RADIO+TELEVISION BUSINESS REPORT™
THE FINANCIAL + REGULATORY VOICE OF ELECTRONIC MEDIA

The New Entercom: Not A Direct Asset Sale

By Adam R Jacobson on Feb, 2 2017
RBR + TVBR

The tax-free merger between the fourth-largest radio broadcasting company in the U.S. and **CBS Radio**, announced early Thursday (2/2), will give the newly enlarged **Entercom Communications** a presence in 23 of the top 25 markets. Closing is expected in the second half of 2017.

It creates a powerful player set to compete directly against **Cumulus Media** and **iHeartMedia** in key markets including Los Angeles, New York, Dallas-Fort Worth, San Francisco, Atlanta, and Washington, D.C.

RBR + TVBR crunched the numbers, and the transaction is valued at approximately $1.49 billion, based on the current value of Entercom shares — plus any assumed debt that Entercom will be assuming.

The deal with Entercom is not wholly unexpected, with rumors swirling as far back as May 2016. But, as one media broker notes, this transaction could only happen thanks to a rarely used maneuver that eliminates a tremendous tax bill — the “Reverse Morris Trust.”

In September 2016, **Bob Heymann,** Director of brokerage **Media Services Group**‘s Chicago office, told *RBR + TVBR* that a July 2016 Initial Public Offering for CBS Radio “put the kibosh on any spin-off.”

But, questions arose over direct inquiries received by CBS Corp. CEO Les Moonves regarding a potential sale.

At the time, Heymann suspected that CBS Radio would have difficulty attracting a serious buyer. That's because one drawback to a direct sale of assets, rather than a spin, was the tax bill. "The tax liabilities are very, very difficult to overcome in a direct sale of assets," he said.

There was one way a deal could happen, however. Enter the "Reverse Morris Trust." This type of transaction combines a spin-off with a statutory merger, allowing a tax-free transfer — in the guise of a merger — of a subsidiary under U.S. law.

Such deals are scarce, but have existed since 1966. **Procter & Gamble Co.** used a Reverse Morris Trust when it sold Folgers coffee to J.M. Smucker in 2008, and again in 2015 when it sold more than 40 health and beauty aid brands to Coty Inc.

In the media world, the Reverse Morris Trust is best-remembered as the key to a roughly $2.5 billion deal that saw **The Walt Disney Co.** spin off its ABC Radio O&Os and network to **Citadel Broacasting.** The deal was announced in Feb. 2006 but did not close until June 2007, as regulatory approval from the Department of Justice and FCC delayed closing.

The Reverse Morris Trust is what truly jumps out to Heymann.

"They are rare," he says.

Indeed, the only other instance where a Reverse Morris Trust has been noted in the media industry has involved Liberty Media and **Sirius XM Radio**, when in 2012 Bloomberg reported that Liberty was interested in splitting off its Sirius stake as a separate entity and giving its stockholders the option to hold or sell their Sirius shares.

"Typically you don't have assets as fully depreciated as they could possibly be," Heymann says of CBS Radio's AMs and FMs. "This means that, based on whatever sales price can be reached, it is all gain … and all taxable. That's what led them to choose this method, to avoid taxes. It's not all capital gains, but it is a very large percentage of the sale price."

The "huge tax burden" is also why practically everybody thought an IPO for CBS Radio was a foregone conclusion. By late November, **Matthew Siegel** had recently joined CBS Radio as CFO after a lengthy tenure at Time Warner Cable. **Scott Herman**, a CBS veteran, was already expected to continue serve as COO at the newly spun CBS Radio, as he had since July 2015.

Furthermore, **Stefan Selig** and **Sean Cramer** were announced as nominees to the CBS Radio Board of Directors, with each sitting on the board with President Andre Fernandez once the CBS Radio initial public offering was made.

This will no longer happen, given the merger with Entercom. The ticker symbol "CBSR" will also not be seen on the New York Stock Exchange, as CBS Corp. stated in a Form S-1 for registration in December 2016.

BEHIND THE DOLLARS

As noted by Entercom, which has taken the lead in informing consumers and clients about its tax-free merger with CBS Radio and has already updated its corporate website homepage, the combined companies' pro forma revenue on a trailing 12-month basis was approximately $1.7 billion.

This makes the new Entercom the second-largest radio station owner in the U.S., based on revenue.

Adjusted EBITDA is expected to be $468 million, before expected transaction synergies. An *RBR* + *TVBR* analysis determined that the bulk of this EBITDA is attributable to CBS Radio, as Entercom saw net income before income taxes of $47.6 million in fiscal 2015 — putting CBS Radio's net income before taxes at roughly $450 million.

Additionally, the two entities will see pro forma leverage of approximately 4.0x net debt — an excellent position for a radio company, given the high leverage seen by other high-profile publicly traded companies.

"The merger will create a well-capitalized company with a market cap of over $2 billion, a strong balance sheet, significant free cash flow generation, and an attractive dividend — positioned to drive shareholder value," Entercom said in an official release.

With the use of a Reverse Morris Trust, CBS shareholders will have the opportunity to exchange an amount of CBS shares their discretion (all, some or none) for CBS Radio shares. Immediately after the completion of this exchange offer, CBS Radio will engage in its merger with an Entercom subsidiary. The new CBS Radio shareholders will then receive Entercom shares in exchange for their CBS Radio shares.

Once the merger is done, **CBS Radio shareholders will receive approximately 105 million Entercom shares** (valued at $1.49 million, based on the opening price on Feb. 2), or 72% of all outstanding shares of the combined company on a fully diluted basis. Existing Entercom shareholders will own 28% of the combined company on a fully diluted basis.

The transaction is subject to approval by Entercom shareholders, and — to little surprise — Entercom Chairman **Joseph M. Field**, a controlling shareholder of Entercom, has agreed to vote in favor of the transaction.

‘TRANSFORMATIVE DEAL’ DISCUSSED BY KEY EXECS

In a pre-Opening Bell conference call, President/CEO **David Field** said the combination of Entercom and CBS Radio “is truly a transformational event” — labeling the tax-free merger as “a game-changing transaction.”

He said, “The merger will create a leading local media and entertainment company with the scale to compete much more effectively with other media for a larger share of advertising dollars … creating a preeminent radio platform.”

Field was joined by Entercom CFO Steve Fisher and COO **Weezie Kramer**, and CBS Radio COO **Scott Herman,** on the call.

Kramer exuded positives regarding the deal. She said, “When you combine CBS Radio’s Top 25 market footprint, their sports and news, digital and event platforms, with Entercom’s singular focus and belief in radio — and then add in our culture, our systems, our process and our local approach — the alchemy is ‘crazy good.'”

Kramer spent a decade at CBS Radio before joining Entercom, and spoke positively of the “great people and brands” at her former employer. This gives her the confidence that “mashing up” the companies will be highly beneficial for Entercom, creating a better place to work. “I could not be more fired up about the opportunity,” she added.

Herman added that he has been in radio for nearly 40 years, and “could not imagine a more strategic fit” than combining Entercom with CBS Radio. “Both companies are best-in-class in so many areas, and it will reunite CBS Radio will so many markets that were once part of our group.”

With the merger, Field will take the title of Chairman/CEO at Entercom. The company plans to nominate five directors to the Board, while CBS will nominate four directors. **Morgan Stanley & Co. LLC** and **Centerview Partners** are serving as financial advisors, and **Latham & Watkins LLP** is serving as legal counsel to Entercom. **Goldman, Sachs & Co.** is serving as financial advisor. **Wachtell, Lipton, Rosen & Katz** is serving as legal counsel to CBS Corp.

For Heymann, the deal is a great sign that the radio business is healthy, and continues to provide a strong platform for advertisers.

“You have a seller who wasn’t interested in owning radio but has a tremendous group of stations that is being bought by a pure radio group who loves radio,” he says. “That is a good thing for our industry.”

Read more at http://rbr.com/etm-cbsr-details/#rK4k36cfEWxMAdCT.99