million and \$275 million (\$1.11 and \$1.04 per common share).

The 1996 and 1995 comparison of pro forma results are similarly affected by any underlying historical trends that are unrelated to the transactions given pro forma effect to therein, such as lower gains on certain asset sales discussed above. The increased pro forma over historical net loss for each period is principally the result of higher amortization and interest expense associated with the TBS Transaction and the Cable Acquisitions. The 1996 pro forma results are further affected by the significant pre-merger operating losses incurred by TBS's filmed entertainment companies as a consequence of disappointing results from worldwide theatrical releases.

The Entertainment Group had revenues of \$10.861 billion and net income of \$220 million in 1996, compared to revenues of \$9.629 billion, income of \$170 million before an extraordinary loss on the retirement of debt and net income of \$146 million in 1995. On a pro forma basis, giving effect to the Entertainment Group Transactions as if each of such transactions had occurred at the beginning of 1995, the Entertainment Group would have reported for the year ended December 31, 1995, revenues of \$9.686 billion, EBITDA of \$2.072 billion, operating income of \$994 million, income before extraordinary item of \$203 million and net income of \$179 million. No pro forma financial information has been presented for the Entertainment Group for the year ended December 31, 1996 because all of such transactions are already reflected, in all material respects, in the historical financial statements of the Entertainment Group.

As discussed more fully below, the Entertainment Group's historical net income was higher in 1996 as compared to pro forma results in 1995 due to an overall increase in operating income generated by its business segments, interest savings due to lower floating interest rates and the absence of a \$24 million extraordinary loss on the retirement of debt recognized in 1995, offset in part by a decrease in investment-related income and an increase in minority interest expense related to the TWE-Advance/Newhouse Partnership. On a historical basis, such underlying operating trends were enhanced by favorable comparisons as 1996 more fully benefited from the interest savings on lower average debt levels related to management's ongoing debt reduction program.

The relationship between income before income taxes and income tax expense of Time Warner is principally affected by the amortization of goodwill and certain other financial statement expenses that are not deductible for income tax

purposes. Income tax expense of Time Warner includes all income taxes related to its allocable share of partnership income and its equity in the income tax expense of corporate subsidiaries of the Entertainment Group.

#### TIME WARNER

**Publishing** Revenues increased to \$4.117 billion, compared to \$3.722 billion in 1995. EBITDA increased to \$535 million from \$478 million. Depreciation and amortization amounted to \$117 million in 1996 and \$95 million in 1995. Operating income increased to \$418 million from \$381 million. Revenues benefited from across-the-board increases in magazine circulation, advertising and book revenues. All major magazine brands achieved revenue gains, including *People*, *Entertainment Weekly* and *Sports Illustrated*, the latter of which benefited in part from Olympics-related coverage. The increase in book revenues was led by the direct marketing businesses. EBITDA and operating income increased principally as a result of the revenue gains.

**Music** Revenues decreased to \$3.949 billion, compared to \$4.196 billion in 1995. EBITDA increased to \$744 million from \$690 million. Depreciation and amortization, including amortization related to the purchase of WCI, amounted to \$383 million in 1996 and \$369 million in 1995. Operating income increased to \$361 million from \$321 million. Operating results for 1995 included an \$85 million charge relating to certain start-up businesses and joint ventures owned by the Music division which were restructured or closed. With regard to 1996, despite maintaining its leading domestic market share (over 22%), the Music division's domestic recorded music operating results were negatively affected by the industry-wide softness in the overexpanded U.S. retail marketplace, which has resulted in a number of music retail store closings and higher returns of music product. The decline in revenues principally related to (i) the effects from the current U.S. retail environment, including an increase in the Music division's provision for returns, (ii) a decline in international recorded music sales and (iii) the absence of revenues from certain start-up businesses which are no longer being operated by the Music division. The increase in EBITDA and operating income principally resulted from the absence of losses from certain start-up businesses and joint ventures, the absence of the \$85 million charge recognized in 1995 and the inclusion of certain one-time gains, including gains

on the sale of investments, offset in part by the decline in the worldwide recorded music business, a related increase in the Music division's provision for bad debts and lower results from direct marketing activities. Management expects that the current state of the U.S. retail environment will continue to affect 1997 operating results.

**Cable Networks - TBS** Cable Networks results reflect the acquisition of TBS effective in October 1996 and include revenues of \$680 million, EBITDA of \$162 million, depreciation and amortization of \$63 million and operating income of \$99 million. Such operating results are not comparable to the prior year and, accordingly, are discussed on a pro forma basis.

On a pro forma basis, revenues increased to \$2.477 billion, compared to \$2.106 billion in 1995. EBITDA increased to \$547 million from \$502 million. Depreciation and amortization, including amortization related to the purchase of TBS, amounted to \$250 million in 1996 and \$235 million in 1995. Operating income increased to \$297 million from \$267 million. Revenues benefited from increases in advertising and subscriptions. Advertising revenues increased due to a strong overall advertising market for TNT and the TBS Superstation, the continued expansion of CNN International, and increased viewership for the news networks during the 1996 U.S. political conventions and presidential campaign. Subscription revenues increased as a result of higher rates, as well as an increase in both cable and home satellite viewers, primarily at TNT, the Cartoon Network, CNN and CNN International. EBITDA and operating income increased principally as a result of the revenue gains, offset in part by higher sports and entertainment programming costs and start-up costs for three new networks, including CNN/51.

**Filmed Entertainment - TBS** Filmed Entertainment results reflect the acquisition of TBS effective in October 1996, and include revenues of \$455 million, EBITDA of \$32 million, depreciation and amortization of \$24 million and operating income of \$8 million. Such operating results are not comparable to the prior year and, accordingly, are discussed on a pro forma basis.

On a pro forma basis, revenues increased to \$1.458 billion, compared to \$1.352 billion in 1995. EBITDA decreased from \$48 million in 1995 to a loss of \$108 million in 1996. Depreciation and amortization, including amortization related to the purchase

of TBS, amounted to \$94 million in 1996 and \$110 million in 1995. Operating losses increased to \$202 million from \$62 million. Revenues benefited from increases in worldwide theatrical and home video revenues. Worldwide theatrical revenues benefited from an increase in the number of theatrical releases. Home video revenues increased primarily due to an increase in sales of theatrical and existing library product. Despite such revenue increases, EBITDA and operating income decreased principally as a result of disappointing results for theatrical releases, which resulted in approximately \$200 million of write-offs at New Line and Castle Rock during the nine-month, pre-merger period.

**Cable** The 1996 Cable operating results increased as a result of the CVI Acquisition effective as of January 4, 1996, and the full year effect from the acquisitions of KBLCOM effective as of July 6, 1995 and Summit effective as of May 2, 1995. Revenues increased to \$909 million, compared to \$172 million in 1995. EBITDA increased to \$476 million from \$90 million. Depreciation and amortization amounted to \$401 million in 1996 and \$95 million in 1995. Operating income increased to \$75 million from a loss of \$5 million.

On a pro forma basis, Time Warner's Cable division had 1995 revenues of \$847 million, EBITDA of \$425 million, depreciation and amortization of \$396 million and operating income of \$29 million. In comparison to 1995 pro forma results, 1996 revenues benefited from an increase in basic cable subscribers, increases in regulated cable rates as permitted under Time Warner Cable's "social contract" with the Federal Communications Commission (the "FCC") and an increase in pay per view and advertising revenues. EBITDA and operating income increased principally as a result of revenue gains, offset in part, with respect to operating income only, by higher depreciation and amortization relating to increased capital spending.

**Interest and Other, Net** Interest and other, net, increased to \$1.174 billion in 1996, compared to \$877 million in 1995. Interest expense increased to \$968 million, compared to \$877 million. The increase in interest expense was principally due to the assumption or incurrence of approximately \$6.1 billion of debt in the Cable Acquisitions and the TBS Transaction, offset in part by the favorable effect from Time Warner's redemption of the 8.75% Convertible Debentures and the reduction in debt

associated with the Preferred Stock Refinancing. Other expense, net, increased to \$206 million in 1996 from an immaterial amount in 1995, principally because of a decrease in investment-related income resulting from lower gains on certain asset sales, increased losses from reductions in the carrying value of certain investments and an increase in dividend requirements on preferred securities of subsidiaries issued in 1995 in connection with the redemption of the 8.75% Convertible Debentures.

#### ENTERTAINMENT GROUP

**Filmed Entertainment-Warner Bros.** Revenues increased to \$5.648 billion, compared to \$5.078 billion in 1995. EBITDA increased to \$546 million from \$490 million. Depreciation and amortization, including amortization related to the purchase of WCI, amounted to \$292 million in 1996 and \$237 million in 1995. Operating income increased to \$254 million from \$253 million. Revenues benefited from increases in worldwide home video, television distribution and consumer products operations, offset in part by lower international theatrical revenues. EBITDA and operating income benefited principally from the revenue gains, offset in large part, with respect to operating income only, by higher depreciation and amortization principally related to the 1996 summer opening of an international theme park in Germany.

**Six Flags Theme Parks.** As a result of TWE's sale of 51% of its interest in Six Flags, the operating results of Six Flags have been deconsolidated effective as of June 23, 1995 and TWE's remaining 49% interest in Six Flags is accounted for under the equity method of accounting.

**Broadcasting - The WB Network.** The WB Network recorded an operating loss of \$90 million on \$87 million of revenues in 1996, compared to an operating loss of \$66 million on \$33 million of revenues in 1995. The increase in revenues and operating losses primarily resulted from the expansion of the WB Network's primetime programming schedule (now at three nights) and the expansion of *Kids' WB!*, the network's animated programming lineup on Saturday mornings and weekdays. In addition, operating losses for 1995 were mitigated by a favorable legal settlement. Due to the start-up nature of this national broadcast operation, losses are expected to continue.

**Cable Networks - HBO.** Revenues increased to \$1.763 billion, compared to \$1.607 billion in 1995. EBITDA increased to \$350 million from \$293 million. Depreciation and amortization amounted to \$22 million in 1996 and \$19 million in 1995. Operating income increased to \$328 million from \$274 million. Revenues benefited primarily from a significant increase in subscriptions to 32.4 million from 29.7 million at the end of 1995. EBITDA and operating income improved principally as a result of the revenue gains.

**Cable.** Revenues increased to \$3.851 billion, compared to \$3.094 billion in 1995. EBITDA increased to \$1.536 billion from \$1.275 billion. Depreciation and amortization, including amortization related to the purchase of WCI and the acquisition of the ATC minority interest, amounted to \$930 million in 1996 and \$773 million in 1995. Operating income increased to \$606 million from \$502 million. The 1996 Cable operating results increased as a result of the full year effect from the formation of the TWE-Advance/Newhouse Partnership effective as of April 1, 1995, and the consolidation of Paragon Communications effective as of July 8, 1995.

On a pro forma basis, the Entertainment Group's Cable division had 1995 revenues of \$3.378 billion, EBITDA of \$1.355 billion, depreciation and amortization of \$822 million and operating income of \$533 million. In comparison to 1995 pro forma results, 1996 revenues benefited from an aggregate increase in basic cable and Primestar-related, direct broadcast satellite subscribers, increases in regulated cable rates as permitted under Time Warner Cable's "social contract" with the FCC and increases in pay-per-view and advertising revenues. EBITDA and operating income increased principally as a result of revenue gains, offset in part, with respect to operating income only, by higher depreciation and amortization relating to increased capital spending.

**Interest and Other, Net.** Interest and other, net, decreased to \$524 million in 1996, compared to \$539 million in 1995. Interest expense decreased to \$478 million, compared to \$579 million in 1995, principally as a result of interest savings on lower average debt levels related to management's debt reduction program and lower short-term, floating rates of interest paid on borrowings under TWE's former and existing bank credit agreements.



There was other expense, net, of \$46 million in 1996, compared to other income, net, of \$40 million in 1995, principally due to an overall decrease in investment-related income. The decrease in investment-related income resulted from a reduction in interest income and lower aggregate gains on the sale of certain unclustered cable systems and other investments. The reduction in interest income related to lower average cash balances and lower average principal amounts due under the note receivable from U S WEST that was fully collected during 1996.

#### 1995 VS. 1994

EBITDA and operating income for Time Warner and the Entertainment Group in 1995 and 1994 are as follows:

Years Ended December 31, (millions)	EBITDA		Operating Income	
	1995	1994	1995	1994
<b>Time Warner:</b>				
Publishing	\$ 476	\$ 430	\$ 381	\$ 347
Music <sup>(1)</sup>	690	720	321	366
Cable	90	-	(5)	-
<b>Total</b>	<b>\$1,256</b>	<b>\$1,150</b>	<b>\$ 697</b>	<b>\$ 713</b>
<b>Entertainment Group:</b>				
<b>Filmed Entertainment -</b>				
Warner Bros.	\$ 480	\$ 430	\$ 253	\$ 219
Six Flags Theme Parks <sup>(2)</sup>	60	135	29	56
<b>Broadcasting -</b>				
The WB Network	(66)	-	(66)	-
Cable Networks - HBO	293	257	274	237
Cable	1,275	989	902	340
<b>Total</b>	<b>\$2,052</b>	<b>\$1,811</b>	<b>\$ 992</b>	<b>\$ 852</b>

(1) Includes pretax losses of \$85 million recorded in 1995 related to certain businesses and joint ventures owned by the Music division which were restructured or closed.

(2) Declassified as a result of the sale of a 51% interest in Six Flags effective as of July 23, 1995.

Time Warner had revenues of \$8.067 billion, a loss of \$124 million (\$ .46 per common share) before an extraordinary loss on the retirement of debt and a net loss of \$166 million (\$ .57 per common share) in 1995, compared to revenues of \$7.396 billion and a net loss of \$91 million (\$ .27 per common share) in 1994. Time Warner's equity in the pretax income of the Entertainment Group was \$256 million in 1995, compared to \$176 million in 1994.

The increase in Time Warner's net loss in 1995 was principally related to a \$42 million extraordinary loss on the retirement of debt (\$ .11 per common share) and \$85 million in pretax losses (\$52 million after taxes and \$ .13 per common share) related to certain businesses and joint ventures owned by the Music division which were restructured or closed. As discussed more fully below, the increase in Time Warner's net loss in 1995 from such losses was principally mitigated by an overall increase in the fundamental operating income of Time Warner's business segments and increased income from its equity in the pretax income of the Entertainment Group, offset in part by a decrease in investment-related income and higher interest expense on approximately \$1.3 billion of debt assumed in the acquisitions of Summit and KBLCOM. The increase in Time Warner's net loss per common share in 1995 also related to a \$39 million increase in preferred dividend requirements as a result of the preferred stock issued in connection with the acquisitions of Summit and KBLCOM and the ITOCHU/Toshiba Transaction.

The Entertainment Group had revenues of \$9.629 billion, income of \$170 million before an extraordinary loss on the retirement of debt and net income of \$146 million in 1995, compared to revenues of \$8.509 billion and net income of \$136 million in 1994. As discussed more fully below, the Entertainment Group's operating results in 1995 reflect an overall increase in operating income generated by its business segments (including the contribution by the TWE-Advance/Nowhouse Partnership) and an increase in investment-related income resulting from gains on the sale of certain unclustered cable systems and other investments, offset in part by minority interest expense related to the consolidation of the operating results of the TWE-Advance/Nowhouse Partnership effective as of April 1, 1995.

#### TIME WARNER

**Publishing** Revenues increased to \$3.722 billion, compared to \$3.433 billion in 1994. EBITDA increased to \$476 million from \$430 million. Depreciation and amortization amounted to \$95 million in 1995 and \$83 million in 1994. Operating income increased to \$381 million from \$347 million. Revenues benefited from increases in magazine circulation, advertising and book revenues. Contributing to the revenue gain were increases achieved by *People*, *Sports Illustrated*, *Fortune* and book publisher Oxmoor House. EBITDA and operating income increased as a result of the revenue gains, offset in part by significantly higher postal and paper costs as a result of price increases.

**Music** Revenues increased to \$4.198 billion, compared to \$3.986 billion in 1994. EBITDA decreased to \$690 million from \$720 million. Depreciation and amortization, including amortization related to the purchase of WCI, amounted to \$369 million in 1995 and \$354 million in 1994. Operating income decreased to \$321 million from \$366 million. Operating results were adversely affected by \$85 million in losses recorded in 1995 that related to certain businesses and joint ventures owned by the Music division which were restructured or closed. Revenues for 1995 were negatively affected by certain reclassifications relating to third party, pressing and distribution arrangements and changes in the Music division's ownership interests in certain investments and subsidiaries that resulted in changes from the consolidation to the equity method of accounting. Excluding the effects from such reclassifications and changes, revenues from the fundamental business increased by approximately 8%, principally as a result of increases in both domestic and international recorded music revenues and increased music publishing revenues. Domestic and international recorded music revenues benefited from a number of popular releases and an increase in the percentage of compact disc to total unit sales. Excluding the \$85 million in losses, EBITDA increased, and operating income benefited, principally from the revenue gains and interest income on the resolution of a recorded music tax matter, offset in part by expenses incurred in connection with the settlement of certain employment contracts and lower results from direct marketing activities attributable to higher amortization of member acquisition costs.

The losses in 1995 relating to certain businesses and joint ventures that were restructured or closed are primarily related to Warner Music Enterprises, one of the Company's direct marketing efforts, and the write off of its related direct mail order assets that were not recoverable due to the closure of this business. The activities that were not continued were not material to previous historical operating results.

**Cable** The 1995 Cable operating results reflect the acquisition of KBL.COM effective as of July 6, 1995 and Summit effective as of May 2, 1995 and include revenues of \$172 million, EBITDA of \$90 million, depreciation and amortization of \$95 million and operating losses of \$5 million. Such operating results are not comparable to the prior year.

**Interest and Other, Net** Interest and other, net, increased to \$877 million in 1995, compared to \$724 million in 1994. Interest expense increased to \$877 million, compared to \$769 million, principally as a result of approximately \$1.3 billion of debt assumed in the cable acquisitions and higher short-term, floating rates of interest paid on \$2.6 billion notional amount of interest rate swap contracts. Other income, net, was immaterial in 1995, compared to \$45 million in 1994, principally because of a decrease in investment-related income. Investment-related income in both periods consisted of gains on the sale of certain assets, including the sale of an interest in QVC, Inc. in 1995, which were offset by losses from reductions in the carrying value of certain investments taken in each period.

#### ENTERTAINMENT GROUP

**Filmed Entertainment - Warner Bros.** Revenues increased to \$5.078 billion, compared to \$4.484 billion in 1994. EBITDA increased to \$490 million from \$430 million. Depreciation and amortization, including amortization related to the purchase of WCI, amounted to \$237 million in 1995 and \$211 million in 1994. Operating income increased to \$253 million from \$219 million. Revenues benefited from increases in worldwide theatrical, home video, consumer products and television distribution operations. Worldwide theatrical and domestic home video revenues in 1995 were led by the success of *Batman Forever*. EBITDA and operating income benefited from the revenue gains and increased income from licensing operations.



**Six Flags Theme Parks** As a result of TWE's sale of 51% of its interest in Six Flags, the operating results of Six Flags have been deconsolidated effective as of June 23, 1995 and TWE's remaining 49% interest in Six Flags is accounted for under the equity method of accounting. Accordingly, revenues decreased to \$227 million, compared to \$557 million in 1994. EBITDA decreased to \$60 million from \$135 million. Depreciation and amortization amounted to \$31 million in 1995 and \$79 million in 1994. Operating income decreased to \$29 million from \$56 million.

**Broadcasting - The WB Network** The WB Network was launched in January 1995, and generated \$66 million of operating losses on \$33 million of revenues. The operating loss was mitigated by a favorable legal settlement, as well as by funding from a limited partner admitted as of August 1995. Due to the start-up nature of this national broadcast operation, losses are expected to continue.

**Cable Networks - HBO** Revenues increased to \$1.607 billion, compared to \$1.513 billion in 1994. EBITDA increased to \$293 million from \$257 million. Depreciation and amortization amounted to \$19 million in 1995 and \$20 million in 1994. Operating income increased to \$774 million from \$737 million. Revenues benefited primarily from an increase in subscriptions to 29.7 million from 27 million at the end of 1994, as well as from higher pay-TV rates. EBITDA and operating income improved principally as a result of the revenue gains.

**Cable** The 1995 Cable operating results reflect the formation of the TWE-Advance/Newhouse Partnership effective as of April 1, 1995 and the consolidation of Paragon effective as of July 6, 1995. Revenues increased to \$3.094 billion, compared to \$2.242 billion in 1994. EBITDA increased to \$1.275 billion from \$989 million. Depreciation and amortization, including amortization related to the purchase of WCI and the acquisition of the ATC minority interest, amounted to \$773 million in 1995 and \$649 million in 1994. Operating income increased to \$502 million from \$340 million. Revenues and operating results benefited from the formation of the TWE-Advance/Newhouse Partnership and the consolidation of Paragon. Excluding such effects, revenues benefited from an aggregate increase in basic cable

and Primestar related, direct broadcast satellite subscribers and increases in nonregulated revenues, including pay-TV, pay-per-view and advertising. Excluding the positive contributions from the TWE-Advance/Newhouse Partnership and the consolidation of Paragon, EBITDA and operating income increased as a result of the revenue gains, offset in part by the full year impact of the second round of cable rate regulations that went into effect in July 1994, higher start-up costs for telephony operations and, with respect to operating income only, higher depreciation and amortization related to increased capital spending.

**Interest and Other, Net** Interest and other, net, decreased to \$539 million in 1995, compared to \$616 million in 1994. Interest expense increased to \$579 million, compared to \$567 million in 1994, principally as a result of higher short-term, floating rates of interest paid on borrowings under TWE's former and existing bank credit agreements, offset in part by interest savings in the last quarter of 1995 on lower debt levels related to management's asset sales program. There was other income, net, of \$40 million in 1995, compared to other expense, net, of \$49 million in 1994, principally because of an increase in investment-related income related to gains on the sale of certain unclustered cable systems and other investments.

#### FINANCIAL CONDITION AND LIQUIDITY DECEMBER 31, 1996

##### TIME WARNER

**1996 Financial Condition** At December 31, 1996, Time Warner had \$12.7 billion of debt, \$452 million of available cash and equivalents (net debt of \$12.2 billion), \$488 million of borrowings against future stock option proceeds, \$949 million of mandatorily redeemable preferred securities of subsidiaries, \$1.7 billion of Series M Preferred Stock and \$9.5 billion of shareholders' equity, compared to \$9.9 billion of debt, \$1.2 billion of available cash and equivalents (net debt of \$8.7 billion), \$949 million of mandatorily redeemable preferred securities of subsidiaries and \$3.7 billion of shareholders' equity at December 31, 1995. At December 31, 1996, Time Warner also had \$82 million of noncurrent cash and equivalents held in escrow for purposes of funding certain preferred dividend

requirements. The increase in net debt principally reflects the assumption or incurrence of approximately \$4.8 billion of debt related to the TBS Transaction and the CVI Acquisition, offset in part by the use of approximately \$1.55 billion of net proceeds from the issuance of the Series M Preferred Stock for debt reduction. The increase in shareholders' equity principally reflects the issuance in 1996 of approximately 173.4 million shares of common stock in connection with the TBS Transaction and approximately 2.9 million shares of common stock and 6.3 million shares of preferred stock in connection with the CVI Acquisition. The effect from such issuances was offset in part by an increase in dividend requirements and the repurchase of approximately 11.4 million shares of Time Warner common stock at an aggregate cost of \$456 million.

**Investment in TWE** Time Warner's investment in TWE at December 31, 1996 consisted of interests in 74.49% of the Series A Capital and Residual Capital of TWE, and 100% of the Senior Capital and Series B Capital of TWE. The priority capital interests provide Time Warner (and with respect to the Series A Capital only, U S WEST) with certain priority claims to the net partnership income of TWE and distributions of TWE partnership capital, including certain priority distributions of partnership capital in the event of liquidation or dissolution of TWE. Each level of priority capital interest provides for an annual rate of return equal to or exceeding 8%, including an above-market 13.25% annual rate of return (11.25% to the extent concurrently distributed) related to Time Warner's Series B Capital interest, which, when taken together with Time Warner's contributed capital, represented a cumulative priority Series B Capital interest of \$5.2 billion at December 31, 1996. While the TWE partnership agreement contemplates the reinvestment of significant partnership cash flows in the form of capital expenditures and otherwise provides for certain other restrictions that are expected to limit cash distributions on partnership interests for the foreseeable future, Time Warner's \$1.5 billion Senior Capital interest and, to the extent not previously distributed, partnership income allocated thereto (based on an 8% annual rate of return) is required to be distributed to Time Warner in three annual installments beginning on July 1, 1997. Time Warner expects that the initial distribution of Senior Capital will be approximately \$535 million.

**Series M Exchangeable Preferred Stock** In April 1996, Time Warner raised approximately \$1.55 billion of net proceeds for debt reduction in a private placement of 1.6 million shares of exchangeable preferred stock, which pay cumulative dividends at the rate of 10 1/4% per annum. This issuance allowed the Company to realize cash proceeds through a security whose payment terms are principally linked (until a reorganization of TWE occurs, if any) to a portion of Time Warner's currently non-cash-generating interest in the Series B Capital of TWE, as more fully described herein. Time Warner used these proceeds to redeem \$250 million principal amount of 8.75% Debentures due April 1, 2017 for approximately \$265 million (including redemption premiums and accrued interest thereon), and to reduce bank debt of TWI Cable Inc. ("TWI Cable"), its wholly owned subsidiary, by approximately \$1.3 billion. As part of the TBS Transaction, these preferred shares were converted into registered shares of Series M exchangeable preferred stock with substantially identical terms ("Series M Preferred Stock").

Generally, the terms of the Series M Preferred Stock only require Time Warner to pay cash dividends or to redeem, prior to its mandatory redemption date, any portion of the security for cash upon the receipt of certain cash distributions from TWE with respect to Time Warner's interests in the Series B Capital and Residual Capital of TWE (excluding stock option related distributions and certain tax related distributions). However, because such cash distributions are subject to restrictions under the TWE partnership agreement, Time Warner does not expect to pay cash dividends or to redeem any portion of the Series M Preferred Stock for cash in the foreseeable future. Instead, Time Warner expects to satisfy its dividend requirements through the issuance of additional shares of Series M Preferred Stock with an aggregate liquidation preference equal to the amount of such dividends. In addition, upon a reorganization of TWE, Time Warner must elect either to redeem each outstanding share of Series M Preferred Stock for cash, subject to certain conditions, or to exchange the Series M Preferred Stock for new Series L Preferred Stock, which also pays cumulative dividends at the rate of 10 1/4% per annum but is not linked to Time Warner's interest in the Series B Capital of TWE. The terms of the Series L Preferred Stock do not require Time Warner to pay cash dividends until July 2006 and provide Time Warner with an option to exchange the Series L Preferred Stock, subject to certain conditions, into 10 1/4% Senior Subordinated Debentures which do not require the payment of cash interest until July 2006. See Note 10 to the accompanying consolidated financial statements for a summary of the principal terms of the Series M Preferred Stock.

**Common Stock Repurchase Program** In April 1996, Time Warner's Board of Directors authorized a program to repurchase, from time to time, up to 15 million shares of Time Warner common stock. In connection therewith, Time Warner entered into a five-year, \$750 million revolving credit facility (the "Stock Option Proceeds Credit Facility") in May 1996. Borrowings under the Stock Option Proceeds Credit Facility are principally used to fund stock repurchases and approximately \$200 million of preferred dividend requirements on Time Warner's Series G, H, I and J Preferred Stock. The common stock repurchased under the program is expected to be used to satisfy future share issuances related to the exercise of existing employee stock options. Actual repurchases in any period will be subject to market conditions. As of December 31, 1996, Time Warner had acquired approximately 11.4 million shares of its common stock for an aggregate cost of \$456 million. Such repurchases were principally funded with borrowings under the Stock Option Proceeds Credit Facility.

The Stock Option Proceeds Credit Facility initially provided for borrowings of up to \$750 million, of which up to \$100 million is reserved solely for the payment of interest and fees thereunder. At December 31, 1996, \$488 million had been borrowed under the Stock Option Proceeds Credit Facility. Borrowings under the Stock Option Proceeds Credit Facility generally bear interest at LIBOR plus a margin equal to 75 basis points and are principally expected to be repaid from the cash proceeds received from the exercise of designated employee stock options. The receipt of such stock option proceeds permanently reduces the borrowing availability under the facility, which has been reduced to approximately \$715 million as of December 31, 1996. At December 31, 1996, based on a closing market price of Time Warner common stock of \$37.50, the aggregate value of potential proceeds to Time Warner from the exercise of outstanding vested, "in the money" stock options covered under the facility was approximately \$1.5 billion, representing a 2.1 to 1 coverage ratio over the related borrowing availability.

To the extent that stock option proceeds are not sufficient to satisfy Time Warner's obligations under the Stock Option Proceeds Credit Facility, Time Warner is generally required to repay such borrowings using proceeds from the sale of shares

of its common stock held in escrow under the Stock Option Proceeds Credit Facility or, at Time Warner's election, using available cash on hand. In addition, as a result of Time Warner's commitment to use the Stock Option Proceeds Credit Facility to fund approximately \$200 million of preferred dividend requirements on its Series G, H, I and J Preferred Stock, Time Warner has also supplementally agreed to place in escrow an amount of cash equal to the excess of the unpaid preferred dividend requirements on such series of convertible preferred stock over the borrowing availability under the facility at any time. At December 31, 1996, Time Warner had placed \$52 million of cash and 36 million shares in escrow under these arrangements, which shares are not considered to be issued and outstanding capital stock of the Company. Time Warner may be required, from time to time, to have up to 52.5 million shares held in escrow.

Because borrowings under the Stock Option Proceeds Credit Facility are expected to be principally repaid by Time Warner from the cash proceeds related to the exercise of employee stock options, Time Warner's principal credit rating agencies have concluded that such borrowings and related financing costs are credit neutral and are excludable from debt and interest expense, respectively, for their purposes in evaluating Time Warner's leverage and coverage ratios. In addition, because Time Warner has committed to use the Stock Option Proceeds Credit Facility to fund approximately \$200 million of preferred dividend requirements on its Series G, H, I and J Preferred Stock, and has entered into the escrow arrangements described above, such preferred dividend requirements are similarly excluded from preferred dividends for purposes of evaluating Time Warner's coverage ratio.

**Debt Refinancings** In 1996 and early 1997, Time Warner continued to capitalize on favorable market conditions through certain debt refinancings, which lowered interest rates, staggered debt maturities and, with respect to the redemption of the 8.75% Convertible Debentures in February 1996 and the TBS Convertible Notes in February 1997, eliminated the potential dilution from the conversion of such securities into 31.3 million shares of common stock.

In January 1996, in connection with the CVI Acquisition, subsidiaries of Time Warner assumed \$500 million of public notes and debentures of CVI and borrowed \$1.5 billion under the 1995 Credit Agreement to refinance a like amount of other indebtedness assumed or incurred in such acquisition.

In February 1996, Time Warner redeemed the remaining \$1.2 billion principal amount of 8.75% Convertible Debentures for \$1.28 billion, including redemption premiums and accrued interest thereon. The redemption was financed with (1) proceeds raised from a \$575 million issuance in December 1995 of Company-obligated mandatorily redeemable preferred securities of a subsidiary and (2) \$750 million of proceeds raised from the issuance in January 1996 of (i) \$400 million principal amount of 6.85% debentures due 2026, which are redeemable at the option of the holders thereof in 2003, (ii) \$200 million principal amount of 8.3% discount debentures due 2036, which do not pay cash interest until 2016, (iii) \$166 million principal amount of 7.48% debentures due 2008 and (iv) \$150 million principal amount of 8.05% debentures due 2016.

During the first quarter of 1997, Time Warner entered into a number of financing transactions, which resulted in the refinancing of approximately \$600 million of debt. Time Warner redeemed \$300 million principal amount of 10.75% Senior Notes due January 30, 2002 of TWI Cable and approximately \$283 million accreted amount of TBS Convertible Notes at an aggregate redemption price of approximately \$600 million, including redemption premiums and accrued interest thereon. Time Warner also issued \$600 million principal amount of Floating Rate Reset Notes due December 30, 2031 (the "Floating Rate Reset Notes"). The Floating Rate Reset Notes bear interest at a floating rate equal to LIBOR less 25 basis points until December 30, 2001, at which time the interest rate will be reset at a fixed rate equal to 6.59% plus a margin based upon Time Warner's credit risk at such time. The Floating Rate Reset Notes are redeemable at the election of the holders, in whole but not in part, on December 30, 2001.

**Debt Reduction Program.** As part of a continuing strategy to enhance the financial position and credit statistics of Time Warner and the Entertainment Group, a \$2.3 billion debt reduction program was initiated in 1995. Including the sale of 51% of TWE's interest in Six Flags in June 1995, the sale of an interest in QVC, Inc. in February 1995, the sale of certain unclustered cable systems, the proceeds raised from the monetization of Time Warner's investment in Hasbro in August 1995 (through the issuance of mandatorily redeemable preferred securities of a subsidiary) and a portion of its interest in TWE in April 1996 (through the issuance of Series M Preferred Stock) and the expected 1997 sale of TWE's interest in E! Entertainment Television, Inc., Time Warner and the Entertainment Group on a combined basis have exceeded their initial goals under this program.

**Credit Statistics.** The combination of asset sales and debt refinancings is intended to strengthen the financial position of Time Warner and the Entertainment Group and, when taken together with EBITDA growth, is expected to continue the improvement of Time Warner's overall credit statistics. Those credit statistics consist of commonly used liquidity measures such as leverage and coverage ratios. The leverage ratio represents the ratio of total debt, less available cash and equivalents ("Net debt") to total business segment EBITDA, less corporate expenses ("Adjusted EBITDA"). The coverage ratio represents the ratio of Adjusted EBITDA to total interest expense, and/or preferred dividends. Those ratios, on a pro forma basis for 1996 and 1995, and on a historical basis for 1994, are as set forth below for each of Time Warner and Time Warner and the Entertainment Group combined. Certain rating agencies and other credit analysts place more emphasis on the combined ratios while others place more emphasis on the Time Warner stand alone ratios. It should be understood, however, that the assets of the Entertainment Group are not freely available to fund the cash needs of Time Warner.

	Pro Forma <sup>(a)</sup>		Historical 1994
	1996	1995	
<b>Time Warner and</b>			
<b>Entertainment Group combined</b>			
Net debt/Adjusted EBITDA	4.1x	4.3x	5.3x
Adjusted EBITDA/Interest <sup>(b)</sup>	2.9x	2.5x	2.1x
Adjusted EBITDA/Interest and preferred dividends <sup>(c)</sup>	2.3x	2.0x	2.1x
<b>Time Warner</b>			
Net debt/Adjusted EBITDA	5.9x	5.7x	8.3x
Adjusted EBITDA/Interest <sup>(b)</sup>	2.0x	1.9x	1.4x
Adjusted EBITDA/Interest and preferred dividends <sup>(c)</sup>	1.5x	1.4x	1.4x

(a) Pro forma ratios for 1996 and 1995 give effect to the Time Warner Transactions as if each of such transactions occurred at the beginning of 1995. Historical ratios for 1996 and 1995 are not meaningful and have not been presented because they reflect the operating results of acquired or disposed entities for only a portion of the year in comparison to year end Net debt levels.

(b) Excludes interest of \$26 million in 1996, \$28 million in 1995 and \$12 million in 1994 which was paid to TWE in connection with borrowings under Time Warner's \$400 million credit agreement with TWE, and, in 1996 only, excludes interest of \$13 million on borrowings under the Stock Option Proceeds Credit Facility.

(c) Includes preferred dividends related to Company obligated mandatorily redeemable preferred securities of subsidiaries. Excludes preferred dividends of \$17 million in 1996 related to Time Warner's Series G, H, I and J Preferred Stock, which Time Warner has funded with borrowings under the Stock Option Proceeds Credit Facility.

**Cash Flows.** During 1996, Time Warner's cash provided by operations amounted to \$253 million and reflected \$1.954 billion of EBITDA from its Publishing, Music, Cable Networks-TBS, Filmed Entertainment-TBS and Cable businesses, \$228 million of distributions from TWE and \$147 million from the securitization of receivables, less \$839 million of interest payments, \$338 million of income taxes, \$78 million of corporate expenses and \$821 million related to an increase in other working capital requirements, balance sheet accounts and noncash items. Cash provided by operations of \$1.051 billion in 1995 reflected \$1.256 billion of EBITDA from the Publishing, Music and Cable businesses, \$1.063 billion of net distributions from TWE and

\$35 million from the securitization of receivables, less \$659 million of interest payments, \$278 million of income taxes, \$74 million of corporate expenses and \$292 million related to an increase in other working capital requirements, balance sheet accounts and noncash items.

Cash used by investing activities increased to \$424 million in 1996, compared to \$271 million in 1995, principally as a result of a decrease in investment proceeds realized in connection with management's debt reduction program and higher capital expenditures, offset in part by lower investment spending. Capital expenditures increased to \$481 million in 1996, compared to \$266 million in 1995, principally as a result of higher cable capital spending associated with Time Warner's cable acquisitions.

Cash used by financing activities was \$500 million in 1996, compared to cash provided by financing activities of \$123 million in 1995. The use of cash in 1996 principally resulted from higher cash dividend requirements and the use of \$557 million of noncurrent cash and equivalents raised in the December 1995 issuance of the Preferred Trust Securities to redeem the remaining portion of the B 7.5% Convertible Debentures in February 1996, offset in part by borrowings incurred to finance the cash portion of the consideration paid to acquire CVI. Cash dividends paid increased to \$287 million in 1996, compared to \$171 million in 1995, principally as a result of dividends paid on the preferred stock issued in connection with the Cable Acquisitions and the ITOCHU/Toshiba Transaction. In addition, Time Warner raised approximately \$1.55 billion of net proceeds in 1996 from the issuance of 1.6 million shares of Series M Preferred Stock and used the net proceeds therefrom to reduce debt. Time Warner also borrowed \$488 million under its Stock Options Proceeds Credit Facility and used the proceeds therefrom to repurchase approximately 11.4 million shares of its common stock at an aggregate cost of \$456 million.

The assets and cash flows of certain consolidated and unconsolidated subsidiaries of Time Warner are restricted by certain borrowing and partnership agreements. The assets and cash flows of TBS, TWE and TWI Cable are restricted by their respective bank credit agreements, although each entity is

permitted to incur additional indebtedness to make loans, advances, distributions and other cash payments to Time Warner, subject to its individual compliance with the cash flow coverage and leverage ratio covenants contained therein. Further, under the TWE partnership agreement, the assets and cash flows of TWE are unavailable to Time Warner except through the payment of certain fees, reimbursements, cash distributions and loans, which are subject to limitations.

Management believes that Time Warner's operating cash flow, cash and marketable securities and additional borrowing capacity are sufficient to fund its capital and liquidity needs for the foreseeable future without distributions and loans from its restricted subsidiaries, including TWE, above those permitted by existing agreements.

#### ENTERTAINMENT GROUP

**1996 Financial Condition** At December 31, 1996, the Entertainment Group had \$5.7 billion of debt, \$1.5 billion of Time Warner General Partners' Senior Capital and \$6.7 billion of partners' capital, compared to \$6.2 billion of debt, \$1.4 billion of Time Warner General Partners' Senior Capital and \$6.8 billion of partners' capital (net of the \$189 million uncollected portion of the note receivable from U S WEST) at December 31, 1995. Cash and equivalents were \$218 million at December 31, 1996, compared to \$209 million at December 31, 1995, reducing the debt-net-of-cash amounts for the Entertainment Group to \$5.5 billion and \$6 billion, respectively.

**Credit Statistics** Entertainment Group leverage and coverage ratios for 1996, 1995 and 1994 were as follows:

	Historical 1996	Pro Forma 1995 <sup>(a)</sup>	Historical 1994
Net debt/Adjusted EBITDA	2.4x	2.9x	3.5x
Adjusted EBITDA/Interest	4.8x	3.8x	3.1x

(a) Pro forma ratios for 1995 give effect to the Entertainment Group transactions as if each of such transactions had occurred at the beginning of 1995. Historical ratios for 1995 are not meaningful and have not been presented because they reflect the operating results of acquired or disposed entities for only a portion of the year in comparison to year-end net debt levels.

**Cash Flows** In 1996, the Entertainment Group's cash provided by operations amounted to \$1.912 billion and reflected \$2.334 billion of EBITDA from the Filmed Entertainment, Warner Bros., Broadcasting-The WB Network, Cable Networks, HBO and Cable businesses and \$234 million related to a reduction in working capital requirements, other balance sheet accounts and noncash items, less \$513 million of interest payments, \$74 million of income taxes and \$69 million of corporate expenses. Cash provided by operations of \$1.495 billion in 1995 reflected \$2.052 billion of business segment EBITDA and \$159 million related to a reduction in working capital requirements, other balance sheet accounts and noncash items, less \$577 million of interest payments, \$75 million of income taxes and \$64 million of corporate expenses.

Cash used by investing activities was \$1.253 billion in 1996, compared to \$750 million in 1995, principally as a result of a \$508 million decrease in investment proceeds realized in 1995 in connection with management's debt reduction program and higher capital expenditures. Capital expenditures increased to \$1.719 billion in 1996, compared to \$1.651 billion in 1995, principally as a result of higher capital spending by the Cable Division.

Cash used by financing activities was \$652 million in 1996, compared to \$1.607 billion in 1995, principally as a result of a lower level of debt reduction realized in 1996 in connection with management's debt reduction program and an \$835 million decrease in net distributions paid to Time Warner, offset in part by a \$433 million decrease in collections on the note receivable from U S WEST.

Management believes that TWE's operating cash flow, cash and equivalents and additional borrowing capacity are sufficient to fund its capital and liquidity needs for the foreseeable future.

#### CABLE CAPITAL SPENDING

Since the beginning of 1994, Time Warner Cable has been engaged in a plan to upgrade the technological capability and reliability of its cable television systems and develop new services, which it believes will position the business for sustained, long-term growth. Capital spending by Time Warner Cable, including the cable operations of both Time Warner and



TWE, amounted to \$1.563 billion in 1996, compared to \$1.349 billion in 1995, and was financed in part through collections on the note receivable from U S WEST of \$169 million in 1996 and \$602 million in 1995. Cable capital spending for 1997 is budgeted to be steady at approximately \$1.6 billion and is expected to be funded principally by cable operating cash flow in exchange for certain flexibility in establishing cable rate pricing structures for regulated services that went into effect on January 1, 1996 and consistent with Time Warner Cable's long-term strategic plan. Time Warner Cable has agreed with the FCC to invest a total of \$4 billion in capital costs in connection with the upgrade of its cable infrastructure, which is expected to be substantially completed over a five-year period ending December 31, 2000. The agreement with the FCC covers all of the cable operations of Time Warner Cable, including the owned or managed cable television systems of Time Warner, TWE and the TWE-Advance/Newhouse Partnership. Management expects to continue to finance such level of investment principally through the growth in cable operating cash flow derived from increases in subscribers and cable rates, bank credit agreement borrowings and the development of new revenue streams from expanded programming options, high speed data transmission and other services.

#### **OFF-BALANCE SHEET ASSETS**

As discussed below, Time Warner believes that the value of certain off-balance sheet assets should be considered, along with other factors discussed elsewhere herein, in evaluating the Company's financial condition and prospects for future results of operations, including its ability to fund its capital and liquidity needs.

**Intangible Assets** As a creator and distributor of branded information and entertainment copyrights, Time Warner and the Entertainment Group have a significant amount of internally-generated intangible assets whose value is not fully reflected in

their respective consolidated balance sheets. Such intangible assets extend across Time Warner's principal business interests, but are best exemplified by Time Warner's collection of copyrighted music product, its libraries of copyrighted film and television product and the creation or extension of brands. Generally accepted accounting principles do not recognize the value of such assets, except at the time they may be acquired in a business combination accounted for by the purchase method of accounting.

Because Time Warner owns the copyrights to such creative material, it continually generates revenue through the sale of such products across different media and in new and existing markets. The value of film and television-related copyrighted product and trademarks is continually realized by the licensing of films and television series to secondary markets and the licensing of trademarks, such as the *Looney Tunes* characters and *Batman*, to the retail industry and other markets. In addition, technological advances, such as the introduction of the compact disc and home videocassette in the 1980's and potentially the digital video disc in the future, have historically generated significant revenue opportunities through the repackaging and sale of such copyrighted products in the new technological format. Accordingly, such intangible assets have significant off-balance sheet asset value that is not fully reflected in the consolidated balance sheets of Time Warner and the Entertainment Group.

**Filmed Entertainment Backlog** Backlog represents the amount of future revenue not yet recorded from cash contracts for the licensing of theatrical and television product for pay cable, basic cable, network and syndicated television exhibition. Backlog of Warner Bros. amounted to \$1.502 billion and \$1.056 billion at December 31, 1996 and 1995, respectively (including amounts relating to the licensing of film product to Time Warner's and TWE's cable television networks of \$463 million and \$175 million, respectively). Warner Bros.' backlog increased



principally as a result of the licensing of the hit television series *Friends* and *ER* for domestic syndication, as well as for exhibition on Time Warner's cable television networks beginning in 1998. Backlog of the recently-acquired film production companies of TBS amounted to approximately \$290 million at December 31, 1996 (including amounts relating to the licensing of film product to Time Warner's cable television networks of approximately \$90 million).

Because backlog generally relates to contracts for the licensing of theatrical and television product which have already been produced, the recognition of revenue for such completed product is principally only dependent upon the commencement of the availability period for telecast under the terms of the related licensing agreement. Cash licensing fees are collected periodically over the term of the related licensing agreements. Accordingly, the portion of backlog for which cash advances have not already been received has significant off-balance sheet asset value as a source of future funding. The backlog excludes advertising barter contracts, which are also expected to result in the future realization of revenues and cash through the sale of advertising spots received under such contracts.

#### INTEREST RATE AND FOREIGN CURRENCY RISK MANAGEMENT

**Interest Rate Swap Contracts.** Time Warner uses interest rate swap contracts to adjust the proportion of total debt that is subject to variable and fixed interest rates. At December 31, 1996, Time Warner had interest rate swap contracts to pay floating rates of interest (average six-month LIBOR rate of 5.7%) and receive fixed rates of interest (average rate of 5.5%) on \$2.3 billion notional amount of indebtedness, which resulted in approximately 47% of Time Warner's underlying debt and 43% of the debt of Time Warner and the Entertainment Group combined, being subject to variable interest rates. At December 31, 1995, Time Warner had interest rate swap contracts on \$2.6 billion notional amount of indebtedness.

**Foreign Exchange Contracts.** Time Warner uses foreign exchange contracts primarily to hedge the risk that unremitted or future royalties and license fees owed to Time Warner or TWE 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. As part of its overall strategy to manage the level of exposure to the risk of foreign currency exchange rate fluctuations, Time Warner hedges a portion of its and TWE's combined foreign currency exposures anticipated over the ensuing twelve month period. At December 31, 1996, Time Warner had effectively hedged approximately half of the combined estimated foreign currency exposures that principally relate to anticipated cash flows to be remitted to the U.S. over the ensuing twelve month period, using foreign exchange contracts that generally have maturities of three months or less, which are generally issued over to provide continuing coverage throughout the year. Time Warner often closes foreign exchange sale contracts by purchasing an offsetting purchase contract. At December 31, 1996, Time Warner had contracts for the sale of \$447 million and the purchase of \$104 million of foreign currencies at fixed rates, compared to contracts for the sale of \$504 million and the purchase of \$140 million of foreign currencies at December 31, 1995.

See Note 14 to the accompanying consolidated financial statements for a more comprehensive description of Time Warner's interest rate and foreign currency risk management activities.

## Consolidated Balance Sheet

December 31 (millions, except per share amounts)

1994

1995

### ASSETS

#### Current assets

Cash and equivalents	\$ 452	\$ 628
Receivables, less allowances of \$976 and \$786 million	2,421	1,755
Inventories	941	443
Prepaid expenses	1,007	894
<b>Total current assets</b>	<b>4,821</b>	<b>3,720</b>

Noncurrent cash and equivalents	62	557
Noncurrent inventories	1,698	-
Investments in and amounts due to and from Entertainment Group	5,814	5,734
Other investments	1,919	2,389
Property, plant and equipment, net	1,986	1,119
Music catalogues, contracts and copyrights	1,035	1,140
Cable television and sports franchises	4,203	1,696
Goodwill	12,421	5,213
Other assets	1,105	584
<b>Total assets</b>	<b>\$ 35,064</b>	<b>\$ 22,132</b>

	1996	1995
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities</b>		
Accounts payable .....	\$ 715	\$ 672
Participations, royalties and programming costs payable .....	1,196	755
Debt due within one year .....	11	34
Other current liabilities .....	2,090	1,566
<b>Total current liabilities .....</b>	<b>4,012</b>	<b>3,027</b>
<b>Long-term debt .....</b>		
Borrowings against future stock option proceeds .....	488	-
Deferred income taxes .....	4,082	3,420
Unearned portion of paid subscriptions .....	679	654
Other liabilities .....	967	508
Company-obligated mandatorily redeemable preferred securities of subsidiaries holding solely subordinated notes and debentures of subsidiaries of the Company <sup>(a)</sup> .....	949	949
Series M exchangeable preferred stock, \$ .10 par value, 15.2 million shares authorized, 1.72 million shares outstanding and \$1.720 billion liquidation preference .....	1,672	-
<b>Shareholders' equity</b>		
Preferred stock, \$ .10 and \$1 par value, 250 million shares authorized, 35.6 million and 29.7 million shares outstanding, \$3.559 billion and \$2.994 billion liquidation preference .....	4	30
LMCN-V Class Common Stock, \$ .01 par value, 60 million shares authorized, 50.6 million shares outstanding .....	1	-
Common stock, \$ .01 and \$1 par value, 2 billion shares authorized, 508.4 million and 387.7 million shares outstanding .....	5	388
Paid-in capital .....	1,250	5,422
Accumulated deficit .....	(2,758)	(2,173)
<b>Total shareholders' equity .....</b>	<b>8,502</b>	<b>3,687</b>
<b>Total liabilities and shareholders' equity .....</b>	<b>\$ 35,064</b>	<b>\$ 22,132</b>

(a) Includes \$374 million of preferred securities that are redeemable for cash or, at Time Warner's option, approximately 18.1 million shares of Hushco, Inc. common stock owned by Time Warner (Note 9).

See accompanying notes.

## Consolidated Statement of Operations

Years Ended December 31, (millions, except per share amounts)	1996	1995	1994
Revenues <sup>(a)</sup>	\$ 10,084	\$ 8,067	\$ 7,396
Cost of revenues <sup>(a)(b)</sup>	5,922	4,682	4,307
Selling, general and administrative <sup>(a)(b)</sup>	3,176	2,680	2,378
Operating expenses	9,098	7,370	6,883
Business segment operating income	966	697	713
Equity in pretax income of Entertainment Group <sup>(a)</sup>	290	256	178
Interest and other, net <sup>(a)</sup>	(1,174)	(877)	(724)
Corporate expenses <sup>(a)</sup>	(780)	(74)	(78)
Income before income taxes	4	2	89
Income taxes	(160)	(126)	(180)
Loss before extraordinary item	(156)	(124)	(91)
Extraordinary loss on retirement of debt, net of \$22 million and \$26 million income tax benefit in 1996 and 1995, respectively	(35)	(42)	-
Net loss	(191)	(166)	(91)
Preferred dividend requirements	(257)	(52)	(13)
Net loss applicable to common shares	\$ (448)	\$ (218)	\$ (104)
Loss per common share:			
Loss before extraordinary item	\$ (95)	\$ (46)	\$ (27)
Net loss	\$ (104)	\$ (57)	\$ (27)
Average common shares	431.2	383.8	378.9

(a) Includes the following income (expenses) resulting from transactions with the Entertainment Group and other related companies for the years ended December 31, 1996, 1995 and 1994, respectively: revenues \$224 million, \$211 million and \$203 million, cost of revenues \$(177) million, \$(108) million and \$(109) million, selling, general and administrative \$34 million, \$46 million and \$47 million, equity in pretax income of Entertainment Group \$(29) million, \$(95) million and \$(120) million, interest and other, net \$(33) million, \$(27) million and \$13 million, and corporate expenses \$69 million, \$64 million and \$80 million (Note 17).

(b) Includes depreciation and amortization expense of

	\$ 988	\$ 558	\$ 437
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See accompanying notes

## Consolidated Statement of Cash Flows

Years Ended December 31, (in millions)	1998	1995	1994
<b>Operations</b>			
Net loss	\$ (191)	\$ (166)	\$ (91)
Adjustments for noncash and nonoperating items:			
Extraordinary loss on retirement of debt	35	42	-
Depreciation and amortization	988	559	437
Noncash interest expense	96	176	219
Excess (deficiency) of distributions over equity in pretax income of Entertainment Group	(62)	807	(56)
Equity in income of other investee companies, net of distributions	(53)	(16)	(17)
Changes in operating assets and liabilities:			
Receivables	(39)	(68)	(47)
Inventories	(180)	(52)	(38)
Accounts payable and other liabilities	(408)	160	324
Other balance sheet changes	67	(391)	(258)
Cash provided by operations	253	1,051	473
<b>Investing Activities</b>			
Investments and acquisitions	(261)	(381)	(187)
Capital expenditures	(481)	(266)	(164)
Investment proceeds	318	376	118
Cash used by investing activities	(424)	(271)	(233)
<b>Financing Activities</b>			
Borrowings	3,431	2,023	582
Debt repayments	(5,271)	(2,693)	(626)
Borrowings against future stock option proceeds	488	-	-
Repurchases of Time Warner common stock	(456)	-	-
Issuance of Series M Preferred Stock	1,550	-	-
Issuance of Company-obligated mandatorily redeemable preferred securities of subsidiaries	-	949	-
Dividends paid	(287)	(171)	(142)
Stock option and dividend reinvestment plans	105	106	34
Other, principally financing costs	(60)	(91)	(6)
Cash provided (used) by financing activities	(500)	123	(158)
Increase (Decrease) in Cash and Equivalents	(671)	903	82
Cash and Equivalents at Beginning of Period <sup>(a)</sup>	1,185	282	200
Cash and Equivalents at End of Period <sup>(a)</sup>	\$ 514	\$ 1,185	\$ 282

(a) Includes current and noncurrent cash and equivalents at December 31, 1998 and 1995.

See accompanying notes.

## Consolidated Statement of Shareholders' Equity

<i>(millions, except per share amounts)</i>	Preferred Stock	Common Stock <sup>(a)</sup>	Paid in Capital	Accumulated Deficit	Total
<b>BALANCE AT DECEMBER 31, 1993</b>	\$ 1	\$ 378	\$ 2,537	\$ (1,546)	\$ 1,370
Net loss				(91)	(91)
Dividends on common stock - \$ .35 per share				(133)	(133)
Dividends on Series B preferred stock - \$9.28 per share			4	(13)	(9)
Shares issued pursuant to stock option, dividend reinvestment and benefit plans (1 million shares)		1	53		54
Unrealized losses on certain marketable equity investments				(75)	(75)
Other			(6)	38	32
<b>BALANCE AT DECEMBER 31, 1994</b>	1	379	2,588	(1,820)	1,148
Net loss				(166)	(166)
Dividends on common stock - \$ .36 per share				(138)	(138)
Dividends on Series B preferred stock - \$6.40 per share			3	(8)	(5)
Dividends on Series C, D, G, H and I preferred stock - \$3.75 per share per year effective from the respective dates of issuance				(44)	(44)
Issuance of common and preferred stock in the KBL/COM and Summit acquisitions (14.3 million preferred shares and 2.6 million common shares)	14	3	1,367		1,384
Issuance of preferred stock in the ITOCHU/Toshiba Transaction (15 million shares)	15		1,335		1,350
Shares issued pursuant to stock option, dividend reinvestment and benefit plans (3.9 million shares)		4	122		126
Unrealized losses on certain marketable equity investments				(14)	(14)
Other (1.9 million shares issued)		2	7	17	26
<b>BALANCE AT DECEMBER 31, 1995</b>	30	388	5,472	(2,173)	3,667
Net loss				(191)	(191)
Dividends on common stock - \$ .38 per share				(155)	(155)
Dividends on Series B preferred stock - \$3.36 per share				(2)	(2)
Dividends on Series D, E, F, G, H, I and J preferred stock - \$3.75 per share				(133)	(133)
Dividends on Series M exchangeable preferred stock (120 thousand shares paid in-kind)				(122)	(122)
Issuance of common and preferred stock in the CVI acquisition (6.3 million preferred shares and 2.9 million common shares)	6	3	671		680
Reduction in par value of common stock and preferred stock in connection with the TBS Transaction	(32)	(382)	414		
Issuance of common stock in the TBS Transaction (173.4 million shares)		2	6,025		6,027
Repurchases of Time Warner common stock (11.4 million shares)		(11)	(404)		(456)
Shares issued pursuant to stock option, dividend reinvestment and benefit plans (4.6 million shares)		4	159	(8)	155
Unrealized gains on certain marketable equity investments				17	17
Other (1.8 million shares issued)		2	4	9	15
<b>BALANCE AT DECEMBER 31, 1996</b>	\$ 4	\$ 6	\$12,290	\$ (2,758)	\$ 9,502

(a) Includes 30.6 million shares of LMCH V Class Common Stock issued in 1996 in connection with the TBS Transaction (Note 2)

See accompanying notes

## Notes to Consolidated Financial Statements

### 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Description of Business** On October 10, 1996, Time Warner Inc. ("Time Warner" or the "Company"), acquired the remaining 80% interest in Turner Broadcasting System, Inc. ("TBS") that it did not already own, as more fully described herein (Note 2). As a result of this transaction, a new parent company with the name "Time Warner Inc." replaced the old parent company of the same name ("Old Time Warner", now known as Time Warner Companies, Inc.), and Old Time Warner and TBS became separate, wholly owned subsidiaries of the new parent company ("New Time Warner"). References herein to "Time Warner" or the "Company" refer to Old Time Warner prior to October 10, 1996 and New Time Warner thereafter.

Time Warner is the world's leading media and entertainment company whose principal business objective is to create and distribute branded information and entertainment copy rights throughout the world. Time Warner classifies its business interests into four fundamental areas: Entertainment, consisting principally of interests in recorded music and music publishing, filmed entertainment, television production, television broadcasting and theme parks; Cable Networks, consisting principally of interests in cable television programming and sports franchises; Publishing, consisting principally of interests in magazine publishing, book publishing and direct marketing; and Cable, consisting principally of interests in cable television systems. A majority of Time Warner's interests in filmed entertainment, television production, television broadcasting and theme parks, a portion of its interests in cable television programming and a majority of its cable television systems are held through Time Warner Entertainment Company, L.P. ("TWE"). Time Warner owns general and limited partnership interests in TWE consisting of 74.49% of the pro rata priority capital ("Series A Capital") and residual equity capital ("Residual Capital"), and 100% of the senior priority capital ("Senior Capital") and junior priority capital ("Series B Capital"). The remaining 25.51% limited partnership interests in the Series A Capital and Residual Capital of TWE are held by a subsidiary of U.S. WEST, Inc. ("U.S. WEST"). Time Warner does not consolidate TWE and certain related companies (the "Entertainment Group") for financial reporting purposes because of certain limited partnership approval rights related to TWE's interest in certain cable television systems.

Each of the business interests within Entertainment, Cable Networks, Publishing and Cable is important to management's objective of increasing shareholder value through the creation, extension and distribution of recognizable brands and copy rights throughout the world. Such brands and copyrights include (1) copyrighted music from many of the world's leading recording artists that is produced and distributed by a family of established record labels such as Warner Bros. Records, the Atlantic and Elektra Entertainment Groups and Warner Music International; (2) the unique and extensive film, television and animation libraries of Warner Bros. and TBS, and trademarks such as the Looney Tunes characters, Batman and The Flintstones; (3) The WB Network, a national broadcasting network launched in 1995 as an extension of the Warner Bros. brand and is an additional distribution outlet for the Company's collection of children's cartoons and television programming; (4) Six Flags, the largest regional theme park operator in the United States, in which TWE owns a 49% interest; (5) leading cable television networks, such as HBO, Cinemax, CNN, TNT and the TBS Superstation; (6) sports franchises consisting of the Atlanta Braves and Atlanta Hawks; (7) magazine franchises such as Time, People and Sports Illustrated and direct marketing brands such as Time Live Inc. and Book-of-the-Month Club and (8) Time Warner Cable, the second largest operator of cable television systems in the U.S.

The operating results of Time Warner's various business interests are presented herein as an indication of financial performance (Note 15). Except for start-up losses incurred in connection with The WB Network, Time Warner's principal business interests generate significant operating income and cash flow from operations. The cash flow from operations generated by such business interests is considerably greater than their operating income due to significant amounts of noncash amortization of intangible assets recognized in various acquisitions accounted for by the purchase method of accounting. Noncash amortization of intangible assets recorded by Time Warner's business interests, including the unconsolidated business interests of the Entertainment Group amounted to \$1.117 billion in 1996, \$822 million in 1995 and \$782 million in 1994.



**Basis of Presentation** The consolidated financial statements of Time Warner reflect the acquisitions of Summit Communications Group, Inc. ("Summit") effective as of May 2, 1995, KBLCOM Incorporated ("KBLCOM") effective as of July 6, 1995, Cablevision Industries Corporation and related companies ("CVI") effective as of January 4, 1996 (collectively, the "Cable Acquisitions") and TBS effective as of October 10, 1996. Certain reclassifications have been made to the prior years' financial statements to conform to the 1996 presentation.

**Basis of Consolidation and Accounting for Investments** The consolidated financial statements include 100% of the assets, liabilities, revenues, expenses, income, loss and cash flows of Time Warner and all companies in which Time Warner has a controlling voting interest ("subsidiaries"), as if Time Warner and its subsidiaries were a single company. Significant inter-company accounts and transactions between the consolidated companies have been eliminated. Significant accounts and transactions between Time Warner and the Entertainment Group are disclosed as related party transactions (Note 17).

The Entertainment Group and investments in certain other companies in which Time Warner has significant influence but less than a controlling voting interest, are accounted for using the equity method. Under the equity method, only Time Warner's investment in and amounts due to and from the equity investee are included in the consolidated balance sheet, only Time Warner's share of the investee's earnings is included in the consolidated operating results, and only the dividends, cash distributions, loans or other cash received from the investee, less any additional cash investments, loan repayments or other cash paid to the investee are included in the consolidated cash flows.

Investments in companies in which Time Warner does not have the controlling interest or an ownership and voting interest so large as to exert significant influence are accounted for at market value if the investments are publicly traded and there are no resale restrictions, or at cost, if the sale of a publicly traded investment is restricted or if the investment is not publicly traded. Unrealized gains and losses on investments accounted for at market value are reported net-of-tax in accumulated deficit until the investment is sold, at which time the realized

gain or loss is included in income. Dividends and other distributions of earnings from both market value and cost method investments are included in income when declared.

The effect of any changes in Time Warner's ownership interests resulting from the issuance of equity capital by consolidated subsidiaries or equity investees to unaffiliated parties is included in income.

**Foreign Currency** The financial position and operating results of substantially all foreign operations are consolidated 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, which have not been material, are included in accumulated deficit. Foreign currency transaction gains and losses, which have not been material, are included in operating results.

**Use of Estimates** The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and footnotes thereto. Actual results could differ from those estimates.

Significant estimates inherent in the preparation of the accompanying consolidated financial statements include management's forecast of anticipated revenues from the sale of future and existing music and publishing-related products, as well as from the distribution of theatrical and television product, in order to evaluate the ultimate recoverability of accounts receivables, film inventory and artist and author advances recorded as assets in the consolidated balance sheet. Accounts receivables and sales in the music and publishing industries, as well as sales of home video product in the filmed entertainment industry, are subject to customers' rights to return unsold items. Management periodically reviews such estimates and it is reasonably possible that management's assessment of recoverability of accounts receivables, individual films and television product and individual artist and author advances may change based on actual results and other factors.

**Revenues and Costs** The unearned portion of paid subscriptions is deferred until magazines are delivered to subscribers. Upon each delivery, a proportionate share of the gross subscription price is included in revenues.

Inventories of magazines, books, cassettes and compact discs are stated at the lower of cost or estimated realizable value. Cost is determined using first-in, first-out, last-in, first-out, and average cost methods. In accordance with industry practice, certain products (such as magazines, books, home videocassettes, compact discs and cassettes) are sold to customers with the right to return unsold items. Revenues from such sales represent gross sales less a provision for future returns. Returned goods included in inventory are valued at estimated realizable value but not in excess of cost.

Feature films are produced or acquired for initial exhibition in theaters followed by distribution in the home video, pay cable, basic cable, broadcast network and syndicated television markets. Generally, distribution to the theatrical, home video and pay cable markets (the primary markets) is principally completed within eighteen months of initial release and thereafter with respect to distribution to the basic cable, broadcast network and syndicated television markets (the secondary markets). Theatrical revenues are recognized as the films are exhibited. Home video revenues, less a provision for returns, are recognized when the home videos are sold. Revenues from the distribution of theatrical product to cable, broadcast network and syndicated television markets are recognized when the films are available to telecast.

Television films and series are initially produced for the networks or first-run television syndication (the primary markets) and may be subsequently licensed to foreign or domestic cable and syndicated television markets (the secondary markets). Revenues from the distribution of television product are recognized when the films or series are available to telecast, except for barter agreements where the recognition of revenue is deferred until the related advertisements are exhibited.

License agreements for the telecast of theatrical and television product in the cable, broadcast network and syndicated television markets are routinely entered into well in advance of

their available date for telecast, which is generally determined by the telecast privileges granted under previous license agreements. Accordingly, there are significant contractual rights to receive cash and barter upon which revenues will not be recognized until such product is available for telecast under the contractual terms of the related license agreement. Such contractual rights for which revenue is not yet recognizable is referred to as "backlog." Excluding advertising barter contracts, backlog of the recently acquired film production companies of TBS amounted to approximately \$290 million at December 31, 1996 (including amounts relating to the licensing of film product to Time Warner's cable television networks of approximately \$90 million).

Inventories of theatrical and television product are stated at the lower of amortized cost or net realizable value. Cost includes direct production and acquisition costs, production overhead and capitalized interest. A portion of the cost to acquire TBS in 1996 was allocated to its theatrical and television product, including an allocation to purchased program rights (such as the film and animation libraries of Hanna-Barbera Inc. and Turner Entertainment Co., the latter of which includes the former film and television libraries of Metro-Goldwyn-Mayer, Inc. and RKO Pictures, Inc.) and product that had been exhibited at least once in all markets ("Library"). The Library is amortized on a straight-line basis over twenty years. Individual films and series are amortized, and the related participations and residuals are accrued, based on the proportion that current revenues from the film or series bear to an estimate of total revenues anticipated from all markets. These estimates are revised periodically and losses, if any, are provided in full. Current film inventories include the unamortized cost of completed feature films allocated to the primary markets, television films and series in production pursuant to a contract of sale, film rights acquired for the home video market and advances pursuant to agreements to distribute third-party films in the primary markets. Noncurrent film inventories include the unamortized cost of completed theatrical and television films allocated to the secondary markets, theatrical films in production and the Library.

A significant portion of cable system and cable programming revenues are derived from subscriber fees and advertising. Subscriber fees are recorded as revenue in the period the service is provided and advertising revenues are recognized in the period that the advertisements are exhibited. The cost of rights to exhibit feature films and other programming on the cable networks during one or more availability periods ("programming costs") generally is recorded when the programming is initially available for exhibition, and is allocated to the appropriate availability periods and amortized as the programming is exhibited.

**Advertising** In accordance with Financial Accounting Standards Board ("FASB") Statement No. 53, "Financial Reporting by Producers and Distributors of Motion Picture Films," advertising costs for theatrical and television product are capitalized and amortized over the related revenue streams in each market for which such costs are intended to benefit, which generally does not exceed three months. Other advertising costs are expensed upon the first exhibition of the advertisement, except for certain direct-response advertising, for which the costs are capitalized and amortized over the expected period of future benefits. Direct-response advertising principally consists of product promotional mailings, broadcast advertising, catalogs and other promotional costs incurred in the Company's direct-marketing businesses. Deferred advertising costs are generally amortized over periods of up to three years subsequent to the promotional event using straight-line or accelerated methods, with a significant portion of such costs amortized in twelve months or less. Deferred advertising costs for Time Warner amounted to \$217 million and \$195 million at December 31, 1996 and 1995, respectively. Advertising expense, excluding theatrical and television product, amounted to \$1.050 billion in 1996, \$1.045 billion in 1995 and \$931 million in 1994.

**Cash and Equivalents** Cash equivalents consist of commercial paper and other investments that are readily convertible into cash, and have original maturities of three months or less. Noncurrent cash and equivalents at December 31, 1996 consist of amounts held in escrow for purposes of funding certain preferred dividend requirements (Note 7). Noncurrent cash and equivalents at December 31, 1995 consist of net proceeds received from the issuance of Preferred Trust Securities in December 1995, which were segregated for the redemption of the 8.75% Convertible Debentures in February 1998 (Notes 6 and 9).

**Property, Plant and Equipment** Property, plant and equipment are stated at cost. Additions to cable property, plant and equipment generally include material, labor, overhead and interest. Depreciation is provided generally on the straight-line method over useful lives ranging up to thirty years for buildings and improvements and up to fifteen years for furniture, fixtures, cable television equipment and other equipment. Property, plant and equipment consists of:

December 31, (millions)	1996	1995
Land and buildings	\$ 914	\$ 431
Cable television equipment	777	361
Furniture, fixtures and other equipment	1,337	1,196
	3,028	1,988
Less accumulated depreciation	(1,042)	(869)
Total	\$ 1,986	\$ 1,119

Effective January 1, 1996, Time Warner adopted FASB Statement No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of" ("FAS 121"), which established standards for the recognition and measurement of impairment losses on long-lived assets and certain intangible assets. The adoption of FAS 121 did not have a material effect on Time Warner's financial statements.

**Intangible Assets** As a creator and distributor of branded information and entertainment copyrights, Time Warner has a significant and growing amount of intangible assets, including goodwill, cable television and sports franchises, music catalogues, contracts and copyrights, and other copyrighted products and trademarks. In accordance with generally accepted accounting principles, Time Warner does not recognize the fair value of internally-generated intangible assets. Costs incurred to create and produce copyrighted product, such as feature films, television series and compact discs, are generally either expensed as incurred, or capitalized as tangible assets as in the case of cash advances and inventoriable product costs. However, accounting recognition is not given to any increasing asset value that may be associated with the collection of the underlying copyrighted material. Additionally, costs incurred to create or extend brands, such as magazine titles and new cable networks, generally result in losses over an extended development period and are recognized as a reduction of income as incurred, while any corresponding brand value created is not

recognized as an intangible asset in the consolidated balance sheet. On the other hand, intangible assets acquired in business combinations accounted for by the purchase method of accounting are capitalized and amortized over their expected useful life as a noncash charge against future results of operations. Accordingly, the intangible assets reported in the consolidated balance sheet do not reflect the fair value of Time Warner's internally-generated intangible assets, but rather are limited to intangible assets resulting from certain acquisitions in which the cost of the acquired companies exceeded the fair value of their tangible assets at the time of acquisition.

Time Warner amortizes goodwill and sports franchises over periods up to forty years using the straight-line method. Cable television franchises, music catalogues, contracts and copyrights, and other intangible assets are amortized over periods up to twenty years using the straight-line method. In 1996, 1995 and 1994, amortization of goodwill amounted to \$250 million, \$175 million and \$158 million, respectively; amortization of music copyrights, artists' contracts and record catalogues amounted to \$132 million, \$118 million and \$115 million, respectively; amortization of cable television and sports franchises amounted to \$212 million in 1996 and \$42 million in 1995 and amortization of other intangible assets amounted to \$87 million, \$43 million and \$31 million, respectively. Accumulated amortization of intangible assets at December 31, 1996 and 1995 amounted to \$2.452 billion and \$1.845 billion, respectively.

Time Warner separately reviews the carrying value of acquired intangible assets for each acquired entity on a quarterly basis to determine whether an impairment may exist. Time Warner considers relevant cash flow and profitability information, including estimated future operating results, trends and other available information, in assessing whether the carrying value of intangible assets can be recovered. Upon a determination that the carrying value of intangible assets will not be recovered from the undiscounted future cash flows of the acquired business, the carrying value of such intangible assets would be considered impaired and will be reduced by a charge to operations in the amount of the impairment. An impairment charge is measured as any deficiency in estimated discounted future cash flows of the acquired business to recover the carrying value related to the intangible assets.

**Income Taxes.** Income taxes are provided using the liability method prescribed by FASB Statement No. 109, "Accounting for Income Taxes." Under the liability method, deferred income taxes reflect tax carryforwards and the net tax effects of temporary differences between the carrying amount of assets and liabilities for financial statement and income tax purposes, as determined under enacted tax laws and rates. The financial effect of changes in tax laws or rates is accounted for in the period of enactment.

Realization of the net operating loss and investment tax credit carryforwards, which were acquired in acquisitions, are accounted for as a reduction of goodwill.

The principal operations of the Entertainment Group are conducted by partnerships. Income tax expense includes all income taxes related to Time Warner's allocable share of partnership income and its equity in the income tax expense of corporate subsidiaries of the partnerships.

**Stock Options.** In accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"), compensation cost for stock options is recognized in income based on the excess, if any, of the quoted market price of the stock at the grant date of the award or other measurement date over the amount an employee must pay to acquire the stock. The exercise price for stock options granted to employees equals or exceeds the fair market value of Time Warner common stock at the date of grant, thereby resulting in no recognition of compensation expense by Time Warner.

**Loss Per Common Share.** Loss per common share is based upon the net loss applicable to common shares after preferred dividend requirements and upon the weighted average of common shares outstanding during the period. The conversion of securities convertible into common stock and the exercise of stock options were not assumed in the calculations of loss per common share because the effect would have been antidilutive.

## 2. MERGERS AND ACQUISITIONS

**TBS Transaction** On October 10, 1996, New Time Warner acquired the remaining 80% interest in TBS that was not already owned by Old Time Warner (the "TBS Transaction"). As part of the transaction, each of Old Time Warner and TBS became separate, wholly owned subsidiaries of New Time Warner which combines, for financial reporting purposes, the consolidated net assets and operating results of Old Time Warner and TBS. Each issued and outstanding share of each class of capital stock of Old Time Warner was converted into one share of a substantially identical class of capital stock of New Time Warner.

In connection with the TBS Transaction, New Time Warner issued (i) approximately 173.4 million shares of common stock (including 50.6 million shares of a special class of non-redeemable common stock having 1/100th of a vote per share on certain limited matters ("LMCN-V Class Common Stock") to affiliates of Liberty Media Corporation ("LMC"), a subsidiary of Tele-Communications, Inc.), in exchange for shares of TBS capital stock and (ii) approximately 14 million stock options to replace all outstanding TBS stock options. In addition, New Time Warner agreed to issue to LMC and its affiliates at a later date an additional five million shares of LMCN-V Class Common Stock and \$67 million of consideration payable, at the election of New Time Warner, in cash or additional shares of LMCN-V Class Common Stock. This additional consideration will be issued pursuant to a separate option and non-competition agreement that will provide, if New Time Warner exercises its option, for a subsidiary of LMC to provide certain satellite uplink and distribution services for WTBS, a broadcast television station owned by TBS, if it is converted to a copyright-paid, cable television programming service. New Time Warner has also fully and unconditionally guaranteed all of TBS's and Old Time Warner's outstanding publicly traded indebtedness, which amounted to \$1.030 billion and \$7.754 billion, respectively, at December 31, 1996.

The TBS Transaction was accounted for by the purchase method of accounting for business combinations; accordingly, the cost to acquire TBS of approximately \$6.2 billion was preliminarily allocated to the net assets acquired in proportion to estimates of their respective fair values, as follows: goodwill - \$6.746 billion; other current and noncurrent assets - \$3.806 billion; long-term debt - \$2.765 billion; deferred income taxes - \$189 million; and other current and noncurrent liabilities - \$1.416 billion.

**Cable Transactions** On January 4, 1996, Time Warner acquired CVI which owned cable television systems serving approximately 1.3 million subscribers, in exchange for the issuance of approximately 2.9 million shares of common stock and approximately 6.3 million shares of new convertible preferred stock ("Series E Preferred Stock" and "Series F Preferred Stock"), as adjusted, and the assumption or incurrence of approximately \$2 billion of indebtedness. The acquisition was accounted for by the purchase method of accounting for business combinations; accordingly, the cost to acquire CVI of \$904 million was allocated to the net assets acquired in proportion to their respective fair values, as follows: cable television franchises - \$2.390 billion; goodwill - \$688 million; other current and noncurrent assets - \$481 million; long-term debt - \$1.766 billion; deferred income taxes - \$731 million; and other current and noncurrent liabilities - \$158 million.

On July 6, 1995, Time Warner acquired KBLCOM, which owned cable television systems serving approximately 700,000 subscribers, and a 50% interest in Paragon Communications ("Paragon"), which owned cable television systems serving an additional 972,000 subscribers. The other 50% interest in Paragon was already owned by TWE. To acquire KBLCOM, Time Warner issued 1 million shares of common stock and 11 million shares of a new convertible preferred stock ("Series D Preferred Stock") and assumed or incurred approximately \$1.2 billion of indebtedness. The acquisition was accounted for by the purchase method of accounting for business combinations; accordingly, the cost to acquire KBLCOM of approximately \$1.033 billion was allocated to the net assets acquired in proportion to their respective fair values, as follows: investments - \$950 million; cable television franchises - \$1.366 billion; goodwill - \$586 million; other current and noncurrent assets - \$289 million; long-term debt - \$1.213 billion; deferred income taxes - \$895 million; and other current liabilities - \$50 million.

On May 2, 1995, Time Warner acquired Summit, which owned cable television systems serving approximately 162,000 subscribers, in exchange for the issuance of approximately 1.6 million shares of common stock and approximately 3.3 million shares of a new convertible preferred stock ("Series C Preferred Stock") and the assumption of \$140 million of indebtedness. The acquisition was accounted for by the purchase method of accounting for business combinations; accordingly, the cost to acquire Summit of approximately \$351 million was allocated to the assets acquired in proportion to their respective fair values, as follows: cable television franchises - \$272 million; goodwill - \$146 million; other current and noncurrent assets - \$144 million.



long term debt, \$140 million; deferred income taxes, \$166 million; and other current liabilities, \$5 million. In August 1996, all shares of Series C Preferred Stock were exchanged for shares of a new series of convertible preferred stock with substantially identical terms ("Series J Preferred Stock").

On April 1, 1995, TWE formed a cable television joint venture with the Advance/Newhouse Partnership ("Advance/Newhouse") to which Advance/Newhouse and TWE contributed cable television systems (or interests therein) serving approximately 4.5 million subscribers, as well as certain foreign cable investments and programming investments that included Advance/Newhouse's 10% interest in Primestar Partners, L.P. ("Primestar"). TWE owns a two-thirds equity interest in the TWE-Advance/Newhouse Partnership and is the managing partner. TWE consolidates the partnership and the one-third equity interest owned by Advance/Newhouse is reflected in TWE's consolidated financial statements as minority interest. In accordance with the partnership agreement, Advance/Newhouse can require TWE to purchase its equity interest for fair market value at specified intervals following the death of both of its principal shareholders. Beginning on April 1, 1998, either partner can initiate a dissolution in which TWE would receive two-thirds and Advance/Newhouse would receive one-third of the partnership's net assets. The assets contributed by TWE and Advance/Newhouse to the partnership were recorded at their predecessor's historical cost. No gain was recognized by TWE upon the capitalization of the partnership.

**Pro Forma Financial Information.** The accompanying consolidated statement of operations includes the operating results of each acquired business from the respective closing date of each transaction. On a pro forma basis, giving effect to (i) the TBS Transaction, (ii) the cable transactions as described above, (iii) the ITOCHU/Toshiba Transaction (Note 3), (iv) the Preferred Stock Refinancing (Note 10), (v) Time Warner's and TWE's debt refinancings (Note 6) and (vi) certain asset sales, including the sale of 51% of TWE's interest in Six Flags Entertainment Corporation ("Six Flags") (Note 3), as if each of such transactions had occurred at the beginning of 1995, Time Warner would have reported for the years ended December 31, 1996 and 1995, respectively, revenues of \$12.799 billion and \$12.154 billion.

depreciation and amortization of \$1.245 billion and \$1.205 billion, operating income of \$939 million and \$942 million, equity in the pretax income of the Entertainment Group of \$290 million and \$1.86 million, a loss before extraordinary item of \$284 million and \$233 million (\$1.05 and \$ .97 per common share) and a net loss of \$319 million and \$275 million (\$1.11 and \$1.04 per common share).

### 3. ENTERTAINMENT GROUP

Time Warner's investment in and amounts due to and from the Entertainment Group at December 31, 1996 and 1995 consists of the following:

December 31, (in millions)	1996	1995
Investment in TWE	\$ 6,254	\$ 6,179
Stock option related		
distributions due from TWE	93	122
Credit agreement debt due to TWE	(400)	(400)
Other net liabilities due to TWE, principally related to home video distribution	(256)	(278)
Investment in and amounts due to and from TWE	5,691	5,623
Investment in other		
Entertainment Group companies	123	111
Total	\$ 5,814	\$ 5,734

TWE is a Delaware limited partnership that was capitalized on June 30, 1992 to own and operate substantially all of the Filmed Entertainment, Warner Bros., Cable Networks, HBO and Cable businesses previously owned by subsidiaries of Time Warner. Certain Time Warner subsidiaries are the general partners of TWE ("Time Warner General Partners"). Time Warner acquired the aggregate 11.22% limited partnership interests previously held by subsidiaries of each of ITOCHU Corporation and Toshiba Corporation in 1995 for an aggregate cost of \$1.36 billion, consisting of 15 million shares of convertible preferred stock ("Series G Preferred Stock", "Series H Preferred Stock" and "Series I Preferred Stock") and \$10 million in cash (the "ITOC HU/Toshiba Transaction"). Accordingly, Time Warner, through its wholly owned subsidiaries, collectively owns general

and limited partnership interests in TWE consisting of 74.49% of the Series A Capital and Residual Capital and 100% of the Senior Capital and Series B Capital. The remaining 25.51% limited partnership interests in the Series A Capital and Residual Capital of TWE are owned by U S WEST, which acquired such interests in 1993 for \$1.532 billion of cash and a \$1.021 billion 4.4% note (the "U S WEST Note Receivable") that was fully collected during 1996. The ITOCHU/Toshiba Transaction was accounted for by the purchase method of accounting for business combinations.

Each partner's interest in TWE consists of the initial priority capital and residual equity amounts that were assigned to that partner or its predecessor based on the estimated fair value of the net assets each contributed to TWE, as adjusted for the fair value of certain assets distributed by TWE to the Time Warner General Partners in 1993 which were not subsequently reacquired by TWE in 1995 ("Contributed Capital"), plus, with respect to the priority capital interests only, any undistributed priority capital return. The priority capital return consists of net partnership income allocated to date in accordance with the provisions of the TWE partnership agreement and the right to be allocated additional partnership income which, together with any previously allocated net partnership income, provides for the various priority capital rates of return specified in the table below. The sum of Contributed Capital and the undistributed priority capital return is referred to herein as "Cumulative Priority Capital." Cumulative Priority Capital is not necessarily indicative of the fair value of the underlying priority capital interests principally due to above-market rates of return on certain priority capital interests as compared to securities of comparable credit risk and maturity, such as the 13.25% rate of return on the Series B Capital interest owned by the Time Warner General Partners. Furthermore, the ultimate realization of Cumulative Priority Capital could be affected by the fair value of TWE which is subject to fluctuation.

A summary of the priority of Contributed Capital, Time Warner's ownership of Contributed Capital and Cumulative Priority Capital at December 31, 1996 and priority capital rates of return thereon is as set forth below:

Priority of Contributed Capital	Contributed Capital <sup>(a)</sup> (billions)	Cumulative Priority Capital (billions)	Priority Capital Rates of Return <sup>(b)</sup> 1% per annum compounded quarterly	% Owned by Time Warner
Senior Capital	\$1.4	1.5 <sup>(c)</sup>	8.00%	100.00%
Series A Capital	5.6	9.9	13.00% <sup>(d)</sup>	74.49%
Series B Capital	2.9 <sup>(e)</sup>	5.2	13.25% <sup>(d)</sup>	100.00%
Residual Capital	3.3 <sup>(e)</sup>	3.3 <sup>(e)</sup>	- <sup>(f)</sup>	74.49%

(a) Excludes partnership income or loss allocated thereon.

(b) The income allocations related to priority capital rates of return are based on partnership income after any special tax allocations.

(c) Net of \$386 million of partnership income distributed in 1995 representing the priority capital return thereon through June 30, 1995.

(d) 11.00% to the extent concurrently distributed.

(e) 11.25% to the extent concurrently distributed.

(f) Residual Capital is not entitled to stated priority rates of return and, as such, its Cumulative Priority Capital is equal to its Contributed Capital. However, in the case of certain events such as the liquidation or dissolution of TWE, Residual Capital is entitled to any excess of the fair value of the net assets of TWE over the aggregate amount of Cumulative Priority Capital and special tax allocations.

(g) The Contributed Capital relating to the Series B Capital has priority over the priority returns on the Series A Capital. The Contributed Capital relating to the Residual Capital has priority over the priority returns on the Series B Capital and the Series A Capital.

Because Contributed Capital is based on the fair value of the net assets that each partner contributed to the partnership, the aggregate of such amounts is significantly higher than TWE's partners' capital as reflected in the consolidated financial statements, which is based on the historical cost of the contributed net assets. For purposes of allocating partnership income or loss to the partners, partnership income or loss is based on the fair value of the net assets contributed to the



partnership and results in significantly less partnership income, or results in partnership losses, in contrast to the net income reported by TWE for financial statement purposes, which is also based on the historical cost of contributed net assets.

Under the TWE partnership agreement, partnership income, to the extent earned, is first allocated to the partners' capital accounts so that the economic burden of the income tax consequences of partnership operations is borne as though the partnership were taxed as a corporation ("special tax allocations"), then to the Senior Capital, Series A Capital and Series B Capital, in order of priority, at rates of return ranging from 8% to 13.25% per annum, and finally to the Residual Capital. Partnership losses generally are allocated first to eliminate prior allocations of partnership income to, and then to reduce the Contributed Capital of, the Residual Capital, Series B Capital and Series A Capital, in that order, then to reduce the Time Warner General Partners' Senior Capital, including partnership income allocated thereto, and finally to reduce any special tax allocations. To the extent partnership income is insufficient to satisfy all special allocations in a particular accounting period, the right to receive additional partnership income necessary to provide for the various priority capital rates of return is carried forward until satisfied out of future partnership income, including any partnership income that may result from any liquidation, sale or dissolution of TWE.

The TWE partnership agreement provides, under certain circumstances, for the distribution of partnership income allocated to the Senior Capital owned by the Time Warner General Partners. Pursuant to such provision, \$366 million of partnership income was distributed to the Time Warner General Partners in 1995. Beginning on July 1, 1997, the Senior Capital and, to the extent not previously distributed, partnership income allocated thereto is required to be distributed in three annual installments, with the initial distribution expected to be approximately \$535 million. The Series B Capital owned by the Time Warner General Partners may be increased if certain operating performance targets are achieved over a five year period ending on December 31, 1996 and a ten year period ending on December 31, 2001. Although satisfaction of the ten year operating performance target is indeterminable at this time, the five year target was not attained.

TWE reported net income of \$210 million, \$73 million and \$181 million in 1998, 1995 and 1994, respectively, no portion of which was allocated to the limited partners. Time Warner did not recognize a gain when TWE was capitalized. TWE recorded the assets contributed by the Time Warner General Partners at Time Warner's historical cost. The excess of the Time Warner General Partners' interests in the net assets of TWE over the net book value of their investment in TWE is being amortized to income over a twenty-year period.

U.S. WEST has an option to obtain up to an additional 6.33% of Series A Capital and Residual Capital interests, depending on cable operating performance. The option is exercisable between January 1, 1999 and on or about May 31, 2005 at a maximum exercise price of \$1.25 billion to \$1.8 billion depending on the year of exercise. Either U.S. WEST or TWE may elect that the exercise price be paid with partnership interests rather than cash.

Each Time Warner General Partner has guaranteed a pro rata portion of approximately \$5.4 billion of TWE's debt and accrued interest at December 31, 1996, based on the relative fair value of the net assets each Time Warner General Partner contributed to TWE. Such indebtedness is recourse to each Time Warner General Partner only to the extent of its guarantee. In addition to their interests in TWE and the other Entertainment Group companies, the assets of the Time Warner General Partners include a 10.6% interest in TBS, a 10.2% interest in Old Time Warner, 18.1 million common shares of Hasbro, Inc. and substantially all the assets of Time Warner's music business. There are no restrictions on the ability of the Time Warner General Partner guarantors to transfer assets, other than TWE assets, to parties that are not guarantors.

Set forth below is summarized financial information of the Entertainment Group, which reflects the formation by TWE of the TWE-Advance/Newhouse Partnership effective as of April 1, 1995 (Note 2), the deconsolidation of Six Flags effective as of June 23, 1995 and the consolidation of Paragon effective as of July 6, 1995.

**TIME WARNER ENTERTAINMENT GROUP**

**Operating Statement Information**

Years Ended December 31, (millions)	1996	1995	1994
Revenues	\$ 10,861	\$ 9,829	\$ 8,508
Depreciation and amortization	1,244	1,060	959
Business segment operating income	1,090	992	852
Interest and other, net	524	539	616
Minority interest	207	133	-
Income before income taxes	290	256	176
Income before extraordinary item	220	170	136
Net income	220	146	136

**Cash Flow Information**

Years Ended December 31, (millions)	1996	1995	1994
Cash provided by operations	\$ 1,912	\$ 1,495	\$ 1,341
Capital expenditures	(1,719)	(1,653)	(1,235)
Investments and acquisitions	(146)	(217)	(186)
Investment proceeds	612	1,120	51
Loan to Time Warner	-	-	(400)
Borrowings	215	2,484	1,001
Debt repayments	(716)	(3,596)	(953)
Collections on note receivable from U S WEST	169	602	234
Capital distributions	(228)	(1,063)	(120)
Other financing activities, net	(92)	(34)	-
Increase (decrease) in cash and equivalents	7	(862)	(287)

**Balance Sheet Information**

December 31, (millions)	1996	1995
Cash and equivalents	\$ 216	\$ 209
Total current assets	3,147	2,909
Total assets	20,027	18,960
Total current liabilities	4,092	3,230
Long term debt	5,676	6,137
Minority interests	1,020	726
Time Warner General Partners' Senior Capital, consisting of \$1.364 billion		
Contributed Capital plus an undistributed priority return	1,543	1,426
Partners' capital	6,681	6,576

The assets and cash flows of TWE are restricted by the TWE partnership and credit agreements and are unavailable for use by the partners except through the payment of certain fees, reimbursements, cash distributions and loans, which are subject to limitations. At December 31, 1996 and 1995, the Time Warner General Partners had recorded \$93 million and \$122 million, respectively, of stock option related distributions due from TWE, based on closing prices of Time Warner common stock of \$37.50 and \$37.875, respectively. Time Warner is paid when the options are exercised. The Time Warner General Partners also receive tax-related distributions from TWE. The payment of such distributions was previously subject to restrictions until July 1995 and is now made to the Time Warner General Partners on a current basis. During 1996, the Time Warner General Partners received distributions from TWE in the amount of \$228 million, consisting of \$215 million of tax-related distributions and \$13 million of stock option related distributions. During 1995, the Time Warner General Partners received net distributions from TWE in the amount of \$1,063 million, consisting of \$366 million of TWE partnership income allocated to the Time Warner General Partners' Senior Capital interest, \$680 million of tax-related distributions and \$17 million of stock option related distributions. During 1994, the Time Warner General Partners received net distributions from TWE in the amount of \$120 million, consisting of \$115 million of tax-related distributions and \$5 million of stock option related distributions. In addition to the tax, stock option and Time Warner General Partners' Senior Capital distributions, TWE may make other distributions, generally depending on excess cash and credit agreement limitations. The Time Warner General Partners' full share of such distributions may be deferred if the limited partners do not receive certain threshold amounts by certain dates.

On June 23, 1995, TWE sold 51% of its interest in Six Flags to an investment group led by Boston Ventures for \$204 million and received \$640 million in additional proceeds from Six Flags, representing payment of certain intercompany indebtedness and licensing fees. As a result of the transaction, Six Flags has been deconsolidated and TWE's remaining 49% interest in Six Flags is now accounted for under the equity method of accounting. TWE reduced debt by approximately \$850 million in connection with the transaction, and a portion of the income on the transaction has been deferred by TWE principally as a result of its guarantee of certain third-party, zero-coupon indebtedness of Six Flags due in 1999.

#### 4. OTHER INVESTMENTS

Time Warner's other investments consist of:

December 31, (millions)	1996	1995
Equity method investments <sup>(1)</sup>	\$ 1,302	\$ 1,800
Market value method investments	401	375
Cost method investments	126	116
Total	\$ 1,819	\$ 2,289

(1) Equity method investments at December 31, 1995 included Time Warner's investment in TBS which was carried at \$541 million. On October 10, 1996, Time Warner consolidated its investment in TBS as a result of its acquisition of the remaining interest in TBS that it did not already own (Note 2).

Market value method investments include 18.1 million shares of common stock of Hasbro, Inc. ("Hasbro"). Notwithstanding the market value per share, such shares can be used, at Time Warner's option, to fully satisfy either its obligations with respect to the zero coupon exchangeable notes due 2012 (Note 6) or the Company-obligated mandatorily redeemable preferred securities of a subsidiary due 1997 (Note 9). Because the issuance of the mandatorily redeemable preferred securities provides Time Warner with protection against the risk of depreciation of the market price of Hasbro common stock and the zero coupon exchangeable notes limit Time Warner's ability to share in the appreciation of the market price of Hasbro common stock, the combination thereof has effectively monetized Time Warner's investment in Hasbro.

In addition to TWE and its equity investees, companies accounted for using the equity method include: Cinamerica Theatres, L.P. (50% owned) and The Columbia House Company

partnerships (50% owned), other music joint ventures (generally 50% owned) and in 1995 and 1994 only, TBS (20% owned).

A summary of combined financial information as reported by the equity investees of Time Warner is set forth below:

Years Ended December 31, (millions)	1996	1995	1994
Revenues	\$ 1,773	\$ 5,123	\$ 4,444
Depreciation and amortization	29	219	182
Operating income	173	547	584
Income before extraordinary items and cumulative effect of a change in accounting principle	61	188	281
Net income	61	188	256
Current assets	1,002	2,272	2,113
Total assets	1,816	5,851	5,194
Current liabilities	517	1,318	1,136
Long-term debt	1,360	3,826	3,730
Total liabilities	1,999	5,886	5,423
Total shareholders' deficit or partners' capital	(383)	(35)	(229)

#### 5. INVENTORIES

Inventories consist of:

December 31, (millions)	1996		1995	
	Current	Noncurrent	Current	Noncurrent
<b>Film costs:</b>				
Released, less amortization	\$ 209	\$ 142	\$ -	\$ -
Completed and not released	4	-	-	-
In process and other	24	251	-	-
Library, less amortization	-	1,116	-	-
Programming costs, less amortization	213	189	-	-
Magazines, books and recorded music	441	-	443	-
Total	\$ 941	\$ 1,600	\$ 443	\$ -

The increase in film and programming costs resulted from the acquisition of TBS effective as of October 10, 1996. Excluding the Library, the total cost incurred in the production of theatrical and television films since such date amounted to \$339 million in 1996, and the total cost amortized amounted to \$239 million. Excluding the Library, the unamortized cost of completed films at December 31, 1996 amounted to \$405 million, more than 90% of which is expected to be amortized within three years after release.

## 8. LONG-TERM DEBT

Long-term debt consists of

December 31, (millions)	1996	1995
<b>Old Time Warner<sup>(1)</sup>:</b>		
7.45% Notes due February 1, 1998	\$ 500	\$ 500
7.95% Notes due February 1, 2000	500	500
Floating rate notes due		
August 15, 2000 (6.5% and 6.8%)	454	454
7.975% Notes due August 15, 2004	272	272
7.75% Notes due June 15, 2005	497	497
8.11% Debentures due August 15, 2006	545	545
8.18% Debentures due August 15, 2007	545	545
7.48% Debentures due January 15, 2008	166	-
Zero coupon exchangeable notes		
due December 17, 2012 (6.25% yield)	618	581
Zero coupon convertible notes		
due June 22, 2013 (5% yield)	1,070	1,019
9.125% Debentures due January 15, 2013	1,000	1,000
8.75% Convertible subordinated debentures due January 10, 2015	-	1,226
8.05% Debentures due January 15, 2016	150	-
8.75% Debentures due April 1, 2017	-	248
9.15% Debentures due January 15, 2023	1,000	1,000
6.85% Debentures due January 15, 2026	400	-
8.30% Discount Debentures due January 15, 2036	37	-
Debt due to TWE (6.7% and 6.8%)	400	400
<b>TBS<sup>(1)</sup>:</b>		
TBS Credit Agreements (7.0%)	677	-
7.4% Senior Notes due February 1, 2004	250	-
Zero coupon subordinated convertible notes due February 13, 2007 (7.25% yield)		
8.375% Senior Notes due July 1, 2013	297	-
8.4% Senior Debentures due February 1, 2024	200	-
<b>TWI Cable:</b>		
1995 Credit Agreement (6.5% and 6.8%)	2,530	1,265
10.75% Senior Notes due January 30, 2002	300	-
10.5% Debentures due April 15, 2005	140	140
9.25% Senior Debentures due April 1, 2008	200	-
Other	82	115
Subtotal	13,113	10,307
Reclassification of debt due to TWE to:		
amounts due to the Entertainment Group	(400)	(400)
<b>Total</b>	<b>\$12,713</b>	<b>\$ 9,907</b>

(1) New Time Warner has guaranteed all such indebtedness of Old Time Warner and TBS, except for debt due to TWE and borrowings under the TBS Credit Agreements. New Time Warner has not guaranteed any indebtedness of TWI Cable.

**Debt Refinancings** During the past two years and in early 1997, in response to favorable market conditions and in connection with certain acquisitions, Time Warner entered into a series of financing transactions which has resulted in the refinancing of approximately \$6.4 billion of debt and the reduction of an additional \$2.5 billion of debt, as more fully described below. The debt refinancings have had the positive effect of lowering interest rates, staggering debt maturities and, with respect to the redemption of its 8.75% Convertible Subordinated Debentures due 2015 (the "8.75% Convertible Debentures") and TBS's zero coupon subordinated convertible notes due February 13, 2007 (the "TBS Convertible Notes"), eliminating the potential dilution from the conversion of such securities into 52.2 million shares of common stock. In turn, the reduction in debt, using proceeds raised from the issuance of certain preferred equity securities, has partially offset the assumption or incurrence of \$6.1 billion of debt in connection with the Cable Acquisitions and the TBS Transaction.

During the first quarter of 1997, Time Warner entered into a number of financing transactions, which resulted in the refinancing of approximately \$600 million of debt. Time Warner redeemed \$300 million principal amount of 10.75% Senior Notes due January 30, 2002 of TWI Cable Inc. ("TWI Cable"), its wholly owned subsidiary, and approximately \$283 million accreted amount of TBS Convertible Notes at an aggregate redemption price of approximately \$600 million, including redemption premiums and accrued interest thereon (collectively, the "1997 Debt Redemptions"). Time Warner also issued \$600 million principal amount of Floating Rate Reset Notes due December 30, 2001 (the "Floating Rate Reset Notes"). The Floating Rate Reset Notes bear interest at a floating rate equal to LIBOR less 25 basis points until December 30, 2001, at which time the interest rate will be reset at a fixed rate equal to 6.58% plus a margin based upon Time Warner's credit risk at such time. The Floating Rate Reset Notes are redeemable at the election of the holders, in whole but not in part, on December 30, 2001.

In October 1996, Time Warner assumed approximately \$2.8 billion of indebtedness in connection with the TBS Transaction, of which approximately \$1.1 billion was subsequently repaid during 1996 principally using proceeds from additional borrowings under the 1995 Credit Agreement (as defined below).

In April 1996, Time Warner raised approximately \$1.55 billion of net proceeds in a private placement of 10.1/4% exchangeable preferred stock (Note 10). The proceeds were used by Time Warner to redeem \$250 million principal amount of 8.75% Debentures due April 1, 2017 (the "8.75% Non-Convertible Debentures") and when taken together with the

8.75% Convertible Debentures, the "8.75% Debentures") for approximately \$265 million in May 1996 (including redemption premiums and accrued interest thereon), and to reduce bank debt of TWI Cable by approximately \$1.3 billion.

In February 1996, Time Warner redeemed its remaining \$1.2 billion principal amount of 8.75% Convertible Debentures for \$1.28 billion, including redemption premiums and accrued interest thereon. The redemption was financed with (1) proceeds raised from a \$575 million issuance in December 1995 of Company-obligated mandatorily redeemable preferred securities of a subsidiary and (2) \$750 million of proceeds raised from the issuance in January 1996 of (i) \$400 million principal amount of 6.85% debentures due 2026, which are redeemable at the option of the holders thereof in 2003, (ii) \$200 million principal amount of 8.3% discount debentures due 2036, which do not pay cash interest until 2016, (iii) \$166 million principal amount of 7.48% debentures due 2008 and (iv) \$150 million principal amount of 8.05% debentures due 2016. Time Warner had previously redeemed approximately \$1 billion principal amount of 8.75% Convertible Debentures for \$1.06 billion (including redemption premiums and accrued interest) in September 1995 using proceeds raised from (a) a \$500 million issuance in June 1995 of 7.75% ten-year notes, (b) a \$374 million issuance in August 1995 of Company-obligated mandatorily redeemable preferred securities of a subsidiary and (c) available cash and equivalents. See Note 9 for a description of the mandatorily redeemable preferred securities issued in connection with such redemptions.

In January 1996, in connection with its acquisition of CVI, subsidiaries of Time Warner assumed \$500 million of public notes and debentures of CVI and borrowed \$1.5 billion under the 1995 Credit Agreement (as defined below) to refinance a like amount of other indebtedness assumed or incurred in such acquisition.

In August 1995, Time Warner redeemed all of its \$1.8 billion principal amount of outstanding Redeemable Reset Notes due August 15, 2002 (the "Reset Notes") in exchange for new securities, consisting of approximately \$454 million aggregate principal amount of Floating Rate Notes due August 15, 2000, approximately \$272 million aggregate principal amount of 7.975% Notes due August 15, 2004, approximately \$545 million aggregate principal amount of 8.11% Debentures due August 15, 2006, and approximately \$545 million aggregate principal amount of 8.18% Debentures due August 15, 2007.

In July 1995, TWI Cable borrowed approximately \$1.2 billion under the 1995 Credit Agreement to refinance certain indebtedness assumed or incurred in the acquisition of KBLCOM.

In June 1995, TWI Cable, TWE and the TWE-Advance/Newhouse Partnership executed a five-year revolving credit facility (the "1995 Credit Agreement"). The 1995 Credit Agreement enabled such entities to refinance certain indebtedness assumed in the cable acquisitions, to refinance TWE's indebtedness under a pre-existing bank credit agreement and to finance the ongoing working capital, capital expenditure and other corporate needs of each borrower.

An extraordinary loss of \$17 million was recognized by Time Warner in the first quarter of 1997 in connection with the 1997 Debt Redemptions. An extraordinary loss of \$35 million was recognized in 1996 in connection with Time Warner's redemption of the 8.75% Debentures. An extraordinary loss of \$42 million was recognized in 1995 in connection with Time Warner's partial redemption of the 8.75% Convertible Debentures and the write-off by TWE of deferred financing costs related to its former bank credit agreement that was terminated.

**Zero Coupon Notes.** Time Warner's zero coupon notes do not pay interest until maturity. The zero coupon exchangeable notes due December 17, 2012 are exchangeable at any time by the holders into an aggregate of 18.1 million shares of common stock of Hasbro at the rate of 10.9515 shares for each \$1,000 principal amount of notes, subject to Time Warner's right to pay in whole or in part with cash instead of Hasbro common stock. The terms of these notes have been adjusted for a 3-for-2 stock split of Hasbro common stock that occurred in March 1997 (the "Hasbro Stock Split"). Time Warner can elect to redeem the notes any time after December 17, 1997, and holders can elect to have the notes redeemed prior thereto in the event of a change of control, at the issue price plus accrued interest. Holders also can elect to have the notes redeemed at the issue price plus accrued interest on December 17, 1997, 2002 and 2007, subject to Time Warner's right to pay in whole or in part with Hasbro common stock instead of cash. The equivalent conversion price of Hasbro common stock at the first date of redemption is \$36.27 per share, and will be adjusted thereafter in proportion to changes in the accrued original issue discount of each note. The 18.1 million shares of Hasbro common stock owned by Time Warner can be used by the Company, at its election, to satisfy its obligations under such notes or its obligations under certain mandatorily redeemable preferred securities of a subsidiary (Note 9). Unamortized original issue discount on the zero coupon exchangeable notes due 2012 was \$1.033 billion and \$1.070 billion at December 31, 1996 and 1995, respectively.

The zero coupon convertible notes due June 22, 2013 are convertible at any time by the holders into an aggregate of 18.7 million shares of Time Warner common stock at the rate of 7.759 shares for each \$1,000 principal amount of notes. Time Warner can elect to redeem the notes any time after June 22, 1998, and holders can elect to have the notes redeemed prior thereto in the event of a change in control, at the issue price plus accrued interest. Holders also can elect to have the notes redeemed at the issue price plus accrued interest on June 22, 1998, 2003 and 2008, subject to Time Warner's right to pay in whole or in part with Time Warner common stock instead of cash. The equivalent conversion price of Time Warner common stock at the first date of redemption is \$61.44 per share, and will be adjusted thereafter in proportion to changes in the accrued original issue discount of each note. Unamortized original issue discount on the zero coupon convertible notes due 2013 was \$1.345 billion and \$1.396 billion at December 31, 1996 and 1995, respectively.

**Bank Credit Facilities.** The 1995 Credit Agreement permits borrowings in an aggregate amount of up to \$8.3 billion, with no scheduled reductions in credit availability prior to maturity in June 2000. Borrowings are limited to \$4 billion in the case of TWI Cable, \$5 billion in the case of the TWE-Advance/Newhouse Partnership and \$8.3 billion in the case of TWE, subject in each case to certain limitations and adjustments. Such borrowings bear interest at specific rates for each of the three borrowers, generally equal to LIBOR plus a margin initially ranging from 50 to 87.5 basis points, which margin will vary based on the credit rating or financial leverage of the applicable borrower. Unused credit is available for general business purposes and to support any commercial paper borrowings. Each borrower is required to pay a commitment fee initially ranging from .2% to .35% per annum on the unused portion of its commitment. TWI Cable may also be required to pay an annual facility fee equal to .1875% of the entire amount of its commitment, depending on the level of its financial leverage in any given year. The 1995 Credit Agreement contains certain covenants for each borrower relating to, among other things, additional indebtedness; liens on assets; cash flow coverage and leverage ratios; and loans, advances, distributions and other cash payments or transfers of assets from the borrowers to their respective partners or affiliates.

In connection with the TBS Transaction, Time Warner assumed approximately \$1.7 billion of debt under two separate revolving credit facilities of TBS (the "TBS Credit Agreements"). The TBS Credit Agreements permit borrowings by TBS in an

aggregate amount of up to \$2 billion. Borrowing availability under the TBS Credit Agreements is scheduled to be reduced by \$100 million for each calendar quarter in 1998 and thereafter, by \$200 million per quarter until December 31, 2000, at which time the TBS Credit Agreements expire. Borrowings under the TBS Credit Agreements bear interest at rates generally equal to LIBOR plus a margin ranging from 50 to 150 basis points, which margin will vary based on a measure of TBS's financial leverage. Unused credit is available for general business purposes. TBS is required to pay commitment fees of .375% on the unused portion of its commitments. The TBS Credit Agreements contain certain covenants for TBS relating to, among other things, additional indebtedness; liens on assets; guarantees; dispositions and acquisitions; cash flow coverage and leverage ratios; and loans, advances, distributions and other cash payments or transfers of assets from TBS to Time Warner or its affiliates.

Principally as a result of the restrictions under the 1995 Credit Agreement and the TBS Credit Agreements, restricted net assets of consolidated subsidiaries of Time Warner amounted to approximately \$8.7 billion at December 31, 1996.

**Time Warner - TWE Credit Agreement.** Time Warner and TWE entered into a credit agreement in 1994 that allows Time Warner to borrow up to \$400 million from TWE through September 15, 2000. Outstanding borrowings from TWE bear interest at LIBOR plus 1% per annum. Time Warner borrowed \$400 million in 1994 under the credit agreement, and used the proceeds therefrom principally to repay certain of its notes at their maturity. In addition, each Time Warner General Partner has guaranteed a pro rata portion of approximately \$5.4 billion of TWE's debt and accrued interest at December 31, 1996, as more fully described in Note 3.

**Interest Expense and Maturities.** At December 31, 1996, Time Warner had interest rate swap contracts to pay floating rates of interest and receive fixed rates of interest on \$2.3 billion notional amount of indebtedness, which resulted in approximately 47% of Time Warner's underlying debt being subject to variable interest rates (Note 14).

Interest expense amounted to \$968 million in 1996, \$877 million in 1995 and \$769 million in 1994, including \$26 million in 1996, \$28 million in 1995 and \$12 million in 1994 which was paid to TWE in connection with borrowings under Time Warner's \$400 million credit agreement with TWE. The weighted average interest rate on Time Warner's total debt, including the effect of interest rate swap contracts, was 7.5% and 7.9% at December 31, 1996 and 1995, respectively.



Annual repayments of long-term debt for the five years subsequent to December 31, 1996 consist of \$500 million due in 1998 and \$4.161 billion due in 2000. Such repayments exclude the aggregate repurchase or redemption prices of \$656 million in 1997 and \$1.151 billion in 1998 relating to the zero coupon exchangeable notes and zero coupon convertible notes, respectively, in the years in which the holders of such debt may first exercise their redemption options.

## 7. BORROWINGS AGAINST FUTURE STOCK OPTION PROCEEDS

In connection with Time Warner's common stock repurchase program (Note 11), Time Warner entered into a five-year, \$750 million revolving credit facility (the "Stock Option Proceeds Credit Facility") in May 1996. Borrowings under the Stock Option Proceeds Credit Facility are principally used to fund stock repurchases and approximately \$200 million of preferred dividend requirements on Time Warner's Series G, H, I and J Preferred Stock. At December 31, 1996, Time Warner had borrowed \$488 million under the Stock Option Proceeds Credit Facility.

The Stock Option Proceeds Credit Facility initially provided for borrowings of up to \$750 million, of which up to \$100 million is reserved solely for the payment of interest and fees thereunder. Borrowings under the Stock Option Proceeds Credit Facility generally bear interest at LIBOR plus a margin equal to 75 basis points and are principally expected to be repaid from the cash proceeds received from the exercise of designated employee stock options. The receipt of such stock option proceeds permanently reduces the borrowing availability under the facility, which has been reduced to approximately \$715 million as of December 31, 1996. At December 31, 1996, based on a closing market price of Time Warner common stock of \$37.50, the aggregate value of potential proceeds to Time Warner from the exercise of outstanding vested, "in the money" stock options covered under the facility was approximately \$1.5 billion, representing a 2.1 to 1 coverage ratio over the related borrowing availability. To the extent that such stock option proceeds are not sufficient to satisfy Time Warner's obligations under the Stock Option Proceeds Credit Facility, Time Warner is generally required to repay such borrowings using proceeds from the sale of shares of its common stock held in escrow under the Stock Option Proceeds Credit Facility or, at Time Warner's election, using available cash on hand. In addition,

as a result of Time Warner's commitment to use the Stock Option Proceeds Credit Facility to fund approximately \$200 million of preferred dividend requirements on its Series G, H, I and J Preferred Stock, Time Warner has also supplementally agreed to place in escrow an amount of cash equal to the excess of the unpaid preferred dividend requirements on such series of convertible preferred stock over the borrowing availability under the facility at any time. At December 31, 1996, Time Warner had placed \$62 million of cash and 36 million shares in escrow under these arrangements, which shares are not considered to be issued and outstanding capital stock of the Company. Time Warner may be required, from time to time, to have up to 52.5 million shares held in escrow.

## 8. INCOME TAXES

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

Years Ended December 31, (millions)	1996	1995	1994
Domestic	\$ (193)	\$ (203)	\$ (178)
Foreign	197	205	167
Total	\$ 4	\$ 2	\$ 89

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

Years Ended December 31, (millions)	1996	1995	1994
Federal:			
Current <sup>(1)</sup>	\$ 50	\$ 42	\$ 66
Deferred	(143)	(167)	(81)
Foreign:			
Current <sup>(2)</sup>	230	215	194
Deferred	(16)	8	(45)
State and Local:			
Current	89	78	79
Deferred	(50)	(50)	(33)
Total	\$ 180	\$ 126	\$ 180

(1) Includes utilization of tax carryforwards of \$71 million in 1996, \$101 million in 1995 and \$48 million in 1994. Excludes current tax benefits of \$16 million in 1996, \$9 million in 1995 and \$11 million in 1994 resulting from the exercise of stock options and vesting of restricted stock awards, which were credited directly to paid-in capital, and current tax benefits of \$4 million in 1996 and \$3 million in 1995 resulting from the retirement of debt, which reduced the extraordinary losses in such years.

(2) Includes foreign withholding taxes of \$101 million in 1996, \$102 million in 1995 and \$74 million in 1994.



The differences between income taxes expected at the U.S. federal statutory income tax rate and income taxes provided are as set forth below. The relationship between income before income taxes and income tax expense is most affected by the amortization of goodwill and certain other financial statement expenses that are not deductible for income tax purposes.

Years Ended December 31, (millions)	1998	1995	1994
<b>Taxes on income at U.S.</b>			
Federal statutory rate	\$ 2	\$ 1	\$ 31
State and local taxes, net	26	18	30
<b>Nondeductible goodwill amortization</b>	131	100	97
Other nondeductible expenses	10	10	10
<b>Foreign income taxed at different rates, net of U.S. foreign tax credits</b>	4	3	1
Other	(13)	(6)	11
<b>Total</b>	<b>\$ 160</b>	<b>\$ 128</b>	<b>\$ 180</b>

Significant components of Time Warner's net deferred tax liabilities are as follows:

December 31, (millions)	1998	1995
Assets acquired in business combinations	\$ 3,788	\$ 2,863
Depreciation and amortization	912	829
Unrealized appreciation of certain marketable securities	91	81
Other	463	390
Deferred tax liabilities	\$ 254	4,283
Tax carryforwards	458	298
Accrued liabilities	322	228
Receivable allowances and return reserves	222	211
Other	170	108
Deferred tax assets	1,172	843
<b>Net deferred tax liabilities</b>	<b>\$ 4,082</b>	<b>\$ 3,420</b>

U.S. income and foreign withholding taxes have not been recorded on permanently reinvested earnings of foreign subsidiaries aggregating approximately \$860 million at December 31, 1996. Determination of the amount of unrecognized deferred U.S. income tax liability with respect to such earnings is not practicable. If such earnings are repatriated, additional U.S. income and foreign withholding taxes are substantially expected to be offset by the accompanying foreign tax credits.

U.S. federal tax carryforwards at December 31, 1996 consisted of \$752 million of net operating losses, \$37 million of foreign tax credits, \$106 million of investment tax credits and \$52 million of alternative minimum tax credits. The utilization of certain carryforwards is subject to limitations under U.S. federal income tax laws. Except for the alternative minimum tax credits which do not expire, the other U.S. federal tax carryforwards expire in varying amounts as follows for income tax reporting purposes:

(millions)	Carryforwards		
	Net Operating Losses	Investment Tax Credits	Foreign Tax Credits
1997	\$ 3	\$ 9	\$ 7
1998	5	7	15
1999	5	6	-
2000	8	3	15
Thereafter up to 2008	731	81	-
	<b>\$ 752</b>	<b>\$ 106</b>	<b>\$ 37</b>

#### 8. MANDATORILY REDEEMABLE PREFERRED SECURITIES

In August 1995, Time Warner issued approximately 12.1 million Company-obligated mandatorily redeemable preferred securities of a wholly owned subsidiary ("PERCS") for aggregate gross proceeds of \$374 million. The sole assets of the subsidiary that is the obligor on the PERCS are \$385 million principal amount of 4% subordinated notes of Old Time Warner due December 23, 1997. Cumulative cash distributions are payable on the PERCS at an annual rate of 4%. The PERCS are mandatorily redeemable on December 23, 1997, for an amount per PERCS equal to the lesser of \$54.41, and the market value of 1.5 shares of common stock of Hasbro on December 17, 1997 (as adjusted for the Hasbro Stock Split), payable in cash or, at Time Warner's option, Hasbro common stock. Time Warner has the right to redeem the PERCS at any time prior to December 23, 1997, at an amount per PERCS equal to \$54.41 (or in certain limited circumstances the lesser of such amount and the market value of 1.5 shares of Hasbro common stock at the time of redemption) plus accrued and unpaid distributions thereon and a declining premium, payable in cash or, at Time Warner's option, Hasbro common stock.

In December 1995, Time Warner issued approximately 23 million Company-obligated mandatorily redeemable preferred securities of a wholly owned subsidiary ("Preferred Trust Securities") for aggregate gross proceeds of \$575 million.

The sole assets of the subsidiary that is the obligor on the Preferred Trust Securities are \$592 million principal amount of 8 7/8% subordinated debentures of Old Time Warner due December 31, 2025. Cumulative cash distributions are payable on the Preferred Trust Securities at an annual rate of 8 7/8%. The Preferred Trust Securities are mandatorily redeemable for cash on December 31, 2025, and Time Warner has the right to redeem the Preferred Trust Securities, in whole or in part, on or after December 31, 2000, or in other certain circumstances, in each case at an amount per Preferred Trust Security equal to \$25 plus accrued and unpaid distributions thereon.

Time Warner has certain obligations relating to the PERCS and the Preferred Trust Securities which amount to a full and unconditional guaranty (on a subordinated basis) of each subsidiary's obligations with respect thereto.

#### 10. SERIES M EXCHANGEABLE PREFERRED STOCK

In April 1996, Time Warner raised approximately \$1.55 billion of net proceeds in a private placement of 1.6 million shares of 10 1/4% exchangeable preferred stock. This issuance allowed the Company to realize cash proceeds through a security whose payment terms are principally linked (until a reorganization of TWE occurs, if any) to a portion of Time Warner's currently noncash-generating interest in the Series B Capital of TWE. The proceeds raised from this transaction were used by Time Warner to reduce debt. As part of the TBS Transaction, these preferred shares were converted into registered shares of Series M exchangeable preferred stock with substantially identical terms ("Series M Preferred Stock").

Each share of Series M Preferred Stock is entitled to a liquidation preference of \$1,000 and entitles the holder thereof to receive cumulative dividends at the rate of 10 1/4% per annum, payable quarterly (1) in cash, to the extent of an amount equal to the Pro Rata Percentage (as defined below) multiplied by the amount of cash distributions received by Time Warner from TWE with respect to its interests in the Series B Capital and Residual Capital of TWE, excluding stock option related distributions and certain tax related distributions (collectively, "Eligible TWE Cash Distributions"), or (2) to the extent of any balance, at Time Warner's option, (i) in cash or (ii) in-kind, through the issuance of additional shares of Series M Preferred Stock with an aggregate liquidation preference equal to the amount of such dividends. The "Pro Rata Percentage" is equal to the ratio of (1) the aggregate liquidation preference of the outstanding shares of Series M Preferred Stock, including any accumulated and unpaid dividends thereon, to (2) Time Warner's total interest in the

Series B Capital of TWE, including any undistributed priority capital return thereon. Because cash distributions to Time Warner with respect to its interests in the Series B Capital and Residual Capital of TWE are generally restricted until June 30, 1998 and are subject to additional limitations thereafter under the TWE partnership agreement, Time Warner does not expect to pay cash dividends in the foreseeable future.

The Series M Preferred Stock may be redeemed at the option of Time Warner, in whole or in part, on or after July 1, 2006, subject to certain conditions, at an amount per share equal to its liquidation preference plus accumulated and accrued and unpaid dividends thereon, and a declining premium through July 1, 2010 (the "Optional Redemption Price"). Time Warner is required to redeem shares of Series M Preferred Stock representing up to 20%, 25%, 33 1/3% and 50% of the then outstanding liquidation preference of the Series M Preferred Stock on July 1 of 2012, 2013, 2014 and 2015, respectively, at an amount equal to the aggregate liquidation preference of the number of shares to be redeemed plus accumulated and accrued and unpaid dividends thereon (the "Mandatory Redemption Price"). Total payments in respect of such mandatory redemption obligations on any redemption date are limited to an amount equal to the Pro Rata Percentage of any cash distributions received by Time Warner from TWE in the preceding year in connection with the redemption of Time Warner's interest in the Series B Capital of TWE and in connection with certain cash distributions related to Time Warner's interest in the Residual Capital of TWE. The redemption of the Series B Capital of TWE is scheduled to occur ratably over a five-year period commencing on June 30, 2011. Time Warner is required to redeem any remaining outstanding shares of Series M Preferred Stock on July 1, 2016 at the Mandatory Redemption Price; however, in the event that Time Warner's interest in the Series B Capital of TWE has not been redeemed in full prior to such final mandatory redemption date, payments in respect of the final mandatory redemption obligation of the Series M Preferred Stock in 2016 will be limited to an amount equal to the lesser of the Mandatory Redemption Price and an amount equal to the Pro Rata Percentage of the fair market value of TWE (net of taxes) attributable to Time Warner's interests in the Series B Capital and Residual Capital of TWE.

Upon a reorganization of TWE, as defined in the related certificate of designation, Time Warner must elect either to (1) exchange each outstanding share of Series M Preferred Stock for shares of a new series of 10 1/4% exchangeable preferred stock ("Series L Preferred Stock") or (2) subject to certain conditions, redeem the outstanding shares of Series M

Preferred Stock at an amount per share equal to 110% of the liquidation preference thereof, plus accumulated and accrued and unpaid dividends thereon or, after July 1, 2006, at the Optional Redemption Price. The Series L Preferred Stock has terms similar to those of the Series M Preferred Stock, except that (i) Time Warner may only pay dividends in-kind until June 30, 2006, (ii) Time Warner is required to redeem the outstanding shares of Series L Preferred Stock on July 1, 2011 at an amount per share equal to the liquidation preference thereof, plus accumulated and accrued and unpaid dividends thereon and (iii) Time Warner has the option to exchange, in whole but not in part, subject to certain conditions, the outstanding shares of Series L Preferred Stock for Time Warner 10 1/4% Senior Subordinated Debentures due July 1, 2011 (the "Senior Subordinated Debentures") having a principal amount equal to the liquidation preference of the Series L Preferred Stock plus accrued and unpaid dividends thereon. Interest on the Senior Subordinated Debentures is payable in cash or, at Time Warner's option through June 30, 2006, in-kind through the issuance of additional Senior Subordinated Debentures with a principal amount equal to such interest. The Senior Subordinated Debentures may be redeemed at the option of Time Warner, in whole or in part, on or after July 1, 2006, subject to certain conditions, at an amount per debenture equal to its principal amount plus accrued and unpaid interest, and a declining premium through July 1, 2010.

## 11. SHAREHOLDERS' EQUITY

Shareholders' equity of Time Warner at December 31, 1996 included 35.6 million shares of convertible preferred stock, 50.6 million shares of LMCN-V Class Common Stock and 508.4 million shares of common stock (net of 50 million shares of common stock in treasury). At February 28, 1997, there were approximately 26,000 holders of record of Time Warner common stock. This total does not include the large number of investors who hold such shares through banks, brokers or other fiduciaries.

In April 1996, Time Warner's Board of Directors authorized a program to repurchase, from time to time, up to 15 million shares of Time Warner common stock. The common stock repurchased under the program is expected to be used to satisfy future share issuances related to the exercise of existing employee stock options. Actual repurchases in any period will be subject to market conditions. As of December 31, 1996, Time Warner had acquired approximately 11.4 million shares of its common stock for an aggregate cost of \$456 million. Such repurchases were principally funded with borrowings under the Stock Option Proceeds Credit Facility (Note 7).

During 1996 and 1995, Time Warner issued approximately 35.6 million shares of convertible preferred stock in connection with the ITOCHU/Toshiba Transaction and its acquisitions of KBLCOM, Summit and CVI. Set forth below is a summary of the principal terms of Time Warner's outstanding issues of preferred stock:

Description	Shares Outstanding (millions)	Number of Shares of Common Stock Issuable Upon Conversion (millions)	Effective Issuance Date	Earliest Exchange Date	Earliest Redemption Date
Series D Preferred Stock	11.0	22.9	7/6/95	7/6/99	7/6/00
Series E Preferred Stock	3.3	6.8	1/4/96	1/4/01	1/4/01
Series F Preferred Stock	3.0	6.4	1/4/96	1/4/00	1/4/01
Series G Preferred Stock	6.2	12.9	9/5/95	9/5/99	9/5/99
Series H Preferred Stock	1.8	3.7	9/5/95	9/5/00	9/5/99
Series I Preferred Stock	7.0	14.6	10/2/95	10/2/99	10/2/99
Series J Preferred Stock	3.3	6.8	5/2/95	5/2/98	5/2/00
Total shares outstanding at December 31, 1996	35.6	74.1			

The principal terms of each series of convertible preferred stock issued in 1996 and 1995 (the Series D Preferred Stock, the Series E Preferred Stock, the Series F Preferred Stock, the Series G Preferred Stock, the Series H Preferred Stock, the Series I Preferred Stock and the Series J Preferred Stock, and collectively, the "Convertible Preferred Stock") are similar in nature, unless otherwise noted below. Each share of Convertible Preferred Stock: (1) is entitled to a liquidation preference of \$100 per share, (2) is immediately convertible into 2,08264 shares of Time Warner common stock at a conversion price of \$48 per share (based on its liquidation value), except that shares of the Series H Preferred Stock are generally not convertible until September 2000, (3) entitles the holder thereof (i) to receive for a four-year period from the date of issuance (or a five-year period with respect to the Series E and Series J Preferred Stock) an annual dividend per share equal to the greater of \$3.75 and an amount equal to the dividends paid on the Time Warner common stock into which each share may be converted and (ii) to the extent that any of such shares of preferred stock remain outstanding at the end of the period in which the minimum \$3.75 per share dividend is to be paid, the holders thereafter will receive dividends equal to the dividends paid on shares of Time Warner common stock multiplied by the number of shares into which their shares of preferred stock are convertible and (4) except for the Series H Preferred Stock which is generally not entitled to vote, entitles the holder thereof to vote with the common stockholders on all matters on which the common stockholders are entitled to vote, and each share of such Convertible Preferred Stock is entitled to two votes on any such matter.

Time Warner has the right to exchange each series of Convertible Preferred Stock for Time Warner common stock at the stated conversion price at any time on or after the respective exchange date. The Series J Preferred Stock is exchangeable by the holder beginning after the third year from its date of issuance and by Time Warner after the fourth year at the stated conversion price plus a declining premium in years four and five and no premium thereafter. In addition, Time Warner has the right to redeem each series of Convertible Preferred Stock, in whole or in part, for cash at the liquidation value plus accrued dividends, at any time on or after the respective redemption date.

In June 1996, Time Warner exchanged all outstanding shares of its Series B preferred stock having an aggregate liquidation value of \$69 million for approximately 1.7 million shares of Time Warner common stock.

Pursuant to Time Warner's shareholder rights plan, as amended, each share of Time Warner common stock has attached to it one right, which becomes exercisable in certain events involving the acquisition of 15% or more of the then outstanding common stock of Time Warner on a fully-diluted basis. Upon the occurrence of such an event, each right entitles its holder to purchase for \$150 the economic equivalent of common stock of Time Warner, or in certain circumstances, of the acquirer, worth twice as much. In connection with the plan, 8 million shares of preferred stock were reserved. The rights expire on January 20, 2004.

At December 31, 1996, Time Warner had reserved approximately 200 million shares of common stock for the conversion of its Convertible Preferred Stock, zero coupon convertible notes and other convertible securities, and for the exercise of outstanding options to purchase shares of common stock.

## 12. STOCK OPTION PLANS

Time Warner has various stock option plans under which Time Warner may grant options to purchase Time Warner common stock to employees of Time Warner and TWE. Such options have been granted to employees of Time Warner and TWE at, or in excess of, fair market value at the date of grant. Accordingly, in accordance with APB 25 and related interpretations, no compensation cost has been recognized for its stock option plans. Generally, the options become exercisable over a three-year vesting period and expire ten years from the date of grant. Had compensation cost for Time Warner's stock option plans been determined based on the fair value at the grant dates for all awards during 1995 and 1996 under those plans consistent with the method set forth under FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("FAS 123"), Time Warner's net loss and net loss per common share would have been increased to the pro forma amounts indicated below.

Years Ended December 31 in millions, except per share amounts	1996	1995
<b>Net loss</b>		
As reported	\$ (191)	\$ (166)
Pro forma	\$ (216)	\$ (178)
<b>Net loss per common share</b>		
As reported	\$ (1.04)	\$ (.87)
Pro forma	\$ (1.10)	\$ (.80)

FAS 123 is applicable only to stock options granted subsequent to December 31, 1994. Accordingly, since Time Warner's compensation expense associated with such grants would generally be recognized over a three-year vesting period, the initial impact of applying FAS 123 on pro forma net income is not representative of the potential impact on pro forma net income in future years, when the pro forma effect would be fully reflected.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions used for grants in 1996 and 1995, respectively: dividend yields of 1% in both periods, expected volatility of 21.7% and 22.3%, risk-free interest rates of 6.1% and 7.1%, and expected lives of 5 years in both periods. The weighted average fair value of an option granted during the year was \$11.55 (\$6.81, net of taxes) and \$11.95 (\$7.05, net of taxes) for the years ended December 31, 1996 and 1995, respectively. The weighted average exercise price and fair value of an option granted during the year at prices exceeding the market price of the stock on the date of grant are \$52.88 and \$8.87 (\$5.23, net of taxes), respectively.

A summary of stock option activity under all plans is as follows:

	Thousands of Shares	Weighted Average Exercise Price	
Balance at January 1, 1994	72,954	\$ 30.04	
Granted	8,071	37.85	
Exercised	(1,262)	23.55	
Cancelled	(152)	35.24	
Balance at December 31, 1994	77,611	\$ 30.75	
Granted	5,096	38.00	
Exercised	(3,721)	27.16	
Cancelled	(367)	35.80	
Balance at December 31, 1995	78,619	\$ 31.36	
Granted	9,460	43.30	
Exercised	(3,686)	26.91	
Assumed in connection with the TBS Transaction	13,713	26.40	
Cancelled	(238)	40.83	
Balance at December 31, 1996	97,867	\$ 31.97	
December 31 1996/1995/1994	1996	1995	1994
Exercisable	82,897	88,242	83,108
Available for future grants	8,032	7,884	8,849

The following table summarizes information about stock options outstanding at December 31, 1996:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding at 12/31/96 (Thousands)	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable at 12/31/96 (Thousands)	Weighted Average Exercise Price
Under \$17	2,688	3 years	\$12.85	2,688	\$12.85
\$17.00 to \$25.00	20,313	4 years	\$21.26	20,313	\$21.26
\$25.01 to \$35.00	25,873	5 years	\$29.58	25,568	\$29.53
\$35.01 to \$40.00	35,356	5 years	\$36.79	29,054	\$36.59
\$40.01 to \$45.00	11,412	8 years	\$42.08	4,824	\$42.05
\$45.01 to \$63.95	2,225	9 years	\$52.36	250	\$48.29
Total	97,867	5 years	\$31.97	82,897	\$30.22

For options exercised by employees of TWE, Time Warner is reimbursed for the amount by which the market value of Time Warner common stock on the exercise date exceeds the exercise price, or the greater of the exercise price or \$27.75 for options granted prior to the TWE capitalization on June 30, 1997. There were 30.3 million options held by employees of TWE at December 31, 1996, 22.8 million of which were exercisable.

### 13. BENEFIT PLANS

Time Warner and its subsidiaries have defined benefit pension plans covering substantially all domestic employees. Pension benefits are based on formulas that reflect the employees' years of service and compensation levels during their employment period. Qualifying plans are funded in accordance with government pension and income tax regulations. Plan assets are invested in equity and fixed income securities. Time Warner's common stock represents approximately 5% and 6% of plan assets at December 31, 1996 and 1995, respectively.

Pension expense included the following:

Years Ended December 31 (Millions)	1996	1995	1994
Service cost	\$ 48	\$ 29	\$ 34
Interest cost	64	53	50
Actual return on plan assets	(90)	(137)	(2)
Net amortization and deferral	37	89	(45)
Total	\$ 60	\$ 34	\$ 37



The status of funded pension plans is as follows:

December 31, (millions)	1996	1995
Accumulated benefit obligation (90% vested)	\$ 550	\$ 544
Effect of future salary increase	210	192
Projected benefit obligation	760	736
Plan assets at fair value	704	643
Projected benefit obligation in excess of plan assets	(56)	(93)
Unamortized actuarial losses	2	94
Unamortized plan changes	3	2
Other	(2)	(10)
Accrued pension expense	\$ (53)	\$ (7)

The following assumptions were used in accounting for pension plans:

	1996	1995	1994
Weighted average discount rate	7.75%	7.25%	8.5%
Return on plan assets	9%	9%	9%
Rate of increase in compensation	6%	6%	6%

Employees of Time Warner's operations in foreign countries participate to varying degrees in local pension plans, which in the aggregate are not significant.

Time Warner also has certain defined contribution plans, including savings and profit sharing plans, as to which the expense amounted to \$67 million in 1996, \$51 million in 1995 and \$51 million in 1994. Contributions to the savings plans are based upon a percentage of the employees' elected contributions. Contributions to the profit sharing plans are generally determined by management and approved by the board of directors of the participating companies.

#### 14. FINANCIAL INSTRUMENTS

The carrying value of Time Warner's financial instruments approximates fair value, except for differences with respect to long-term, fixed-rate debt and related interest rate swap contracts and certain differences related to cost method investments and other financial instruments which are not significant. The fair value of financial instruments, such as long-term debt and investments, is generally determined by reference to market values resulting from trading on a national securities exchange

or in an over-the-counter market. In cases where quoted market prices are not available, such as for derivative financial instruments, fair value is based on estimates using present value or other valuation techniques.

**Interest Rate Risk Management** Interest rate swap contracts are used to adjust the proportion of total debt that is subject to variable and fixed interest rates. Under interest rate swap contracts, the Company either agrees to pay an amount equal to a specified floating rate of interest times a notional principal amount, and to receive in return an amount equal to a specified fixed rate of interest times the same notional principal amount or, vice versa, to receive a floating rate amount and to pay a fixed-rate amount. The notional amounts of the contracts are not exchanged. No other cash payments are made unless the contract is terminated prior to maturity, in which case the amount paid or received in settlement is established by agreement at the time of termination, and usually represents the net present value, at current rates of interest, of the remaining obligations to exchange payments under the terms of the contract. Interest rate swap contracts are entered into with a number of major financial institutions in order to minimize credit risk.

The net amounts paid or payable, or received or receivable, through the end of the accounting period are included in interest expense. Because interest rate swap contracts are used to modify the interest characteristics of Time Warner's outstanding debt from a fixed to a floating rate basis or, vice versa, unrealized gains or losses on interest rate swap contracts are not recognized in income unless the contracts are terminated prior to their maturity. Gains or losses on any contracts terminated early are deferred and amortized to income over the remaining average life of the terminated contracts.

At December 31, 1996, Time Warner had interest rate swap contracts to pay floating rates of interest (average six-month LIBOR rate of 5.7%) and receive fixed rates of interest (average rate of 5.5%) on \$2.3 billion notional amount of indebtedness, which resulted in approximately 47% of Time Warner's underlying debt, and 43% of the debt of Time Warner and the Entertainment Group combined, being subject to variable interest rates. The notional amount of outstanding contracts by year of maturity at December 31, 1996 is as follows: 1998-\$700 million; 1999-\$1.2 billion; and 2000-\$400 million. At December 31, 1995, Time Warner had interest rate swap contracts on \$2.6 billion notional amount of indebtedness.

Based on the level of interest rates prevailing at December 31, 1996, the fair value of Time Warner's fixed-rate debt exceeded its carrying value by \$231 million and it would have cost \$43 million to terminate the related interest rate swap contracts, which combined is the equivalent of an unrealized loss of \$274 million. Based on the level of interest rates prevailing at December 31, 1995, the fair value of Time Warner's fixed-rate debt exceeded its carrying value by \$407 million and it would have cost \$9 million to terminate its interest rate swap contracts, which combined was the equivalent of an unrealized loss of \$416 million. Unrealized gains or losses on debt or interest rate swap contracts are not recognized for financial reporting purposes unless the debt is retired or the contracts are terminated prior to their maturity.

Changes in the unrealized gains or losses on interest rate swap contracts and debt do not result in the realization or expenditure of cash unless the contracts are terminated or the debt is retired. However, based on Time Warner's variable rate debt and related interest rate swap contracts outstanding at December 31, 1996, each 25 basis point increase or decrease in the level of interest rates would, respectively, increase or decrease Time Warner's annual interest expense and related cash payments by approximately \$16 million, including \$6 million related to interest rate swap contracts. Such potential increases or decreases are based on certain simplifying assumptions, including a constant level of variable-rate debt and related interest rate swap contracts during the period and for all maturities, an immediate, across-the-board increase or decrease in the level of interest rates with no other subsequent changes for the remainder of the period.

**Foreign Exchange Risk Management** Foreign exchange contracts are used primarily by Time Warner to hedge the risk that unremitted or future royalties and license fees owed to Time Warner or TWE 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. As part of its overall strategy to manage the level of exposure to the risk of foreign currency exchange rate fluctuations, Time Warner hedges a portion of its and TWE's combined foreign currency exposures anticipated over the ensuing twelve month period. At December 31, 1996, Time Warner has effectively hedged approximately half of the combined estimated foreign currency exposures that principally relate to anticipated cash flows to be remitted to the U.S. over the ensuing twelve month period, using

foreign exchange contracts that generally have maturities of three months or less, which are generally rolled over to provide continuing coverage throughout the year. Time Warner often closes foreign exchange contracts by purchasing an offsetting purchase contract. At December 31, 1996, Time Warner had contracts for the sale of \$447 million and the purchase of \$104 million of foreign currencies at fixed rates, primarily English pounds (21% of net contract value), German marks (19%), Canadian dollars (18%), French francs (15%) and Japanese yen (19%), compared to contracts for the sale of \$504 million and the purchase of \$140 million of foreign currencies at December 31, 1995.

Unrealized gains or losses related to foreign exchange contracts are recorded in income as the market value of such contracts change; accordingly, the carrying value of foreign exchange contracts approximates market value. The carrying value of foreign exchange contracts was not material at December 31, 1996 and 1995 and is included in other current liabilities. No cash is required to be received or paid with respect to such gains and losses until the related foreign exchange contracts are settled, generally at their respective maturity dates. For the years ended December 31, 1996, 1995 and 1994, Time Warner recognized \$15 million in gains, \$20 million in losses and \$33 million in losses, respectively, and TWE recognized \$6 million in gains, \$11 million in losses and \$20 million in losses, respectively, on foreign exchange contracts, which were or are expected to be offset by corresponding decreases and increases, respectively, in the dollar value of foreign currency royalties and license fee payments that have been or are anticipated to be received in cash from the sale of U.S. copyrighted products abroad. Time Warner reimburses or is reimbursed by TWE for contract gains and losses related to TWE's foreign currency exposure. Foreign currency contracts are placed with a number of major financial institutions in order to minimize credit risk.

Based on the foreign exchange contracts outstanding at December 31, 1996, each 5% devaluation of the U.S. dollar as compared to the level of foreign exchange rates for currencies under contract at December 31, 1996 would result in approximately \$22 million of unrealized losses and \$5 million of unrealized gains on foreign exchange contracts involving foreign currency sales and purchases, respectively. Conversely a 5% appreciation of the U.S. dollar would result in \$22 million of unrealized gains and \$5 million of unrealized losses, respectively. At December 31, 1996, none of Time Warner's foreign



exchange purchase contracts relates to TWE's foreign currency exposure. However, with regard to the \$22 million of unrealized losses or gains on foreign exchange sale contracts, Time Warner would be reimbursed by TWE, or would reimburse TWE, respectively, for approximately \$5 million related to TWE's foreign currency exposure. Consistent with the nature of the economic hedge provided by such foreign exchange contracts, such unrealized gains or losses would be offset by corresponding decreases or increases, respectively, in the dollar value of future foreign currency royalty and license fee payments that would be received in cash within the ensuing twelve month period from the sale of U.S. copyrighted products abroad.

#### 16. SEGMENT INFORMATION

Time Warner classifies its businesses into four fundamental areas: Entertainment, consisting principally of interests in recorded music and music publishing, filmed entertainment, television production, television broadcasting and theme parks; Cable Networks, consisting principally of interests in cable television programming and sports franchises; Publishing, consisting principally of interests in magazine publishing, book publishing and direct marketing; and Cable, consisting principally of interests in cable television systems. A majority of Time Warner's interests in filmed entertainment, television production, television broadcasting and theme parks, a portion of its interests in cable television programming and a majority of its cable television systems are held by the Entertainment Group. The Entertainment Group is not consolidated for financial reporting purposes.

Information as to the operations of Time Warner and the Entertainment Group in different business segments is set forth below. The operating results of Time Warner reflect the acquisitions of Summit effective as of May 2, 1995, KBLCOM effective as of July 6, 1995, CVI effective as of January 4, 1996 and TBS effective as of October 10, 1996. The operating results of the Entertainment Group reflect the formation of the TWE - Advance/Nowhouse Partnership effective as of April 1, 1995, the deconsolidation of Six Flags effective as of June 23, 1995 and consolidation of Paragon effective as of July 6, 1995. The operating results of Six Flags prior to June 23, 1995 are reported separately to facilitate comparability.

Years Ended December 31, (millions)	1996	1995	1994
<b>REVENUES</b>			
<b>Time Warner:</b>			
Publishing	\$ 4,117	\$ 3,722	\$ 3,433
Music	3,949	4,196	3,986
Cable Networks - TBS	680	-	-
Filmed Entertainment - TBS	455	-	-
Cable	909	172	-
Intersegment elimination	(46)	(23)	(23)
Total	<u>\$ 10,064</u>	<u>\$ 8,067</u>	<u>\$ 7,386</u>

<b>Entertainment Group:</b>			
<b>Filmed Entertainment -</b>			
Warner Bros.	\$ 5,648	\$ 5,078	\$ 4,484
Six Flags Theme Parks	-	227	557
<b>Broadcasting -</b>			
The WB Network	87	33	-
Cable Networks - HBO	1,763	1,607	1,913
Cable	3,851	3,094	2,742
Intersegment elimination	(488)	(410)	(287)
Total	<u>\$ 10,861</u>	<u>\$ 9,629</u>	<u>\$ 8,509</u>

Years Ended December 31, (millions)	1996	1995	1994
<b>OPERATING INCOME</b>			
<b>Time Warner:</b>			
Publishing	\$ 418	\$ 381	\$ 347
Music <sup>(1)</sup>	361	321	366
Cable Networks - TBS	99	-	-
Filmed Entertainment - TBS	8	-	-
Cable	75	(5)	-
Intersegment elimination	\$	-	-
Total	<u>\$ 986</u>	<u>\$ 697</u>	<u>\$ 713</u>

<b>Entertainment Group:</b>			
<b>Filmed Entertainment -</b>			
Warner Bros.	\$ 254	\$ 253	\$ 219
Six Flags Theme Parks	-	29	56
<b>Broadcasting -</b>			
The WB Network	(98)	(66)	-
Cable Networks - HBO	328	274	237
Cable	606	502	340
Total	<u>\$ 1,090</u>	<u>\$ 992</u>	<u>\$ 852</u>

(1) Includes pre-tax losses of \$85 million recorded in 1995 related to certain businesses and joint ventures owned by the Music division which were restructured or closed. The losses were primarily related to Warner Music Enterprises, one of the Company's former direct marketing efforts, and the write off of its related direct mail order assets that were not recoverable due to the closure of this business.

Years Ended December 31 (millions)	1996	1995	1994
<b>DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT</b>			
<b>Time Warner:</b>			
Publishing	\$ 71	\$ 59	\$ 47
Music	91	95	86
Cable Networks - TBS	20	-	-
Filmed Entertainment - TBS	2	-	-
Cable	123	27	-
<b>Total</b>	<b>\$ 307</b>	<b>\$ 181</b>	<b>\$ 133</b>
<b>Entertainment Group:</b>			
<b>Filmed Entertainment - Warner Bros.</b>			
	\$ 167	\$ 113	\$ 76
Six Flags Theme Parks	-	20	51
<b>Broadcasting - The WB Network</b>			
	-	-	-
Cable Networks - HBO	22	18	14
Cable	619	465	340
<b>Total</b>	<b>\$ 808</b>	<b>\$ 616</b>	<b>\$ 481</b>

Years Ended December 31 (millions)	1996	1995	1994
<b>AMORTIZATION OF INTANGIBLE ASSETS<sup>(1)</sup></b>			
<b>Time Warner:</b>			
Publishing	\$ 46	\$ 36	\$ 36
Music	292	274	268
Cable Networks - TBS	43	-	-
Filmed Entertainment - TBS	22	-	-
Cable	278	68	-
<b>Total</b>	<b>\$ 681</b>	<b>\$ 378</b>	<b>\$ 304</b>
<b>Entertainment Group:</b>			
<b>Filmed Entertainment - Warner Bros.</b>			
	\$ 125	\$ 124	\$ 135
Six Flags Theme Parks	-	11	28
<b>Broadcasting - The WB Network</b>			
	-	-	-
Cable Networks - HBO	-	1	6
Cable	311	308	309
<b>Total</b>	<b>\$ 436</b>	<b>\$ 444</b>	<b>\$ 478</b>

(1) Amortization includes all amortization relating to the acquisition of Warner Communications Inc. ("WCI") in 1989, the acquisition of the minority interest in American Television and Communications Corporation ("ATC") in 1992, the acquisitions of RBLCOM and Summit in 1995, the acquisitions of TBS and CW in 1996 and other business combinations accounted for by the purchase method.

Information as to the assets and capital expenditures of Time Warner and the Entertainment Group is as follows:

December 31 (millions)	1996	1995	1994
<b>ASSETS</b>			
<b>Time Warner:</b>			
Publishing	\$ 2,418	\$ 2,175	\$ 2,013
Music	7,478	7,828	7,672
Cable Networks - TBS	7,860	-	-
Filmed Entertainment - TBS	3,232	-	-
Cable	7,257	3,875	-
Entertainment Group <sup>(1)</sup>	5,814	5,734	5,350
Corporate <sup>(2)</sup>	1,005	2,520	1,681
<b>Total</b>	<b>\$ 35,064</b>	<b>\$ 22,132</b>	<b>\$ 16,716</b>
<b>Entertainment Group:</b>			
<b>Filmed Entertainment - Warner Bros.</b>			
	\$ 8,111	\$ 7,389	\$ 7,184
Six Flags Theme Parks	-	-	814
<b>Broadcasting - The WB Network</b>			
	67	63	-
Cable Networks - HBO	997	935	911
Cable	10,202	9,842	8,303
Corporate <sup>(2)</sup>	650	731	1,780
<b>Total</b>	<b>\$ 20,027</b>	<b>\$ 18,960</b>	<b>\$ 18,992</b>

(1) Entertainment Group assets represent Time Warner's investment in and amounts due to and from the Entertainment Group.

(2) Consists principally of cash, cash equivalents and other investments.

Years Ended December 31 (millions)	1996	1995	1994
<b>CAPITAL EXPENDITURES</b>			
<b>Time Warner:</b>			
Publishing	\$ 76	\$ 70	\$ 50
Music	142	121	108
Cable Networks - TBS	34	-	-
Filmed Entertainment - TBS	2	-	-
Cable	215	56	-
Corporate	12	19	6
<b>Total</b>	<b>\$ 481</b>	<b>\$ 266</b>	<b>\$ 164</b>
<b>Entertainment Group:</b>			
<b>Filmed Entertainment -</b>			
Warner Bros.	\$ 340	\$ 294	\$ 395
Six Flags Theme Parks	-	43	46
<b>Broadcasting -</b>			
The WB Network	2	-	-
Cable Networks - HBO	29	20	14
Cable <sup>(1)</sup>	1,348	1,293	778
Corporate	-	3	2
<b>Total</b>	<b>\$ 1,719</b>	<b>\$ 1,653</b>	<b>\$ 1,235</b>

(1) Cable capital expenditures were funded in part through collections on the U.S. WEST Note Receivable in the amount of \$169 million in 1996, \$602 million in 1995 and \$274 million in 1994 (Note 3). The U.S. WEST Note Receivable was fully collected during 1996.

Information as to Time Warner's operations in different geographical areas is as follows:

Years Ended December 31 (millions)	1996	1995	1994
<b>REVENUES</b>			
United States <sup>(1)</sup>	\$ 7,562	\$ 5,447	\$ 4,944
Europe	1,494	1,552	1,445
Pacific Rim	697	775	724
Rest of World	311	293	283
<b>Total</b>	<b>\$ 10,064</b>	<b>\$ 8,067</b>	<b>\$ 7,396</b>
<b>Operating Income</b>			
United States	\$ 732	\$ 457	\$ 494
Europe	184	158	108
Pacific Rim	12	57	74
Rest of World	38	25	37
<b>Total</b>	<b>\$ 966</b>	<b>\$ 697</b>	<b>\$ 713</b>

(1) Time Warner's revenues do not include the revenues of the Entertainment Group, which had report revenues of \$2.134 billion in 1996, \$1.882 billion in 1995 and \$1.683 billion in 1994, principally from the sale of filmed Entertainment products abroad.

December 31 (millions)	1996	1995	1994
<b>Assets</b>			
United States	\$ 31,999	\$ 19,301	\$ 13,961
Europe	1,886	1,797	1,717
Pacific Rim	692	628	636
Rest of World	487	406	402
<b>Total</b>	<b>\$ 35,064</b>	<b>\$ 22,132</b>	<b>\$ 16,716</b>

#### 10. COMMITMENTS AND CONTINGENCIES

Total rent expense amounted to \$192 million in 1996, \$174 million in 1995 and \$157 million in 1994. The minimum rental commitments under noncancelable long-term operating leases are: 1997-\$235 million; 1998-\$230 million; 1999-\$205 million; 2000-\$185 million; 2001-\$160 million and after 2001-\$1.151 billion.

Minimum commitments and guarantees under certain programming, licensing, artists, athletes, franchise and other agreements aggregated approximately \$3.8 billion at December 31, 1996, which are payable principally over a five-year period. Such amounts do not include the Time Warner General Partner guarantees of approximately \$5.4 billion of TWE debt.

Pending legal proceedings are substantially limited to litigation incidental to the businesses of Time Warner, alleged damages in connection with class action lawsuits and the pending litigation with the City of New York and Fox News Channel ("FNC") relating to the TBS Transaction and the carriage of FNC on Time Warner Cable's New York City cable television system. In the opinion of management, the ultimate resolution of these matters will not have a material effect on the financial statements of Time Warner.

## 17. RELATED PARTY TRANSACTIONS

In the normal course of conducting their businesses, Time Warner and its subsidiaries and affiliates have had various transactions with TWE and other Entertainment Group companies, generally on terms resulting from a negotiation between the affected units that in management's view results in reasonable allocations. Employees of TWE participate in various Time Warner medical, stock option and other benefit plans for which Time Warner charges TWE its allocable share of plan expenses, including administrative costs. In addition, Time Warner provides TWE with certain corporate support services for which it received a fee in the amount of \$69 million, \$64 million and \$60 million in 1996, 1995 and 1994, respectively. The corporate support services agreement expires on June 30, 1997, subject to the obligation of both parties to negotiate, in good faith, any extension thereto.

Time Warner's Cable division has management services agreements with TWE, pursuant to which TWE manages, or provides services to, the cable television systems owned by Time Warner. Such cable television systems also pay TWE for the right to carry cable television programming provided by TWE's cable networks.

Time Warner's Filmed Entertainment-TBS division has various service agreements with TWE's Filmed Entertainment-Warner Bros. division, pursuant to which TWE's Filmed Entertainment-Warner Bros. division provides certain management and distribution services for Time Warner's theatrical, television and animated product, as well as certain services for administrative and technical support.

Time Warner's Cable Networks-TBS division has license agreements with TWE, pursuant to which the cable networks have acquired broadcast rights to certain film and television product. In addition, Time Warner's Music division provides home videocassette distribution services to certain TWE operations, and certain TWE units place advertising in magazines published by Time Warner's Publishing division.

Time Warner and TWE entered into a credit agreement in 1994 that allows Time Warner to borrow up to \$400 million from TWE through September 15, 2000. Outstanding borrowings from TWE bear interest at LIBOR plus 1% per annum. Time Warner borrowed \$400 million in 1994 under the credit agreement.

In addition to transactions with TWE and other Entertainment Group companies, Time Warner has had transactions with the Columbia House Company partnerships, Cinamerica Theatres, L.P., Comedy Partners, L.P., Six Flags and other equity investees of Time Warner and the Entertainment Group, generally with respect to sales of product in the ordinary course of business.

## 18. ADDITIONAL FINANCIAL INFORMATION

Additional financial information with respect to cash flows is as follows:

Years Ended December 31 (in millions)	1996	1995	1994
Cash payments made:			
for interest	\$ 839	\$ 659	\$ 539
Cash payments made:			
for income taxes	382	302	389
Tax-related distributions:			
received from TWE	215	680	115
Income tax refunds received	44	24	60
Noncash dividends	122	-	-

During the years ended December 31, 1996, 1995 and 1994, Time Warner realized \$147 million, \$35 million and \$179 million, respectively, from the securitization of receivables. Noncash investing activities in 1996 included the \$6.2 billion acquisition of TBS and the \$904 million acquisition of CVI in exchange for capital stock (Note 2). Noncash investing and financing activities in 1995 included the \$1.4 billion acquisitions of KBLCOM and Summit in exchange for capital stock (Note 2), the \$1.36 billion acquisition of ITOCHU's and Toshiba's interests in TWE in exchange for capital stock and \$10 million in cash (Note 3) and the \$1.8 billion redemption of Time Warner's Reset Notes in exchange for other debt securities (Note 6).

Other current liabilities consist of:

December 31 (in millions)	1996	1995
Accrued expenses	\$ 1,410	\$ 972
Accrued compensation	351	337
Accrued income taxes	81	173
Deferred revenues	248	84
Total	\$ 2,090	\$ 1,566

## Report of Management

The accompanying consolidated financial statements have been prepared by management in conformity with generally accepted accounting principles, and necessarily include some amounts that are based on management's best estimates and judgments.

Time Warner maintains a system of internal accounting controls designed to provide management with reasonable assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly. The concept of reasonable assurance is based on the recognition that the cost of a system of internal control should not exceed the benefits derived and that the evaluation of those factors requires estimates and judgments by management. Further, because of inherent limitations in any system of internal accounting control, errors or irregularities may occur and not be detected. Nevertheless, management believes that a high level of internal control is maintained by Time Warner through the selection and training of qualified personnel, the establishment and communication of accounting and business policies, and its internal audit program.

The Audit Committee of the Board of Directors, composed solely of directors who are not employees of Time Warner, meets periodically with management and with Time Warner's internal auditors and independent auditors to review matters relating to the quality of financial reporting and internal accounting control, and the nature, extent and results of their audits. Time Warner's internal auditors and independent auditors have free access to the Audit Committee.



GERALD M. LEVIN  
Chairman and  
Chief Executive Officer



RICHARD D. PARSONS  
President



RICHARD J. BRESSLER  
Senior Vice President  
and Chief Financial Officer

## Report of Independent Auditors

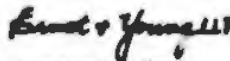
### THE BOARD OF DIRECTORS AND SHAREHOLDERS TIME WARNER INC.

We have audited the accompanying consolidated balance sheet of Time Warner Inc. ("Time Warner") as of December 31, 1996 and 1995, and the related consolidated statements of operations, cash flows and shareholders' equity for each of the three years in the period ended December 31, 1996. These financial statements are the responsibility of Time Warner's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the

accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Time Warner at December 31, 1996 and 1995, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1996, in conformity with generally accepted accounting principles.



New York, New York  
February 11, 1997

## Selected Financial Information

The selected financial information for each of the five years in the period ended December 31, 1996 set forth below has been derived from and should be read in conjunction with the financial statements and other financial information presented elsewhere herein. Capitalized terms are as defined and described in such consolidated financial statements, or elsewhere herein. The selected historical financial information for all periods after 1992 reflects the deconsolidation of the Entertainment Group, principally TWE, effective January 1, 1993.

The selected historical financial information for 1996 reflects (a) the issuance of approximately 173.4 million shares of common stock and the assumption of approximately \$2.8 billion of indebtedness in connection with the TBS Transaction, (b) the issuance of 1.6 million shares of Series M exchangeable preferred stock having an aggregate liquidation preference of \$1.6 billion and the use of approximately \$1.55 billion of net proceeds therefrom to reduce debt and (c)(i) the issuance of 6.3 million shares of convertible preferred stock having an aggregate liquidation preference of \$633 million and 2.9 million shares of common stock and (ii) the assumption or incurrence of

approximately \$2 billion of indebtedness, in connection with the acquisition of CVI. The selected historical financial information for 1995 reflects (a) the issuance of 29.3 million shares of convertible preferred stock having an aggregate liquidation preference of \$2.926 billion and 2.6 million shares of common stock and (b) the assumption or incurrence of approximately \$1.3 billion of indebtedness in connection with (x) the acquisitions of KBLCOM and Summit and (y) the exchange by Toshiba and ITOCHU of their direct and indirect interests in TWE. The selected historical financial information for 1993 reflects the issuance of \$6.1 billion of long-term debt and the use of \$500 million of cash and equivalents for the exchange or redemption of preferred stock having an aggregate liquidation preference of \$6.4 billion. The selected historical financial information for 1992 reflects the capitalization of TWE on June 30, 1992 and associated refinancings, and the acquisition of the 18.7% minority interest in ATC as of June 30, 1992, using the purchase method of accounting for business combinations.

Per common share amounts and average common shares have been restated to give effect to the four-for-one common stock split that occurred on September 10, 1992.

Years Ended December 31, (millions, except per share amounts)	1988	1993	1994	1993	1992
<b>Selected Operating Statement Information</b>					
Revenues	\$ 10,064	\$ 8,067	\$ 7,396	\$ 6,581	\$ 13,070
Depreciation and amortization	988	559	437	424	1,172
Business segment operating income <sup>(a)</sup>	966	697	713	591	1,343
Equity in pretax income of Entertainment Group	290	256	176	281	-
Interest and other, net	1,174	877	724	718	882
Income (loss) before extraordinary item	(156)	(124)	(91)	(164)	86
Net income (loss) <sup>(b)</sup>	(191)	(166)	(91)	(221)	86
Net loss applicable to common shares (after preferred dividends)	(448)	(218)	(104)	(339)	(542)
Per share of common stock:					
Net loss <sup>(c)</sup>	\$ (1.04)	\$ (0.57)	\$ (0.27)	\$ (0.90)	\$ (1.46)
Dividends	\$ 0.36	\$ 0.36	\$ 0.35	\$ 0.31	\$ 0.265
Average common shares	431.2	383.8	378.9	374.7	371.0

#### Selected Balance Sheet Information

Investments in and amounts due to and from Entertainment Group	\$ 5,814	\$ 5,734	\$ 5,350	\$ 5,627	\$ -
Total assets	35,064	22,132	16,716	16,892	27,366
Debt due within one year	11	34	355	120	171
Long-term debt	12,713	9,907	8,839	9,291	10,068
Borrowings against future stock option proceeds	488	-	-	-	-
Company-obligated mandatorily redeemable preferred securities of subsidiaries holding solely subordinated notes and debentures of the Company <sup>(a)</sup>	949	949	-	-	-
Series M exchangeable preferred stock	1,672	-	-	-	-
Shareholders' equity:					
Preferred stock liquidation preference	3,559	2,994	140	140	6,532
Equity applicable to common stock	5,943	673	1,008	1,230	1,635
Total shareholders' equity	9,502	3,667	1,148	1,370	8,167
Total capitalization	25,335	14,557	10,342	10,781	18,408

(a) Business segment operating income for the year ended December 31, 1995 includes \$85 million in losses relating to certain businesses and joint ventures owned by the Music Division which were restructured or closed.

(b) The net loss for the year ended December 31, 1998 includes an extraordinary loss on the retirement of debt of \$35 million (\$09 per common share). The net loss for the year ended December 31, 1985 includes an extraordinary loss on the retirement of debt of \$42 million (\$11 per common share). The net loss for the year ended December 31, 1993 includes an extraordinary loss on the retirement of debt of \$57 million (\$15 per common share) and an unusual charge of \$10 million (\$19 per common share) from the effect of the new income tax law on Time Warner's deferred income tax liability.

(c) Includes \$374 million of preferred securities that are redeemable for cash or, at Time Warner's option, approximately 18.1 million shares of Time Warner Inc. common stock owned by Time Warner.



## Quarterly Financial Information (continued)

(millions, except per share amounts)

Quarter	Revenues	Operating Income of Business Segments	Equity in Pre-tax Income of Entertainment Group	Net Income (Loss)	Net Income (Loss) Applicable to Common Shares <sup>(a)</sup>	Net Income (Loss) Per Common Share <sup>(b)</sup>	Dividends Per Common Share	Average Common Shares	Common Stock	
									High	Low
<b>1996<sup>(c)</sup></b>										
1st <sup>(d)</sup>	\$ 2,068	\$ 110	\$ 116	\$ (119)	\$ (153)	\$ (0.39)	\$ 0.09	391.7	\$ 45 1/4	\$ 37 1/4
2nd <sup>(d)</sup>	2,139	215	93	(40)	(110)	(0.28)	0.09	389.5	42 7/8	38 1/8
3rd	2,157	139	61	(91)	(167)	(0.43)	0.09	385.0	39 7/8	29 3/4
4th	3,700	502	20	59	(18)	(0.03)	0.09	558.7	42 1/4	36 1/2
Year <sup>(e)</sup>	10,064	966	290	(191)	(448)	(1.04)	0.36	431.2	45 1/4	29 3/4
<b>1995</b>										
1st	\$ 1,817	\$ 138	\$ 22	\$ (47)	\$ (50)	\$ (0.13)	\$ 0.09	379.5	\$ 39 1/4	\$ 33 5/8
2nd	1,907	184	84	(8)	(13)	(0.03)	0.09	381.4	43 1/2	34 1/4
3rd <sup>(f)</sup>	1,981	21	129	(144)	(160)	(0.41)	0.09	386.5	45 5/8	38 7/8
4th	2,362	354	21	33	5	0.01	0.09	387.5	41 1/4	35 3/4
Year <sup>(g)</sup>	8,067	697	256	(166)	(718)	(0.57)	0.36	383.8	45 5/8	33 5/8

(a) Quarterly financial information for 1996 reflects the acquisition by Time Warner of the remaining interest in TBS that it did not already own effective as of October 10, 1996.

(b) The net loss for the first quarter of 1996 includes an extraordinary loss on the retirement of debt of \$26 million (\$ 07 per common share). The net loss for the second quarter of 1996 includes an extraordinary loss on the retirement of debt of \$9 million (\$ 02 per common share).

(c) Business segment operating income for the third quarter of 1995 includes \$85 million in losses relating to certain businesses and joint ventures owned by the Music division which were restructured or closed. The net loss for the third quarter of 1995 includes an extraordinary loss on the retirement of debt of \$42 million (\$ 11 per common share).

(d) After preferred dividend requirements.

(e) Per common share amounts for the quarters and full years have been calculated separately. Accordingly, quarterly amounts may not add to the annual amount because of differences in the average common shares outstanding during each period.

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**FRANCIS T. VINCENT JR.**  
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Viacent Enterprises

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**JOSEPH J. COLLINS**  
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**JAMES H. BOODITTLE**  
President and CEO

# Investor Information

## COMMON STOCK INFORMATION

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### EXCHANGE LISTING

Time Warner (ticker symbol "TWX") is listed on the New York Stock Exchange.

### DIVIDEND REINVESTMENT AND STOCK PURCHASE PLAN

Holders of Time Warner common stock can obtain information about this plan by calling:

ChaseMellon Shareholder Services, L.L.C. at (800) 279-1238

### INDEPENDENT AUDITORS

Ernst & Young LLP

### TRANSFER AGENT

ChaseMellon Shareholder Services, L.L.C.  
81 Challenger Road  
Ridgefield Park, NJ 07660  
(800) 279-1238  
(212) 613-7427

### CORPORATE PUBLICATIONS

Copies of Time Warner's Form 10-K annual report, Annual Report, Form 10-Q quarterly reports and Social Responsibility Report are available without charge by writing or calling:

Shareholder Relations  
Time Warner Inc.  
75 Rockefeller Plaza  
New York, NY 10019  
(212) 484-0071

## FIXED INCOME INFORMATION

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### TIME WARNER COMPANIES, INC.

#### Debt Securities

7.45% Notes due 1998  
7.95% Notes due 2000  
Floating Rate Notes due 2000  
7.975% Notes due 2004  
7.75% Notes due 2005  
8.11% Debentures due 2006  
8.18% Debentures due 2007  
7.48% Debentures due 2008  
Liquid Yield Option™ Notes due 2012  
Liquid Yield Option™ Notes due 2013  
9 1/8% Debentures due 2013  
8.05% Debentures due 2016  
9.15% Debentures due 2023  
6.85% Debentures due 2026  
8.30% Discount Debentures due 2036

#### Mandatorily Redeemable Preferred Securities

4% Preferred Exchangeable Redemption Cumulative Securities of Time Warner Financing Trust due 1997  
8.875% Preferred Trust Securities of Time Warner Capital I due 2025

### TURNER BROADCASTING SYSTEM, INC.

7.4% Senior Notes due 2004  
8.375% Senior Notes due 2013  
8.4% Senior Debentures due 2024

### TWI CABLE INC.

10.5% Debentures of Summit Communications Group Inc. due 2005  
9.25% Senior Debentures of Cablevision Industries Inc. due 2008

### TIME WARNER ENTERTAINMENT COMPANY, L.P.

9 5/8% Senior Notes due 2002  
7 1/4% Senior Debentures due 2008  
8 7/8% Senior Notes due 2012  
10.15% Senior Notes due 2012  
8 3/8% Senior Debentures due 2023  
8 3/8% Senior Debentures due 2033

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First National Bank of Chicago

First National Bank of Chicago

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Chase Manhattan Bank  
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Executive portraits: James Salano (p. 3)  
Product/Studio Photography: Bart Wlosowski (pp. 4 & 17)

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