

**ACME COMMUNICATIONS, Inc.**

**Quarterly Financial Report  
(unaudited)**

**September 30, 2012**

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**ACME Communications, Inc. and Subsidiaries**  
**Consolidated Balance Sheets**  
(In thousands, except share data)

	<b>September 30, 2012</b>	<b>December 31, 2011</b>
	<b>(unaudited)</b>	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 795	\$ 2,118
Restricted cash	---	50
Accounts receivable, net of allowance for doubtful accounts of \$365 and \$642 as of September 30, 2012 and December 31, 2011, respectively	3,739	3,589
Investments available-for-sale	---	1,269
Programming rights, current portion	1,561	2,011
Prepaid expenses and other current assets	109	696
Total current assets	6,204	9,733
Property and equipment, net	1,087	1,859
Programming rights, net of current portion	1,158	2,489
Goodwill, net	11,401	11,401
Broadcast licenses, net	3,100	3,359
Other assets	28	28
Total assets	\$ 22,978	\$ 28,869
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 804	\$ 1,296
Accrued liabilities	1,518	1,511
Programming rights payable, current portion	2,157	2,524
Obligations under capital lease, current portion	56	54
Other liabilities, current portion	80	613
Income taxes payable	353	362
Total current liabilities	4,968	6,360
Programming rights payable, net of current portion	1,199	3,001
Obligations under capital lease, net of current portion	557	599
Other liabilities, net of current portion	51	149
Deferred income taxes	---	2,030
Total liabilities	6,775	12,139
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.01 par value; 10,000,000 shares authorized, no shares issued or outstanding	---	---
Common stock, \$0.01 par value; 50,000,000 shares authorized, 16,046,763 shares issued and outstanding at September 30, 2012 and 16,772,415 and 16,046,763 shares issued and outstanding at December 31, 2011	161	168
Additional paid-in capital	128,011	133,004
Accumulated deficit	(111,969)	(111,515)
Accumulated other comprehensive income	---	73
Treasury stock, at cost; 725,652 shares	---	(5,000)
Total stockholders' equity	16,203	16,730
Total liabilities and stockholders' equity	\$ 22,978	\$ 28,869

See the accompanying notes to the unaudited consolidated financial statements.

**ACME Communications, Inc. and Subsidiaries**  
**Consolidated Statements of Operations and Comprehensive Income**  
(Unaudited)  
(In thousands, except per share data)

	<u>For the Three Months Ended</u> <u>September 30,</u>		<u>For the Nine Months Ended</u> <u>September 30,</u>	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Net revenues	\$ 4,491	\$ 3,451	\$ 11,805	\$ 14,528
Operating expenses:				
Cost of service:				
Programming, including program amortization	1,868	1,980	5,769	7,463
Other costs of service (excluding depreciation and amortization of \$125 and \$230 for the three months ended September 30, 2012 and 2011, respectively, and \$401 and \$869 for the nine months ended September 30, 2012 and 2011, respectively)	263	388	845	1,922
Selling, general and administrative expenses	880	1,041	2,895	4,770
Depreciation and amortization	125	230	401	869
Corporate expenses	226	307	717	1,111
Operating expenses	<u>3,362</u>	<u>3,946</u>	<u>10,627</u>	<u>16,135</u>
Operating income (loss)	1,129	(495)	1,178	(1,607)
Other expenses:				
Gain (loss) on disposal of assets	---	(10)	1,049	12,884
Interest expense	<u>(15)</u>	<u>(1)</u>	<u>(42)</u>	<u>(179)</u>
Income (loss) from discontinuing operations, before income taxes	1,114	(506)	2,185	11,098
Income tax benefit (expense)	2,049	74	2,022	(761)
Net income (loss)	<u>3,163</u>	<u>(432)</u>	<u>4,207</u>	<u>10,337</u>
Change in fair value on investment available-for-sale	---	(2,630)	(73)	(2,454)
Comprehensive income (loss)	<u>\$ 3,163</u>	<u>\$ (3,062)</u>	<u>\$ 4,134</u>	<u>\$ 7,883</u>
Net income (loss) per share, basic and diluted (discontinued):	\$ 0.20	\$ (0.03)	\$ 0.26	\$ 0.64
Weighted average basic and diluted common shares outstanding	<u>16,047</u>	<u>16,047</u>	<u>16,047</u>	<u>16,047</u>

See the accompanying notes to the unaudited consolidated financial statements.

**ACME Communications, Inc. and Subsidiaries**  
**Consolidated Statements of Stockholders' Equity**  
(Unaudited)  
(In thousands)

	<u>Common Stock</u>		<u>Additional Paid-in Capital</u>	<u>Accumulated Deficit</u>	<u>Accumulated Other Comprehensive Income</u>	<u>Treasury Stock</u>	<u>Total Stockholders' Equity</u>
	<u>Shares</u>	<u>Amount</u>					
Balance at December 31, 2011	16,772	\$ 168	\$ 133,004	\$ (111,515)	\$ 73	\$ (5,000)	\$ 16,730
Change in fair value on investment available-for-sale	---	---	---	---	(73)	---	(73)
Net income	---	---	---	4,207	---	---	4,207
Cancellation of treasury stock	(726)	(7)	(4,993)	---	---	5,000	---
Shareholder distribution	---	---	---	(4,661)	---	---	(4,661)
Balance at September 30, 2012	<u>16,046</u>	<u>\$ 161</u>	<u>\$ 128,011</u>	<u>\$ (111,969)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 16,203</u>

See the accompanying notes to the unaudited consolidated financial statements.

**ACME Communications, Inc. and Subsidiaries**  
**Consolidated Statements of Cash Flows**  
(Unaudited)  
(In thousands)

	<b>For the Nine Months Ended September 30,</b>	
	<b>2012</b>	<b>2011</b>
Cash flows from operating activities:		
Net income	\$ 4,207	\$ 10,337
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Provision for doubtful accounts receivable	114	66
Depreciation and amortization	401	869
Gain on disposal of assets	(1,049)	(12,884)
Amortization of program rights	1,269	2,691
Amortization of prepaid financing costs	---	41
Deferred income tax provision (benefit)	(2,030)	584
Changes in operating assets and liabilities:		
Restricted cash - litigation escrow	---	(3,225)
Accounts receivable	(264)	2,641
Prepaid expenses and other current assets	587	964
Other assets	(7)	8
Accounts payable	(492)	(1,130)
Accrued liabilities	7	(1,691)
Income taxes payable	(9)	(1,037)
Programming rights payable	(1,453)	(2,999)
Other liabilities	(631)	41
Net cash provided by (used in) operating activities	650	(4,724)
Cash flows from investing activities:		
Purchase of property and equipment	(26)	(25)
Proceeds from sale of property and equipment	---	(30)
Proceeds from sale of station assets	1,798	11,397
Net cash provided by in investing activities	1,772	11,342

See the accompanying notes to the unaudited consolidated financial statements.

**Consolidated Statements of Cash Flows - Continued**  
**(Unaudited)**  
**(In thousands)**

	<b>For the Nine Months Ended</b>	
	<b>September 30,</b>	
	<b>2012</b>	<b>2011</b>
Cash flows from financing activities:		
Borrowings under revolving credit facility	\$ ---	\$ 1,000
Repayments under revolving credit facility	---	(1,000)
Repayments of program deferrals	(225)	(2,700)
Payments on capital lease obligations	(40)	(40)
Cash restricted as escrow deposits	50	---
Cash distribution to shareholders	(3,530)	(5,616)
Net cash used in financing activities	(3,745)	(8,356)
Decrease in cash and cash equivalents		
Cash and cash equivalents at beginning of the period	(1,323)	(1,738)
Cash and cash equivalents at end of the period	2,118	593
Cash and cash equivalents at end of the period	\$ 795	\$ 593
Net cash payments (receipts) for:		
Interest	\$ (193)	\$ 104
Taxes	\$ (268)	\$ 18
Non-cash transactions:		
Program rights in exchange for program rights payable	\$ 370	\$ 159
Shareholder distribution of LIN TV Corp. stock	\$ 1,269	\$ ---
	\$ 1,639	\$ 159

See the accompanying notes to the unaudited consolidated financial statements.

**ACME Communications, Inc. and Subsidiaries**  
**Notes to Consolidated Financial Statements**  
**(Unaudited)**

**1. NATURE OF BUSINESS**

The Company commenced operations in 1997 and ACME Communications, Inc. was formed as the Company's holding company on July 23, 1999, in preparation for and in conjunction with an initial public offering of its stock.

ACME Communications, Inc. (together with its subsidiaries, hereinafter, individually and collectively, "ACME" or the "Company") is a holding company with no independent operations other than through its indirect wholly-owned subsidiary, ACME Television, LLC ("ACME Television"). As of September 30, 2012, ACME Television, through its wholly-owned subsidiaries, owned and operated the following three commercially-licensed, full-power, broadcast television stations located in the Albuquerque-Santa Fe marketplace, including KRWB in Roswell, New Mexico, the Company's satellite station of KWBQ:

<u>Station - Channel</u>	<u>Market</u>	<u>Market Ranking</u> <u>(1)</u>	<u>Network Affiliation</u> <u>(2)</u>
KWBQ - 29 / KRWB - 21	Albuquerque – Santa Fe, NM	45	CW
KASY - 45	Albuquerque – Santa Fe, NM	45	MNT

- (1) based on television households per Nielsen Market Research for the 2011/2012 broadcast season.
- (2) "CW" refers to The CW Television Network and "MNT" refers to MyNetworkTV.

In addition to the above named television stations, the Company also owns The Daily Buzz, LLC, which produces the weekday morning news and lifestyle television program *The Daily Buzz*, a nationally syndicated program which airs in 179 television markets covering approximately 73% of the country.

Effective November 4, 2008, the Company's common stock was delisted from the Nasdaq Global Market and on that same day the Company filed a Form 15 with the U.S. Securities & Exchange Commission ("SEC") to deregister its common stock under Section 12 of the Securities Exchange Act of 1934. Upon the filing of the Form 15, the Company's obligation to file certain reports with the SEC, including Forms 10-K, 10-Q, and 8-K, was immediately suspended. The deregistration of the Company's common stock became effective February 1, 2009. The Company's common stock is currently quoted on the Pink Sheets®, a centralized electronic quotation service for over-the counter securities.

***Sale of Stations and Other Events***

On February 21, 2012, the Company completed its sale of station WBUW in Madison, WI to Byrne Acquisition Group, LLP (Byrne) for approximately \$1.8 million in cash.

On March 22, 2012, the Company's Board of Directors approved a special distribution to its shareholders of record as of April 4, 2012 in the form of a cash distribution of \$.22 per common share which amounted to approximately \$3,530,000 and the remaining 300,000 shares of LIN unregistered common stock (.018695 shares of LIN unregistered common stock per every common share of the Company's stock) received in connection with LIN's purchase of the Company's television stations in Dayton and Green Bay-Appleton. Both, the cash distribution and LIN stock distribution were paid and distributed on April 10, 2012.

On December 10, 2012, the Company completed the sale of its New Mexico stations, KWBQ, its satellite station KRWB and KASY to Tamer Media and LIN Media for approximately \$19.0 million in cash.

On December 10, 2012, the Company's Board of Directors approved a special distribution to its shareholders of record as of December 14, 2012 in the form of a cash distribution of \$.93 per common share and also approved a formal plan of liquidation. The cash distribution which amounted to approximately \$14,923,490 was paid on December 21, 2012.



## ***Discontinued Operations***

The Company sold eight of its stations – KPLR (St. Louis), KWBP (Portland, OR), KUWB (Salt Lake City), WTVK (Ft. Myers-Naples) and WBUI (Champagne-Springfield-Decatur, IL) in previous periods, including WBXX (Knoxville, TN) and both the WBDT (Dayton, OH) and WCWF (Green Bay, WI) stations on May 6, 2011 and May 20, 2011, respectively.

In February 2012, the Company sold WBUW (Madison, WI) and in December 2012, the Company sold its remaining television stations KWBQ and its satellite station KRWB, and KASY (Albuquerque-Santa Fe, NM) – also see Note 1 above “*Sale of Stations and Other Events*”.

In accordance with accounting principles generally accepted in the United States of America, the accompanying Consolidated Statements of Operations and Cash Flows reflect now the results of these television stations and the Company’s remaining operation pursuant to the approved plan of liquidation as discontinued for all periods presented.

## **2. BASIS OF PRESENTATION**

### ***Basis of Consolidation***

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, including The Daily Buzz, LLC. All significant intercompany accounts and transactions have been eliminated for all periods presented. Segment information is not presented since all of the Company’s revenues are attributed to a single reportable segment.

### ***Presentation of Interim Financial Statements***

The accompanying consolidated financial statements for the three months and nine months ended September 30, 2012 and 2011 are unaudited and have been prepared in accordance with accounting principles generally accepted in the United States of America. As of and for the three and nine months ended September 30, 2012 all operations are considered “*Discontinued Operations*”.. In the opinion of management, such consolidated financial statements include all adjustments (consisting of normal recurring accruals) considered necessary for the fair presentation of the financial position and the results of operations, and cash flows for these periods. These consolidated financial statements do not include all disclosures and footnotes normally included with annual consolidated financial statements, and accordingly, should be read in conjunction with the consolidated financial statements, and the notes thereto, included in the Company’s 2011 Annual Report, which can be found on the Company’s website at [www.acmecommunications.com](http://www.acmecommunications.com). The results of operations presented in the accompanying consolidated financial statements are not necessarily indicative of the results that may be expected for the year ending December 31, 2012.

The accompanying consolidated balance sheet as of December 31, 2011 is derived from the audited consolidated financial statements included in the Company’s 2011 Annual Report.

In accordance with the Financial Accounting Standards Board (the “FASB”) *Accounting Standards Codification*<sup>TM</sup> (“ASC”) Topic 855, *Subsequent Events*, or ASC 855, the Company evaluated all events or transactions that occurred after December 11, 2012 through December 21, 2012, which represents the date the consolidated financial statements were available to be issued.

### ***Recent Accounting Pronouncements***

In May 2011, the FASB issued Accounting Standards Update (“ASU”) No. 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS*. This update clarifies the application of certain existing fair value measurement guidance and expands the disclosures for fair value measurements that are estimated using significant unobservable (Level 3) inputs. This update is effective on a prospective basis for annual and interim reporting periods beginning on or after December 15, 2011, which for the Company is January 1, 2012. Adopting this update did not have a material impact on the Company’s Consolidated Financial Statements.

In June 2011, the FASB issued ASU No. 2011-05, *Comprehensive Income (Topic 220)*. This update (1) eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity; (2) requires the consecutive presentation of the statement of net income and other comprehensive income; and (3) requires an entity to present reclassification adjustments on the face of the financial statements from other comprehensive income to net income. This update does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income nor does the update affect how earnings per share is calculated or presented. This update is required to be applied retrospectively and is effective for fiscal years and interim periods within those years beginning after December 15, 2011, which for the Company is January 1, 2012. In December 2011, the FASB issued ASU No. 2011-12, *Comprehensive Income (Topic 220)*. The amendment for this update is temporary and supersedes certain pending paragraphs in ASU No. 2011-05 to effectively defer only those changes in ASU No. 2011-05 that relate to the presentation of reclassification adjustments out of accumulated other comprehensive income until the FASB has time to reconsider these reclassification requirements. Since ASU No. 2011-05 and No. 2011-12 only pertain to enhanced disclosures adopting these updates did not have a material impact on the Company's Consolidated Financial Statements.

In September 2011, the FASB issued ASU No. 2011-08, *Testing Goodwill for Impairment (Topic 350)*, to simplify how entities test goodwill for impairment. The amendments permit an entity to first assess qualitative factors to determine whether it is more likely than not (that is, a likelihood of more than 50 percent) that the fair value of a reporting unit is less than its carrying amount. If this is the case, the entity will need to perform a more detailed two-step goodwill impairment test which is used to identify potential goodwill impairments and to measure the amount of goodwill impairment losses to be recognized, if any. The amendments are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011, with early adoption permitted. Adopting this update did not have a material impact on the Company's Consolidated Financial Statements.

### ***Critical Accounting Policies and Estimates***

The preparation of Consolidated Financial Statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements and the reported amounts of revenues and expenses during the reporting period. On an on-going basis, management evaluates its estimates, including those related to program rights, barter revenues, bad debts, intangible assets, including its broadcast licenses, investments, income taxes, and contingencies and litigation reserves. The Company bases its estimates on historical experience and on various other assumptions that they believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may materially differ from these estimates under different assumptions or conditions. In addition, changes in market conditions or stations' actual or expected performance could materially affect future estimated fair values of the Company's stations or of the estimated fair value of the Company's intangible assets, including the Company's broadcast licenses and goodwill. The Company's critical accounting policies are fully disclosed in the Company's 2011 Annual Report. There have been no material changes to these policies during the quarter ended September 30, 2012.

### **3. LONG-LIVED ASSETS, INCLUDING INTANGIBLES SUBJECT TO AMORTIZATION**

Long-lived assets consist of program rights and property and equipment.

#### ***Programming Rights***

Our programming rights are stated, on a gross basis, at the lower of amortized cost or estimated realizable value. Generally, programming rights are amortized over the life of the contract on a straight-line basis related to the usage of the program. Any reduction in unamortized costs to net realizable value is included in amortization of program rights in the accompanying consolidated statements of operations. We evaluate estimated realizable value of programming rights based on current usage and revenue performance and projected future revenue and usage of such programs. Changes in our programming schedule could impact the estimated realizable value of programming. In addition, estimates of future revenue performance relate to the number of advertising spots we sell and the amount generated from such sales. A decrease in the number of spots sold or the amount for such sales could also impact our estimated realizable value. There was no write-down of programming rights due to impairments during the nine-month periods ended September 30, 2012 and 2011.

## ***Property & Equipment***

Depreciation and amortization of our long-lived assets is provided using the straight-line method over their estimated useful lives. Changes in circumstances, such as the passage of new laws or changes in regulations, technological advances, changes to our business model or changes in our capital strategy could result in the actual useful lives differing from initial estimates. In those cases where we determine that the useful life of a long-lived asset should be revised, we will depreciate the net book value in excess of the estimated residual value over its revised remaining useful life. Factors such as changes in the planned use of equipment, customer attrition, contractual amendments or mandated regulatory requirements could result in shortened useful lives.

Long-lived assets and asset groups are evaluated for impairment whenever events or changes in circumstances indicate that their carrying value may not be recoverable. There were no impairment charges recorded during the nine-month periods ended September 30, 2012 and 2011.

## **4. GOODWILL AND INDEFINITE LIFE INTANGIBLE ASSETS**

In accordance with FASB ASC Topic 350-30, *Intangibles — Goodwill and Other*, Goodwill, or ASC 350-30, Goodwill and indefinite life intangible assets are not amortized but are tested annually for impairment, or more frequently if events or changes in circumstances indicate that the assets might be impaired. In assessing the recoverability of goodwill and indefinite life intangible assets, the Company must make assumptions about the estimated future cash flows and other factors to determine the fair value of these assets.

For goodwill, the impairment evaluation includes a comparison of the carrying value of the reporting unit (including goodwill) to that reporting unit's fair value. If the reporting unit's estimated fair value exceeds the reporting unit's carrying value, no impairment of goodwill exists. If the fair value of the reporting unit does not exceed the unit's carrying value, then an additional analysis is performed to allocate the fair value of the reporting unit to all of the assets and liabilities of that unit as if that unit had been acquired in a business combination and the fair value of the unit was the purchase price. If the excess of the fair value of the reporting unit over the fair value of the identifiable assets and liabilities is less than the carrying value of the unit's goodwill, an impairment charge is recorded for the difference.

Similarly, the impairment evaluation for indefinite life intangible assets includes a comparison of the asset's carrying value to the asset's fair value. When the carrying value exceeds fair value an impairment charge is recorded for the amount of the difference. An intangible asset is determined to have an indefinite useful life when there are no legal, regulatory, contractual, competitive, economic or any other factors that may limit the period over which the asset is expected to contribute directly or indirectly to the future cash flows of the Company. The Company also evaluates annually intangible assets that are not being amortized to determine whether events and circumstances continue to support an indefinite useful life. If an intangible asset that is not being amortized is determined to have a finite useful life, the asset will be amortized prospectively over the estimated remaining useful life and accounted for in the same manner as intangible assets subject to amortization. The annual impairment testing date is December 31. The Company will also test for impairment between annual test dates if an event occurs or circumstances change that would indicate the carrying amount may be impaired. Impairment testing for goodwill is performed at a reporting unit level. An impairment loss would generally be recognized when the carrying amount of the reporting unit's net assets exceeds the estimated fair value of the reporting unit.

Intangible assets with indefinite lives consist of FCC broadcast licenses and goodwill. There were no impairment charges recorded on the Company's FCC broadcast licenses and goodwill during the nine-month periods ended September 30, 2012 and 2011.

## **5. INVESTMENTS AVAILABLE-FOR-SALE**

Available-for-sale investments consist of equity securities, which are classified as available-for-sale securities. Available-for-sale securities are recorded at fair value and unrealized holding gains and losses are excluded from earnings and are reported as a separate component of comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. A decline in the market value of any available-for-sale security below cost that is deemed to be other-than-temporary results in a reduction in the carrying amount to fair value. Any resulting impairment is charged to other expense and a new cost basis for the security is established.

On April 10, 2012, as part of a special distribution to its shareholders, the Company distributed the remaining 300,000 shares of LIN unregistered common stock received in connection with LIN's purchase of the Company's television stations in Dayton and Green Bay-Appleton and accordingly at September 30, 2012 the Company did not have any investment available-for-sale. Also see Note 12 "*Accumulated Other Comprehensive Income*".

## **6. FAIR VALUE OF FINANCIAL INSTRUMENTS**

FASB ASC Topic 820, *Fair Value Measurements and Disclosures*, or ASC 820, applies to certain assets and liabilities that are being measured and reported on a fair value basis. Broadly, the ASC 820 framework requires fair value to be determined based on the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants. ASC 820 also establishes a fair value hierarchy for ranking the quality and reliability of the information used to determine fair values. This hierarchy is as follows:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

*Assets and Liabilities that are Measured at Fair Value on a Recurring Basis:*

Available-for-sale securities are recorded at fair value and unrealized holding gains and losses are excluded from earnings and are reported as a separate component of comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. A decline in the market value of any available-for-sale security below cost that is deemed to be other-than-temporary, results in a reduction in the carrying amount to fair value. Any resulting impairment is charged to other income (expense) and a new cost basis for the security is established.

Under the guidance of ASC 320, "*Investments*", the Company periodically evaluates other-than-temporary impairment (OTTI) of these securities to determine whether a decline in their value is other than temporary. Management utilizes criteria such as the magnitude and duration of the decline, in addition to the reasons underlying the decline, to determine whether the loss in value is other than temporary. Once a decline in value is determined to be other than temporary, the value of the security is reduced and a corresponding impairment charge to earnings is recognized.

*Assets and Liabilities that are Measured at Fair Value on a Nonrecurring Basis:*

Certain assets are measured at fair value on a nonrecurring basis. These assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments only in certain circumstances. Included in this category are goodwill written down to fair value when determined to be impaired, assets and long-lived assets including FCC broadcast licenses that are written down to fair value when they are held for sale or determined to be impaired. The valuation methods for goodwill, assets and liabilities resulting from business combinations, and long-lived assets involve assumptions concerning interest and discount rates, growth projections, and/or other assumptions of future business conditions. As all of the assumptions employed to measure these assets and liabilities on a nonrecurring basis are based on management's judgment using internal and external data, these fair value determinations are classified in Level 3 of the valuation hierarchy.

## **7. STOCK-BASED COMPENSATION**

FASB ASC Topic 718 *Compensation — Stock Compensation*, or ASC 718, requires companies to estimate the fair value of share-based payment awards on the date of grant using an option-pricing model. There were no stock options granted or any other type of share-based issuances during the nine-month periods ended September 30, 2012 and 2011.

There was no stock-based compensation expense for the nine-month periods ended September 30, 2012 and 2011 and as of September 30, 2012, there is no unrecognized compensation cost related to unvested stock options.

## 8. INCOME TAXES

The Company accounts for income taxes in accordance with FASB ASC Topic 740, *Income Taxes*, or ASC 740. Income taxes are provided based on current taxable income and the future tax consequences of temporary differences between the basis of assets and liabilities for financial and tax reporting. The deferred income tax assets and liabilities represent the future state and federal tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred income taxes are also recognized for operating losses that are available to offset future taxable income and tax credits that are available to offset future income taxes. At each reporting period, management assesses the realizable value of deferred tax assets based on, among other things, estimates of future taxable income, and adjusts the related valuation allowance as necessary. Management makes a number of assumptions and estimates in determining the appropriate amount of expense to record for income taxes. These assumptions and estimates consider the taxing jurisdiction in which the Company operates as well as current tax regulations. Accruals are established for estimates of tax effects for certain transactions and future projected profitability of the Company's businesses based on management's interpretation of existing facts and circumstances.

FASB Topic ASC 740, *Income Taxes*, or ASC 740, defines the threshold for recognizing the benefits of tax return positions in the financial statements as "more-likely-than-not" to be sustained by the taxing authority. A tax position that meets the "more-likely-than-not" criterion shall be measured at the largest amount of benefit that is more than 50% likely of being realized upon ultimate settlement. The Company has reviewed its tax positions and determined that an adjustment to the tax provision is not considered necessary nor is a reserve for income taxes required.

## 9. NOTES PAYABLE UNDER REVOLVING CREDIT FACILITY

The Company repaid and terminated its Revolving Credit Facility in May 2011 in connection with the sale of its WBXX station – see Note 1 "*Discontinued Operations*". Accordingly, at September 30, 2012, the Company had no outstanding amounts under its Revolver or any other borrowing arrangements.

## 10. BARTER AND TRADE TRANSACTIONS

Revenue and expenses associated with barter agreements in which broadcast time is exchanged for programming rights are recorded at the estimated average rate of the airtime exchanged, which the Company believes approximates fair value. Barter revenue amounted to \$283,000 and \$316,000, during the three-month periods ended September 30, 2012 and 2011, respectively. For the nine-months periods ended September 30, 2012 and September 30, 2011, barter revenue amounted to \$840,000 and \$1,353,000, respectively. Trade transactions, which represent the exchange of advertising time for goods or services, are recorded at the estimated fair value of the products or services received based on comparable cash transactions. Barter and trade revenue is recognized when advertisements are broadcast. Merchandise or services received from airtime trade sales are charged to expense or capitalized and expensed when used.

## 11. INCOME (LOSS) PER SHARE

Basic income (loss) per common share is computed by dividing net income (loss) to common stockholders by the weighted average number of common shares outstanding for the period. Diluted income (loss) per share includes the effect of our outstanding stock options, warrants and shares issuable pursuant to convertible debt, convertible preferred stock and certain stock incentive plans under the treasury stock method, if including such instruments is dilutive.

During the period ended September 30, 2012, 96,250 stock options expired or were forfeited. Our stock options outstanding at September 30, 2012 and 2011 were 682,500 and 784,500 shares respectively. Stock options were not included in the computation of diluted EPS for the periods ended September 30, 2012 and 2011 because an inclusion of such shares would have been anti-dilutive.

## 12. ACCUMULATED OTHER COMPREHENSIVE INCOME

Accumulated other comprehensive income is the combination of accumulated net unrealized gains or losses on investments available-for-sale - also see Note 6 "*Investments Available-for-sale*".

The carrying value of the Company's investment in LIN unregistered common stock has fluctuated and the respective unrealized gains and losses are recorded in accumulated other comprehensive income in the Company's Consolidated

Balance Sheets and Statement of Stockholders' Equity. As of September 30, 2012 the component of accumulated other comprehensive income is as follows:

	September 30, 2012	December 31, 2011
Unrealized gain on investment available for sale	\$ ---	\$ 73
Ending Balance	<u>\$ ---</u>	<u>\$ 73</u>

### 13. SUBSEQUENT EVENTS

The Company has completed an evaluation of all subsequent events through the date the consolidated financial statements were issued and concluded no subsequent events occurred that required recognition or disclosure other than those events discussed in Note 1 above "*Sale of Stations and Other Events*".

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## Management's Discussion and Analysis ("MD&A") of Financial Condition and Results of Operations

### **Forward Looking Statements**

*This Quarterly Report includes forward-looking statements. We have based these forward-looking statements on our current expectations and projections about future events. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "could," "expect," "believe," "should" or "might" or the negative of such terms or other comparable terminology. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our and the television broadcast industry's actual results, levels of activity, performance, achievements and prospects to be materially different from those expressed or implied by such forward-looking statements. Actual results in the future could differ materially and adversely from those described in the forward-looking statements as a result of various important factors, including (but not limited to) an inability to selectively sell our stations, an inability of The CW Network or MyNetworkTV to attract and grow viewership, the impact of changes in national and regional economies, including advertising demand, pricing fluctuations in local and national advertising, and volatility in programming costs and other risk factors.*

*These forward-looking statements speak only as of the date of this Quarterly Report. We undertake no duty to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, after the date of this Quarterly Report. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this Quarterly Report might not occur.*

### **Presentation of Financial Information in this MD&A**

The financial information and discussion contained in this MD&A for the three and nine-month periods ended September 30, 2012 and 2011 is unaudited and has not been read or reviewed by our independent public accountants. In the opinion of management, such financial information, however, includes all adjustments (consisting of normal recurring accruals) considered necessary for the fair presentation of the financial position and the results of operations, and cash flows for the periods presented. The information contained in the MD&A should be read in conjunction with our audited Consolidated Financial statements, and notes thereto, as of and for the years ended December 31, 2011 and 2010, included in the Company's 2011 Annual Report, which can be found on the Company's website at [www.acmecommunications.com](http://www.acmecommunications.com).

### **Overview**

This MD&A is provided as a supplement to our audited Consolidated Financial Statements and notes thereto, as discussed above, in order to enhance your understanding of our results of operations and financial condition. Our MD&A is organized as follows:

- *Introduction.* This section provides a general description of our Company and discussion about our operations.
- *Recent Developments and Sales of Stations.* This section provides a general description of our Company's recent developments including the sales of the Company's WBXX, Knoxville, TN (WBXX), WBDT, Dayton, OH (WBDT) and WCWF (formerly WIWB, Green Bay-Appleton, WI) television stations completed in 2011 and the sale of station WBUW, Madison, WI (WBUW), completed in February 2012 and our remaining television stations KWBQ, its satellite KRWB and KASY in December 2012.
- *Critical Accounting Policies and Estimates.* This section discusses those accounting policies that are considered important to the evaluation and reporting of our financial condition and results of operations, and whose application requires us to exercise subjective or complex judgments in making estimates and assumptions. In addition, all of our significant accounting policies, including our critical accounting policies, are summarized in Note 2 to our audited Consolidated Financial Statements, which are, as mentioned above, posted separately on our Company's website at [www.acmecommunications.com](http://www.acmecommunications.com).
- *Results of Operations.* This section provides our analysis and outlook for the significant line items on our Consolidated Statements of Operations, as well as other information that we deem meaningful to understand our results of operations, all presented on a discontinuing operations basis.

□ *Liquidity and Capital Resources.* This section provides an analysis of our liquidity and cash flows and discussions of our contractual obligations and commitments, as well as our outlook on our available liquidity as of September 30, 2012.

□ *Recent Accounting Pronouncements.* This section provides a summary of the most recent authoritative accounting standards and guidance that have either been recently adopted by our Company or may be adopted in the future.

As of September 30, 2012, our Company, ACME Communications, Inc. and its wholly-owned subsidiaries (together, unless the context otherwise requires, the "Company" or "we"), owned and operated three independently programmed broadcast television stations serving the Albuquerque-Santa Fe market: KWBQ (an affiliate of The CW Television Network) and KASY (an affiliate of MyNetworkTV), and KRWB, which is a satellite of KWBQ. In addition to our television stations, we also produce a three-hour weekday news and lifestyle morning program, *The Daily Buzz*, which airs on all of our stations and on television stations serving another 179 television markets representing approximately 73% of the country. In May 2011, we sold our stations WBXX, WBDT and WCWF and in February 2012, we sold our station WBUW and in December 2012 we sold our remaining stations, KWBQ, its satellite station KRWB and KASY, all serving the Albuquerque-Santa Fe, New Mexico market – also see “*Sale of Stations and Other Events*” below. All of our previously sold stations, our recently sold stations in New Mexico and our Production company have been treated as discontinued operations in our accompanying Consolidated Financial Statements and in this MD&A.

Since we reached a high of eleven television stations (not counting our satellite in Roswell) in 2002, we have been seeking to monetize shareholder value by the selective sale of our stations. As of September 30, 2012, we have sold all of our stations except those noted above and we continue to be sellers rather than buyers of television station assets. We will continue to market our remaining operating assets in order to maximize the values of those assets.

We derive revenues primarily from the sale of advertising time to local, regional and national advertisers and, to a lesser extent, from program licensing fees from other stations and distributors related to *The Daily Buzz*. At our KWBQ and KASY stations, Albuquerque-Santa Fe, NM we also receive retransmission consent fees. Our advertising revenues depend on popular programming that attracts audiences in the demographic groups targeted by advertisers, allowing us to sell advertising time at satisfactory rates. Similar to all commercial television stations, our rates are directly affected by the number of and demographic makeup of our viewing audience, as measured by Nielsen Media Research. Our revenues also depend significantly on factors such as the national and local economy and the level of local competition.

Approximately 65-75% of our advertising revenues are derived from programming that airs between the hours of 5:00 p.m. to midnight. Network prime time, which is a subset of this broad day part, accounts for 12-15% of our total revenues.

KWBQ, our CW affiliated station and KASY, our MyNetworkTV affiliated station, are ranked fifth and sixth, respectively, amongst English-language commercial television stations in the Albuquerque-Santa Fe marketplace in terms of both share of viewers or share of the market’s broadcast television revenue. In periods of lower advertising demand – as has been the case for the past two years - competition from market leaders, generally the ABC, CBS, NBC and FOX affiliated stations, increases as these stations become more aggressive in their pricing to maintain their revenue share. Over the past several years, biennial political spending in the even years has grown substantially. While we do not directly benefit in any significant way from this political advertising since most such advertising generally targets viewers older than our normal viewing audience, we indirectly benefit as the increased demand for political advertising reduces the overall inventory available to non-political advertisers in each market, which consequently increases the overall advertising price for such non-political advertisers.

Similar to the television advertising business in general, our revenues are usually greatest during the fourth quarter of each year, primarily due to increased expenditures by advertisers in anticipation of holiday season consumer spending and an increase in viewership during this period. We generally pay commissions to advertising agencies on local, regional and national advertising and to national sales representatives on national advertising. Our net revenues reflect deductions from gross revenues for commissions payable to advertising agencies and national sales representatives.

Under our shared services agreement with LIN Media, we incur management expenses for LIN’s management of our stations’ financial accounting and human resources functions and the management of our retransmission arrangements with satellite, cable and telco distributors. In 2012, we have begun receiving retransmission fees for our stations’ signals which has increased the stations’ overall revenues.



Our primary ongoing operating expenses are costs of services, selling, general and administrative expenses, corporate expenses, depreciation and amortization and expenses related to impairments in our broadcast licenses. Costs of services include programming costs, which consist primarily of amortization of programming rights relating to syndicated programs as well as costs associated with our morning news show, *The Daily Buzz*, and music rights fees. Other costs of service include advertising expenses targeted at viewers, which is net of any reimbursement received or due to us for such advertising and promotion from our networks or from other program suppliers, and engineering and transmission related expenses. Selling, general and administrative expenses primarily include salaries, sales commissions to account executives, ratings service expenses, insurance and various related overhead expenses. Corporate expenses reflect costs of corporate management, which includes senior management and other centralized management support staff, along with investor relations expenses, professional fees including but not limited to annual audit and legal expenses, directors and officers insurance and other related corporate overhead.

The national recession that began in the second half of calendar 2008 had an adverse impact on our industry and our Company during 2009, but advertising demand improved in our continuing markets in 2010 and we saw a slow recovery during 2011. Advertising demand was also adversely impacted by the earthquake and tsunami in Japan in March 2011 which adversely impacted production of automobiles and dramatically reduced advertising needs by Japanese importers. While advertising demand has been relatively stable over the past two years, it is clear that the recovery is tenuous and advertisers seem to be cautiously gauging advertising needs.

At the *Daily Buzz*, we replaced most all of our on-air talent at the end of June and the beginning of July this year and our new on-air talent debuted in August 2012. While we have not yet seen an increase in the show's Nielsen ratings, the reception by our television station affiliates for the new look and new talent has been positive.

### ***Sale of Stations and Other Events***

On May 6, 2011, we completed the sale of WBXX-TV, our station in Knoxville, TN to Lockwood Broadcast Group and on May 20, 2011, we completed the sale of WBDT-TV our Dayton, OH station and WCWF-TV (formerly WIWB-TV) our Green Bay, WI station to LIN Media. The aggregate sales price for the three stations was \$17.1 million.

The WBDT and WCWF sales reflected the exercise of an option by LIN, who had assigned certain purchase rights for WBDT to WBDT Television, LLC. LIN exercised its right under the Option Agreement to pay approximately 50% of the combined purchase price with its common stock and issued 1,150,000 unregistered shares.

In connection with the WBXX sale on May 6, 2011, we repaid and terminated our Revolving Credit Facility.

On June 13, 2011, the Company's Board of Directors approved a special distribution to its shareholders of record as of June 30, 2011 in the form of a cash distribution of \$.35 per common share. The distribution was paid on July 14, 2011.

On February 21, 2012, we completed our sale of station WBUW in Madison, WI to Byrne for approximately \$1.8 million in cash.

On March 22, 2012, our Board of Directors approved a special distribution to our shareholders of record as of April 4, 2012 in the form of a cash distribution of \$.22 per common share which amounted to approximately \$3,530,000 and the remaining 300,000 shares of LIN unregistered common stock (.018695 shares of LIN unregistered common stock per every common share of the Company's stock) received in connection with LIN's purchase of our television stations in Dayton and Green Bay-Appleton. Both, the cash distribution and LIN stock distribution were paid and distributed on April 10, 2012.

On December 10, 2012, we completed the sale of our New Mexico stations, KWBQ, its satellite station KRWB and KASY to Tamer Media and LIN Media for approximately \$19.0 million in cash.

On December 10, 2012, our Board of Directors approved a special distribution to our shareholders of record as of December 14, 2012 in the form of a cash distribution of \$.93 per common share and also approved a formal plan of liquidation. The cash distribution which amounted to approximately \$14,923,490 was paid on December 21, 2012.

## ***Critical Accounting Policies and Estimates***

Our discussion and analysis of our financial condition and results of operations are based upon our Consolidated Financial Statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of these Consolidated Financial Statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to program rights, barter revenues, bad debts, intangible assets, including our broadcast licenses and goodwill, investments, income taxes, and contingencies and litigation reserves. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may materially differ from these estimates under different assumptions or conditions.

## ***Results of Operations***

### *Three Months Ended September 30, 2012 Compared to September 30, 2011*

Net revenues from operations for the third quarter of 2012 were \$4.5 million, an increase of 30%, or \$1.0 million, compared to net revenues of \$3.5 million in the third quarter of 2011 mainly due to stronger advertising demand and significant growth in our retransmission fees at our television stations, and the recognition of previously deferred licensing revenue at the Daily Buzz.

Programming expenses were \$1.9 million for the third quarter of 2012, a decrease of 6%, or \$112,000, compared to \$2.0 million in the third quarter of 2011. The decrease relates primarily to the fact that the third quarter of 2011 still included amortization expense for our WBUW station which was sold in February of 2012.

Other costs of service were \$263,000 for the third quarter of 2012, a decrease of 32%, or \$125,000 compared to \$388,000 for the third quarter of 2011 mainly due to lower promotion and engineering costs when compared to the three months ended September 30, 2011.

Selling, general and administrative expenses were \$880,000 for the third quarter of 2012, a decrease of 15%, or \$161,000, compared to \$1.0 million in the third quarter of 2011. The decrease relates lower to general and administrative and lower sales commission expense.

Depreciation and amortization was \$125,000 for the third quarter of 2012, a decrease of 46%, or \$105,000, compared to \$230,000 for the third quarter of 2011. This decrease relates primarily to more assets becoming fully depreciated compared to new assets placed in service over the past year.

There were no impairment charges recorded during the third quarter of 2012 or 2011 related to our FCC broadcast licenses or our goodwill.

There was no gain or loss on disposal of our long-lived assets during the third quarter of 2012 and a \$10,000 loss recorded during the third quarter of 2011.

Corporate expenses for the third quarter of 2012 was \$226,000, a decrease of 26%, or \$81,000, compared to \$307,000 for the third quarter of 2011 principally as a result of lower compensation expense due to the corporate management restructures implemented, and lower professional fees when compared to the third quarter of 2011.

Income tax benefit for the third quarter of 2012 was \$2.0 million compared to an income tax benefit of \$74,000 for the third quarter of 2011. The income tax benefit for the 2012 quarter was calculated at the combined federal and average state statutory rate and mainly arose since it is expected to be fully realized by the tax on the gain on the station sales during 2012.

Our net income for the third quarter of 2012 was \$3.2 million compared to a net loss of \$432,000 for the third quarter of 2011.

*Nine Months Ended September 30, 2012 Compared to September 30, 2011*

Net revenues from continuing operations for the nine months ended September 2012 were \$11.8 million, a decrease of 19%, or \$2.7 million, compared to net revenues of \$14.5 million in the nine months ended September 2011. The decrease is mainly due to the fact that the nine months of 2011 included revenues from our stations WBXX, WBDT, WIWB which sold in May of 2011 and our WBUW station which sold in February of 2012.

Programming expenses for the nine months ended September 2012 were \$5.8 million, a decrease of 23%, or \$1.2 million, compared to \$7.5 million for the nine months ended September 2011. The decrease is mainly due to the fact that the nine months of 2011 included programming expense from our stations WBXX, WBDT, WIWB which sold in May of 2011 and WBUW station which sold in February of 2012.

Other costs of service was \$845,000 for the nine months ended September 2012, a decrease of 56%, or \$1.1 million, compared to \$1.9 million for the nine months ended September 2011. The decrease is mainly due to the fact that the nine months of 2011 included our stations WBXX, WBDT, WIWB which sold in May of 2011 and our WBUW station which sold in February of 2012.

Selling, general and administrative expenses were \$2.9 million for the nine months ended September 2012, a decrease of 39%, or \$1.9 million, compared to \$4.8 million in the nine months ended September 2011. The decrease is mainly due to the fact that the nine months of 2011 included our stations WBXX, WBDT, WIWB which sold in May of 2011 and our WBUW station which sold in February of 2012.

Depreciation and amortization was \$401,000 for the nine months ended September 2012, a decrease of 54%, or \$468,000, compared to \$869,000 for the nine months ended September 2011. This decrease relates primarily to more assets becoming fully depreciated compared to new assets placed in service over the past year.

There were no impairment charges recorded during the nine months ended September 2012 or 2011 related to our FCC broadcast licenses or our goodwill.

The gain on disposal of assets during the nine months ended September 2012 was \$1.0 million and related to the sale of our WBUW station in February 2012 and the gain on disposal of assets during the nine months ended September 2011 was \$12.9 million and related to the sale of our WBXX, WBDT and WIWB stations in May 2011.

Corporate expenses for the nine months ended September 2012 was \$717,000, a decrease of 35%, or \$394,000, compared to \$1.1 million for the nine months ended September 2011 principally as a result of lower compensation expense due to corporate management restructures implemented in July 2011.

Income tax benefit for the nine months ended September 2012 was \$2.2 million, compared to an income tax expense of \$761,000 for the nine months ended September 2011 relating to the difference between book and tax amortization of intangibles. The income tax benefit for the nine months ended September 2011 was comprised of a \$8,000 current tax expense and a \$2.0 million deferred tax benefit was calculated and mainly arose since it is expected to be fully realized by the tax on the gain on the station sales during 2012.

Our net income for the nine months ended September 2012 was \$4.2 million compared to a net income of \$10.3 million for the nine months ended September 2011.

## **Liquidity and Capital Resources**

Net cash provided by operating activities was \$650,000 for the first nine months ended September 30, 2012, compared to net cash used of \$4.7 million for the first nine months of 2011. The cash flow during the first nine months of 2012 mainly related to an income tax refund (including interest thereon) received in March 2012 of \$520,000 relating to a State of Wisconsin tax matter dating back to 2007, net of the effect of seasonal working capital changes while the cash flow usage during the first nine months of 2011 mainly related to the funding our \$3.2 million litigation escrow in connection with our MMT litigation.

Net cash provided by investing activities during the first nine months of 2012 was \$1.8 million consisting mainly of the cash portion of the sales proceeds relating to the sale of our WBUW station. Net cash provided by investing activities was \$11.3 million during the first nine months of 2011 consisting mainly of the cash portion of the sales proceeds relating to the sale of our WBXX, WBDT and WIWB in May 2011.

Net cash used in financing activities during the first nine months of 2012 was \$3.7 million compared to net cash used of \$8.4 million during the first nine months of 2011 consisting mainly of our \$3.5 million cash distribution to our shareholders in April 2012 and repayments of program deferrals while the cash used in financing activities during the first nine months of 2011 mainly related to the special distribution payment to our shareholders of \$5.6 million in July 2011 and repayments of program deferrals and capital lease obligation payments.

As of September 30, 2012, we had cash and cash equivalents of \$593,000 compared to cash and cash equivalents of \$2.3 million as of December 31, 2011.

We believe existing cash and cash equivalents at September 30, 2012 and the cash proceeds received from the sale of our New Mexico stations, net of our dividend payment and other related expenses in December 2012, will be sufficient to meet our operating cash requirements to properly liquidate and dissolve the Company.

## ***Recent Accounting Pronouncements***

Refer to Note 2, "*Recent Accounting Pronouncements*", in "Notes to Consolidated Financial Statements", for a discussion of new accounting standards.

## **Other Information**

On October 14, 2008, we notified the Nasdaq Stock Market of our intent to voluntarily delist our common stock from the Nasdaq Global Market, and to voluntarily deregister our common stock under the Securities Exchange Act of 1934 by filing with the Securities & Exchange Commission ("SEC") a Form 25 relating to the delisting of our common stock on or about October 24, 2008, with the delisting of our common stock to be effective ten days thereafter.

Our last day of trading of our common stock on the Nasdaq Global Market was on Monday, November 3, 2008.

On November 4, 2008 we filed a Form 15 with the SEC to deregister our common stock under Section 12 of the Securities Exchange Act of 1934. Upon the filing of the Form 15, our obligation to file certain reports with the SEC, including Forms 10-K, 10-Q, and 8K, was immediately suspended. The deregistration of our common stock became effective February 1, 2009.

Our common stock is currently quoted on the Pink Sheets®, a centralized electronic quotation service for over-the-counter securities.