

Edgar Filing: Discovery Communications, Inc. - Form 10-K

Discovery Communications, Inc.  
Form 10-K  
February 20, 2014

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

FORM 10-K

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

For the fiscal year ended December 31, 2013

OR

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

For the transition period from to

Commission File Number: 001-34177

Discovery Communications, Inc.  
(Exact name of Registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

35-2333914  
(I.R.S. Employer  
Identification No.)

One Discovery Place  
Silver Spring, Maryland  
(Address of principal executive offices)  
(240) 662-2000  
(Registrant's telephone number, including area code)

20910  
(Zip Code)

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

Title of Each Class

Series A Common Stock, par value \$0.01 per share

Series B Common Stock, par value \$0.01 per share

Series C Common Stock, par value \$0.01 per share

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

None

Name of Each Exchange on Which Registered

The NASDAQ Global Select Market

The NASDAQ Global Select Market

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Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☒ No ☐

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ☐ No ☒

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ☒

Accelerated filer ☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company)

Smaller reporting company ☐

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

The aggregate market value of voting and non-voting common stock held by non-affiliates of the Registrant computed by reference to the last sales price of such stock, as of the last business day of the Registrant's most recently completed second fiscal quarter, which was June 30, 2013, was approximately \$17 billion.

Total number of shares outstanding of each class of the Registrant's common stock as of February 6, 2014 was:

Series A Common Stock, par value \$0.01 per share	146,932,515
Series B Common Stock, par value \$0.01 per share	6,545,033
Series C Common Stock, par value \$0.01 per share	80,635,628

#### DOCUMENTS INCORPORATED BY REFERENCE

Certain information required in Item 10 through Item 14 of Part III of this Annual Report on Form 10-K is incorporated herein by reference to the Registrant's definitive Proxy Statement for its 2014 Annual Meeting of Stockholders, which shall be filed with the Securities and Exchange Commission pursuant to Regulation 14A of the Securities Exchange Act of 1934, as amended, within 120 days of the Registrant's fiscal year end.

DISCOVERY COMMUNICATIONS, INC.  
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## PART I

### ITEM 1. Business.

For convenience, the terms “Discovery,” “DCI,” the “Company,” “we,” “us” or “our” are used in this Annual Report on Form 10-K to refer to both Discovery Communications, Inc. and collectively to Discovery Communications, Inc. and one or more of its consolidated subsidiaries, unless the context otherwise requires.

#### OVERVIEW

We are a global media company that provides content across multiple distribution platforms, including digital distribution arrangements, throughout the world. We were formed on September 17, 2008, as a Delaware corporation in connection with Discovery Holding Company (“DHC”) and Advance/Newhouse Programming Partnership combining their respective ownership interests in Discovery Communications Holding, LLC (“DCH”) and exchanging those interests with and into Discovery (the “Discovery Formation”). As a result of the Discovery Formation, DHC and DCH became wholly-owned subsidiaries of Discovery, with Discovery becoming the successor reporting entity to DHC. As one of the world’s largest nonfiction media companies, we provide original and purchased content to more than 2.2 billion cumulative viewers worldwide through networks that we wholly or partially own. We distribute customized content in the U.S. and over 220 other countries and territories in over 40 languages. Our global portfolio of networks includes prominent television brands such as Discovery Channel, one of the first nonfiction networks and our most widely distributed global brand, TLC and Animal Planet. We also have a diversified portfolio of websites and develop and sell curriculum-based education products and services.

Our objectives are to invest in content for our networks to build viewership, optimize distribution revenue, capture advertising sales, and create or reposition additional branded channels and businesses that can sustain long-term growth and occupy a desired content niche with strong consumer appeal. Our strategy is to maximize the distribution, ratings and profit potential of each of our branded networks. In addition to growing distribution and advertising revenue for our branded networks, we are extending content distribution across new platforms, including brand-aligned websites, on-line streaming, mobile devices, video on demand (“VOD”) and broadband channels, which provide promotional platforms for our television content and serve as additional outlets for advertising and distribution revenue. Audience ratings are a key driver in generating advertising revenue and creating demand on the part of cable television operators, direct-to-home (“DTH”) satellite operators, telecommunication service providers, and other content distributors who deliver our content to their customers.

Our content spans genres including science, exploration, survival, natural history, technology, docu-series, anthropology, heroes, paleontology, history, space, archeology, health and wellness, engineering, adventure, lifestyles, crime and investigation, civilizations, current events and kids. We have an extensive library of content and own all or most rights to the majority of our content and footage, which enables us to exploit our library to launch brands and services into new markets quickly. Our content can be re-edited and updated in a cost-effective manner to provide topical versions of subject matter that can be utilized around the world. Substantially all of our content is produced in high definition (“HD”) format.

We classify our operations in three segments: U.S. Networks, consisting principally of domestic television networks and websites; International Networks, consisting primarily of international television networks and websites; and Education, consisting principally of curriculum-based product and service offerings. Financial information for our segments and geographical areas in which we do business is set forth in Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and Note 22 to the consolidated financial statements included in Item 8, “Financial Statements and Supplementary Data” in this Annual Report on Form 10-K.

Subscriber statistics set forth in this Annual Report on Form 10-K include both wholly-owned networks and networks operated by equity method investees. Domestic subscriber statistics are based on Nielsen Media Research.

International subscriber and viewer statistics are derived from internal data coupled with external sources when available. As used herein, a “subscriber” is a single household that receives the applicable network from its cable television operator, DTH satellite operator, telecommunication service provider, or other television provider, including those who receive our networks from pay television providers without charge pursuant to various pricing plans that include free periods and/or free carriage. The term “viewer” is a single household that receives the signal to

one of our networks using the appropriate receiving equipment without a subscription to a pay television provider. The term “cumulative viewers” refers to the collective sum of the total number of subscribers and viewers to each of our networks or content services. By way of example, two households that each receive five of our networks from their pay television provider represent two subscribers, but 10 cumulative subscribers.

## U.S. NETWORKS

U.S. Networks generated revenues of \$3.0 billion during 2013, which represented 53% of our total consolidated revenues. Our U.S. Networks segment principally consists of national television networks. Our U.S. Networks segment wholly owns and operates nine national television networks, including fully distributed television networks such as Discovery Channel, TLC and Animal Planet. Discovery Channel, TLC and Animal Planet collectively generated 70% of U.S. Networks' total revenue. In addition, this segment holds equity method interests in OWN and The Hub Network.

U.S. Networks generates revenues from fees charged to distributors of our television networks' content, which include cable, DTH satellite and telecommunication service providers, referred to as affiliate fees; fees from digital distributors, which relate to bulk content distribution agreements; and from advertising sold on our television networks and websites. U.S. Networks also generates income by providing sales representation and network distribution services to equity method investee networks and licensing our brands for consumer products.

Typically, our television networks are aired pursuant to multi-year carriage agreements that provide for the level of carriage that our networks will receive, and if applicable, for annual graduated rate increases. Carriage of our networks depends on channel placement and package inclusion, such as whether networks are on the more widely distributed, broader packages or lesser-distributed, specialized packages, also referred to as digital tiers.

Advertising revenue is based on the price received for available advertising spots and is dependent upon a number of factors including the number of subscribers to our channels, viewership demographics, the popularity of our programming, and our ability to sell commercial time over a group of channels. In the U.S., advertising time is sold in the upfront and scatter markets. In the upfront market, advertisers buy advertising time for upcoming seasons, and by committing to purchase in advance, lock in the advertising rates they will pay for the upcoming year. A portion of many upfront advertising commitments include options whereby advertisers may reduce purchase commitments. In the scatter market, advertisers buy advertising time when the commercials will be run, which often results in a pricing premium compared to the upfront rates. The mix of upfront and scatter market advertising time sold is based upon a number of factors, such as pricing, demand for advertising time and economic conditions.

Discovery Channel reached approximately 98 million subscribers in the U.S. as of December 31, 2013. Discovery Channel also reached 8 million subscribers through a licensing arrangement with partners in Canada as of December 31, 2013, according to internal data.

Discovery Channel is dedicated to creating the highest quality non-fiction content that informs and entertains its consumers about the world in all its wonder. The network offers a signature mix of compelling high-end production values and vivid cinematography across genres including, science and technology, exploration, adventure, history and in-depth, behind-the-scenes glimpses at the people, places and organizations that shape and share our world. Content on Discovery Channel includes Gold Rush, Naked and Afraid, Deadliest Catch, Amish Mafia and Moonshiners. Discovery Channel is also home to specials and mini-series, including Skywire Live with Nik Wallenda.

Target viewers are adults ages 25-54, particularly men.

Discovery Channel is simulcast in HD.

TLC reached approximately 97 million subscribers in the U.S. as of December 31, 2013. TLC also reached approximately 7 million subscribers in Canada as of December 31, 2013, according to internal data.

TLC celebrates extraordinary people and relatable life moments through innovative nonfiction programming. A top 10 cable network in key female demographics, TLC has built successful consumer brands around series including, *Cake Boss*, and has transformed Fridays into "Bride-Day" with a lineup of wedding-themed programming anchored by the *Say Yes To The Dress* franchise. Other content on TLC includes *Here Comes Honey Boo Boo*, *Breaking Amish*, *Long Island Medium* and *Sister Wives*.

Target viewers are adults ages 18-54, particularly women.

TLC is simulcast in HD.

Animal Planet reached approximately 96 million subscribers in the U.S. as of December 31, 2013. Animal Planet also reached 2 million subscribers through a licensing arrangement with partners in Canada as of December 31, 2013, according to internal data.

Animal Planet immerses viewers in the full range of life in the animal kingdom with rich, deep content via multiple platforms and offers animal lovers and pet owners access to a centralized online, television and mobile community for immersive, engaging, high-quality entertainment, information and enrichment.

Content on Animal Planet includes *Puppy Bowl*, *River Monsters*, *Treehouse Masters*, *Gator Boys* and *Finding Bigfoot*. 2013 was Animal Planet's most-watched year in network history in prime and total day delivery.

Target viewers are adults ages 25-54.

Animal Planet is simulcast in HD.

Investigation Discovery ("ID") reached approximately 84 million subscribers in the U.S. as of December 31, 2013. ID also reached 1 million subscribers through a licensing arrangement with partners in Canada as of December 31, 2013, according to internal data.

ID is a leading mystery-and-suspense network on television and America's favorite "guilty pleasure." From harrowing crimes and salacious scandals to the in-depth investigation and heart-breaking mysteries that result, ID challenges our everyday understanding of culture, society and the human condition.

Content on ID includes *Redrum*, *Deadline: Crime with Tamron Hall*, *On The Case With Paula Zahn*, *Injustice Files*, *Homicide Hunter: Lt. Joe Kenda* and *Wives With Knives*.

Target viewers are adults ages 25-54, particularly women.

ID is simulcast in HD.



Science Channel reached approximately 76 million subscribers in the U.S. as of December 31, 2013. Science Channel also reached 2 million subscribers through a licensing arrangement with partners in Canada as of December 31, 2013, according to internal data.

Science Channel is home for the thought provocateur and features programming willing to go beyond imagination to explore the unknown. Guided by curiosity, Science Channel looks at innovation in mysterious new worlds as well as in our own backyards.

Content on Science Channel includes Through the Wormhole with Morgan Freeman, Oddities, NASA's Unexplained Files and How It's Made.

Target viewers are adults ages 25-54.

Science Channel is simulcast in HD.

Military Channel reached approximately 62 million subscribers in the U.S. as of December 31, 2013. Military Channel also reached approximately 1 million subscribers in Canada as of December 31, 2013, according to internal data. Military Channel will officially change its name to the American Heroes Channel ("AHC"), on March 3, 2014. AHC will tell timeless stories in which a challenge appears - be it a situation or a villain - and a hero arises. AHC will provide a rare glimpse into major events that shaped our world, visionary leaders and unexpected heroes who made a difference, and the great defenders of freedom.

AHC will feature the most iconic programming from Military Channel, including Air Aces, The Brokaw Files and epic WWII documentaries like Pearl Harbor: Declassified as well as new series and specials, including Against the Odds, Raw War and Codes and Conspiracies.

Target viewers are men ages 35-64.

Destination America reached approximately 59 million subscribers in the U.S. as of December 31, 2013.

Destination America celebrates the people, places and stories of the United States, and emblazons television screens with the grit and tenacity, honesty, work ethic, humor and adventurousness that characterize our nation.

Content on Destination America includes Mountain Monsters, A Haunting, Railroad Alaska and Buying the Bayou.

Target viewers are adults ages 18-54.

Destination America is simulcast in HD.

• Velocity reached approximately 56 million subscribers in the U.S. as of December 31, 2013.

Velocity engages viewers with a variety of high-octane, intelligent programming that is always action-packed and captures the best of the human experience. In addition to series and specials exemplifying the finest of the automotive, sports and leisure, adventure and travel genres, the network broadcasts hundreds of hours of live events coverage every year.

• Content on Velocity includes Wheeler Dealers, Chasing Classic Cars, Overhaulin' and Inside West Coast Customs.

• Target viewers are adults ages 25-54, particularly men.

• Discovery Fit & Health reached approximately 48 million subscribers in the U.S. as of December 31, 2013.

Discovery Fit & Health entertains viewers with gripping, real-life dramas, featuring storytelling that chronicles the human experience from cradle to grave, including forensic mysteries, amazing medical stories, emergency room trauma, baby and pregnancy programming, parenting challenges, and stories of extreme life conditions.

• Content on Discovery Fit & Health includes I Didn't Know I was Pregnant, Untold Stories of the E.R., Secret Sex Lives: Swingers and Bizarre E.R.

• Target viewers are adults ages 25-54.

Our U.S. Networks segment owns interests in the following television networks that are operated by equity method investees:

• OWN: Oprah Winfrey Network ("OWN") reached approximately 83 million subscribers in the U.S. as of December 31, 2013.

OWN is the first and only network named for, and inspired by, a single iconic leader. Oprah Winfrey's heart and creative instincts inform the brand and the magnetism of the channel. Ms. Winfrey provides leadership in programming and attracts superstar talent to join her in primetime, building a global community of like-minded viewers and leading that community to connect on social media and beyond.

• Content on OWN includes Tyler Perry's original series: The Haves and Have Nots and Love Thy Neighbor, as well as Oprah's Next Chapter, Iyanla Fix My Life, Welcome to Sweetie Pies and Life With La Toya.

• Target viewers are adults 25-54, particularly women.

• OWN is simulcast in HD.

- ¶ The Hub Network reached approximately 72 million subscribers in the U.S. as of December 31, 2013. The Hub Network provides enriching, cool, relevant, family-friendly entertainment experiences that children and parents can enjoy together, including animated and live-action series, as well as specials, game shows, and family-favorite movies.
- Content on The Hub Network includes The Aquabats! Super Show!, The Haunting Hour: The Series, SheZow, Goosebumps and My Little Pony Friendship is Magic.
- ¶ Target viewers are children ages 2-11 and families.
- ¶ The Hub Network is simulcast in HD.

- 3net reached approximately 40 million households in the U.S. as of December 31, 2013.
- 3net is the nation's first and only fully programmed, 24/7 3D network, bringing viewers the highest quality and most immersive in-home 3D viewing experience possible.
- Content on 3net includes Dream Defenders, Storm Surfers, Into the Deep and NASCAR.
- ¶ Target viewers are adults 25-54.

#### INTERNATIONAL NETWORKS

International Networks generated revenues of \$2.5 billion during 2013, which represented 45% of our total consolidated revenues. Our International Networks segment principally consists of national and pan-regional television networks. This segment generates revenue from operations in virtually every pay television market in the world through an infrastructure that includes operational centers in London, Singapore and Miami. Discovery Channel, Animal Planet, TLC, ID and Science Channel lead the International Networks' portfolio of television networks. International Networks has a large international distribution platform for its networks with as many as 15 networks in more than 220 countries and territories around the world. At December 31, 2013, International Networks operated over 240 unique distribution feeds in over 40 languages with channel feeds customized according to language needs and advertising sales opportunities. International Networks also has free-to-air networks in Europe and the Middle East, broadcast networks in the Nordics and continues to pursue further international expansion.

Our International Networks segment owns and operates the following television networks, which reached the following number of subscribers via pay television services as of December 31, 2013:

Global Networks	International Subscribers (millions)	Regional Networks	International Subscribers (millions)
Discovery Channel	271	Discovery Kids	76
Animal Planet	200	SBS Nordic <sup>(a)</sup>	28
TLC, Real Time and Travel & Living	162	DMAX <sup>(b)</sup>	16
Discovery Science	81	Discovery History	14
Investigation Discovery	74	Shed	12
Discovery Home & Health	64	Discovery en Espanol (U.S.)	5
Turbo	52	Discovery Familia (U.S.)	4
Discovery World	23	GXT	4

<sup>(a)</sup> Number of subscribers corresponds to the collective sum of the total number of subscribers to each of the SBS Nordic broadcast networks in Sweden, Norway, and Denmark subject to retransmission agreements with pay television providers.

<sup>(b)</sup> Number of subscribers corresponds to DMAX pay television networks in the U.K., Austria, Switzerland and Ireland.

Our International Networks segment also owns and operates free-to-air television networks which reached 285 million cumulative viewers in Europe and the Middle East as of December 31, 2013. Our free-to-air networks include DMAX, Fatafeat, Quest, Real Time, Giallo, Frisbee, Focus and K2.

Similar to U.S. Networks, the primary sources of revenue for International Networks are fees charged to operators who distribute our networks, which primarily include cable and DTH satellite service providers, and advertising sold on our television networks. International television markets vary in their stages of development. Some markets, such as the U.K., are more advanced digital television markets, while others remain in the analog environment with varying degrees of investment from operators to expand channel capacity or convert to digital technologies. Common practice in some markets results in long-term contractual distribution relationships, while customers in other markets renew contracts annually. Distribution revenue for our International Networks segment is largely dependent on the number of subscribers that receive our networks or content, the rates negotiated in the agreements, and the market demand for the content that we provide.

Advertising revenue is dependent upon a number of factors including the development of pay and free-to-air television markets, the number of subscribers to and viewers of our channels, viewership demographics, the popularity of our programming, and our ability to sell commercial time over a group of channels. In certain markets, our advertising sales business operates with in-house sales teams, while we rely on external sales representation services in other markets. In developing television markets, we expect that advertising revenue growth will result from continued subscriber and viewership growth, our localization strategy, and the shift of advertising spending from traditional analog networks to channels in the multi-channel environment. In relatively mature markets, such as Western Europe, growth in advertising revenue will come from increasing viewership and pricing of advertising on our existing television networks and the launching of new services, both organic and through acquisitions. During 2013, distribution, advertising and other revenues were 50%, 47% and 3%, respectively, of total net revenues for this segment.

On January 21, 2014, we entered into an agreement with TF1 to acquire a controlling interest in Eurosport International ("Eurosport"), a leading pan-European sports media platform, by increasing our ownership stake from 20% to 51% for cash of approximately €253 million (\$343 million) subject to working capital adjustments. Due to regulatory constraints the acquisition initially excludes Eurosport France, a subsidiary of Eurosport. We will retain a

20% equity interest in Eurosport France and a commitment to acquire another 31% ownership interest beginning 2015, contingent upon resolution of all regulatory matters. The flagship Eurosport network focuses on regionally popular sports such as tennis, skiing, cycling and motor sports and reaches 133 million homes across 54 countries in 20 languages. Eurosport's brands and platforms also include Eurosport HD (high definition simulcast), Eurosport 2, Eurosport 2 HD (high definition simulcast), Eurosport Asia-Pacific, and Eurosportnews. The acquisition is intended to increase the growth of Eurosport and enhance our pay television offerings in Europe. TF1 will have the right to put the entirety of its remaining 49% non-controlling interest to us for approximately two and a half years after completion of this acquisition. The put has a floor value equal to the fair value at the acquisition date if exercised in the 90 day period beginning on July 1, 2015 and is subsequently priced at fair value if exercised in the 90 day period beginning on July 1, 2016. We expect the acquisition to close in the second quarter of 2014 subject to obtaining necessary regulatory approvals.

On December 28, 2012, we acquired Switchover Media, a group of five Italian television channels with children's and entertainment programming. (See Note 3 to the accompanying consolidated financial statements.)

On January 10, 2013, we purchased an additional 30% ownership interest in Discovery Japan, which was previously a 50% owned equity method investee. As a result, we now have a controlling financial interest in Discovery Japan and account for it as a consolidated subsidiary. We recognized a \$92 million gain upon consolidation for the difference in the carrying value and the fair value of the previously held equity interest. (See Note 3 to the accompanying consolidated financial statements.)

On April 9, 2013, we acquired the general entertainment television and radio business operations ("SBS Nordic") of Prosiebensat.1 Media AG for cash of approximately €1.4 billion (\$1.8 billion), including closing purchase price adjustments. (See Note 3 to the accompanying consolidated financial statements.)

#### EDUCATION

Education generated revenues of \$114 million during 2013, which represented 2% of our total consolidated revenues. Education is comprised of curriculum-based product and service offerings. This segment generates revenues primarily from subscriptions charged to K-12 schools for access to an online suite of curriculum-based VOD tools, professional development services, digital textbooks and, to a lesser extent, student assessments and publication of hardcopy curriculum-based content. Our education business also participates in global brand and content licensing and engages in partnerships with leading non-profits, corporations, foundations and trade associations.

On November 1, 2013, we acquired an education business in the U.K. that will complement our existing service offerings and expand our operations internationally. (See Note 3 to the accompanying consolidated financial statements.)

#### CONTENT DEVELOPMENT

Our content development strategy is designed to increase viewership, maintain innovation and quality leadership, and provide value for our network distributors and advertising customers. Our content is sourced from wholly-owned production companies and a wide range of third-party producers, which include some of the world's leading nonfiction production companies as well as independent producers. Our production arrangements fall into three categories: produced, coproduced and licensed. Produced content includes content that we engage third parties to develop and produce, while we retain editorial control and own most or all of the rights, in exchange for paying all development and production costs. Coproduced content refers to program rights on which we have collaborated with third parties to finance and develop because at times world-wide rights are not available for acquisition or we save costs by collaborating with third parties. Licensed content is comprised of films or series that have been produced by third parties.

International Networks maximizes the use of content from our U.S. Networks. Much of our content tends to be culturally neutral and maintains its relevance for an extended period of time. As a result, a significant amount of our content translates well across international borders and is made even more accessible through extensive use of dubbing and subtitles in local languages. Our content can be re-edited and updated in a cost-effective manner to provide topical versions of subject matter that can be utilized around the world. We also develop local content that is tailored to individual market preferences, which is typically produced through third-party production companies. International Networks executes a localization strategy by offering content from U.S. Networks, customized content and localized schedules via our distribution feeds. While our International Networks segment maximizes the use of content from U.S. Networks, we also develop local content that is tailored to individual market preferences and license the rights to air films, television series and sporting events from third-party producers.

Our largest single cost is content expense, which includes content amortization, content impairments and production costs. We amortize the cost of capitalized content rights based on the proportion that the current year's estimated revenues bear to the estimated remaining total lifetime revenues, which normally results in an accelerated amortization method over the estimated useful lives. Certain networks utilize a straight-line method of amortization over the estimated useful lives of the content.

#### REVENUES

We generate revenues principally from: (i) fees charged to operators who distribute our network content, which primarily include cable, DTH satellite, telecommunication and digital service providers, (ii) advertising sold on our networks and websites, and (iii) other transactions, including curriculum-based products and services, affiliate and advertising sales representation services, content licenses and the licensing of our brands for consumer products. During 2013, distribution, advertising, and other revenues were 46%, 49% and 5%, respectively, of consolidated revenues. No individual customer represented more than 10% of our total consolidated revenues for 2013, 2012 or 2011.

## Distribution

Distribution revenue includes fees charged for the right to view Discovery network branded content made available to customers through a variety of distribution platforms and viewing devices. The largest component of distribution revenue is comprised of affiliate fees charged to cable, DTH satellite and telecommunication service providers for distribution rights to our television networks. We have contracts with distributors representing most cable and satellite service providers around the world, including the largest operators in the U.S. and major international distributors. Typically, our television networks are aired pursuant to multi-year carriage agreements that provide for the level of carriage that Discovery's networks will receive, and, if applicable, for scheduled graduated annual rate increases. Carriage of our networks depends upon channel placement and package inclusion, such as whether networks are on the more widely distributed, broader packages or lesser-distributed, specialized packages. Distribution revenues are largely dependent on the rates negotiated in the agreements, the number of subscribers that receive our networks or content, and the market demand for the content that we provide. We have provided distributors launch incentives, in the form of cash payments or free periods, to carry our networks.

Distribution revenue also includes fees charged for bulk content arrangements and other subscription services for episodic content. Digital distribution agreements are impacted by the quantity, as well as the quality, of the content Discovery provides.

In the U.S., approximately 90% of distribution revenues come from the top 10 distributors, with whom we have agreements that expire at various times from 2014 through 2020. Outside of the U.S., approximately 50% of distribution revenue comes from the top 10 distributors. Distribution fees are typically collected ratably throughout the year. International television markets vary in their stages of development. Some, notably the U.K., are more advanced digital multi-channel television markets, while others operate in the analog environment with varying degrees of investment from distributors in expanding channel capacity or converting to digital.

## Advertising

Our advertising revenue consists of consumer advertising, which is sold primarily on a national basis in the U.S. and on a pan-regional or local-language feed basis outside the U.S. Advertising contracts generally have a term of one year or less.

In the U.S., we sell advertising time in the upfront and scatter markets. In the upfront market, advertisers buy advertising time for the upcoming season and by purchasing in advance often receive discounted rates. In the scatter market, advertisers buy advertising time close to the time when the commercials will be run and often pay a premium. The mix between the upfront and scatter markets is based upon a number of factors, such as pricing, demand for advertising time and economic conditions. Outside the U.S., advertisers typically buy advertising closer to the time when the commercials will be run. Advertising revenue is dependent upon a number of factors, including the stage of development of television markets, the popularity of free-to-air television, the number of subscribers to our channels, viewership demographics, the popularity of our content and our ability to sell commercial time over a group of channels. In developing pay television markets, we expect advertising revenue growth will result from subscriber growth, our localization strategy, and the shift of advertising spending from broadcast to pay television. In mature markets, such as the U.S. and Western Europe, high proportions of market penetration and distribution are unlikely to drive rapid revenue growth. Instead, growth in advertising sales comes from increasing viewership and pricing and launching new services, either in pay television, broadcast, or free-to-air television environments.

Revenue from advertising is subject to seasonality, market-based variations and general economic conditions.

Advertising revenue is typically highest in the second and fourth quarters. In some cases, advertising sales are subject to ratings guarantees that require us to provide additional advertising time if the guaranteed audience levels are not achieved.

We also generate revenue from the sale of advertising on our websites on a stand-alone basis and as part of advertising packages with our television networks.

## Other

We also generate income associated with providing affiliate and advertising sales representation and network services for equity method investee networks, curriculum-based products and services and the licensing of our brands for



consumer products.

#### COMPETITION

Television network content is a highly competitive business worldwide. We experience competition for the development and acquisition of content, distribution of our content, selling of commercial time on our networks and viewership. Our networks compete with studios, television networks, and the internet for the acquisition of content and creative talent such as writers, producers and directors. Our ability to produce and acquire popular content is an important competitive factor for the distribution of our networks, attracting viewers and the sale of advertising. Our success in securing popular content and creative talent depends

on various factors such as the number of competitors providing content that targets the same genre and audience, the distribution of our networks, viewership, and the production, marketing and advertising support we provide.

Our networks compete with other television networks, including broadcast, cable and local, for the distribution of our content and fees charged to cable television operators, DTH satellite service providers, and other distributors that carry our network content. Our ability to secure distribution agreements is necessary to ensure the retention of our audiences. Our contractual agreements with distributors are renewed or renegotiated from time to time in the ordinary course of business. Growth in the number of networks distributed, consolidation and other market conditions in the cable and satellite distribution industry, and increased popularity of other platforms may adversely affect our ability to obtain and maintain contractual terms for the distribution of our content that are as favorable as those currently in place. The ability to secure distribution agreements is dependent upon the production, acquisition and packaging of original content, viewership, the marketing and advertising support and incentives provided to distributors, the product offering across a series of networks within a region, and the prices charged for carriage.

Our networks and websites compete for the sale of advertising with other television networks, including broadcast, cable and local networks, online and mobile outlets, radio content and print media. Our success in selling advertising is a function of the size and demographics of our audiences, quantitative and qualitative characteristics of the audience of each network, the perceived quality of the network and of the particular content, the brand appeal of the network and ratings as determined by third-party research companies, prices charged for advertising and overall advertiser demand in the marketplace.

Our networks and websites also compete for their target audiences with all forms of content and other media provided to viewers, including broadcast, cable and local networks, pay-per-view and VOD services, DVDs, online activities and other forms of news, information and entertainment.

Our education business competes with other providers of curriculum-based products and services to schools.

#### INTELLECTUAL PROPERTY

Our intellectual property assets include copyrights in television content, trademarks in brands, names and logos, websites, and licenses of intellectual property rights from third parties.

We are fundamentally a content company and the protection of our brands and content is of primary importance. To protect our intellectual property assets, we rely upon a combination of copyright, trademark, unfair competition, trade secret and Internet/domain name statutes and laws, and contract provisions. However, there can be no assurance of the degree to which these measures will be successful. Moreover, effective intellectual property protection may be either unavailable or limited in certain foreign territories. Policing unauthorized use of our products and services and related intellectual property is difficult and costly. We seek to limit unauthorized use of our intellectual property through a combination of approaches. However, the steps taken to prevent the infringement of our intellectual property by unauthorized third parties may not work.

Third parties may challenge the validity or scope of our intellectual property from time to time, and the success of any such challenges could result in the limitation or loss of intellectual property rights. Irrespective of their validity, such claims may result in substantial costs and diversion of resources which could have an adverse effect on our operations. In addition, piracy, which encompasses the theft of our signal, and unauthorized use of our content, in the digital environment continues to present a threat to revenues from products and services based on our intellectual property.

#### REGULATORY MATTERS

Our businesses are subject to and affected by regulations of U.S. federal, state and local government authorities, and our international operations are subject to laws and regulations of the countries and international bodies, such as the European Union, in which we operate. Content networks, such as those owned by us, are regulated by the Federal Communications Commission ("FCC") in certain respects if they are affiliated with a cable television operator. Other FCC regulations, although imposed on cable television operators and direct broadcast satellite ("DBS") operators, affect content networks indirectly. The rules, regulations, policies and procedures affecting our businesses are constantly subject to change. These descriptions are summary in nature and do not purport to describe all present and proposed laws and regulations affecting our businesses.

Program Access

The FCC's program access rules prevent a satellite or cable content vendor in which a cable operator has an "attributable" ownership interest from discriminating against unaffiliated multichannel video programming distributors ("MVPDs"), such as cable and DBS operators, in the rates, terms and conditions for the sale or delivery of content. These rules also permit MVPDs to initiate complaints to the FCC against content networks if an MVPD claims it is unable to obtain rights to carry the content network on nondiscriminatory rates, terms or conditions. The FCC allowed a previous blanket prohibition on exclusive

arrangements with cable operators to expire in October 2012, but will consider case-by-case complaints that exclusive contracts between cable operators and cable-affiliated programmers significantly hinder or prevent an unaffiliated MVPD from providing satellite or cable programming.

#### “Must-Carry”/Retransmission Consent

The Cable Television Consumer Protection and Competition Act of 1992 (the “Act”) imposes “must-carry” regulations on cable systems, requiring them to carry the signals of most local broadcast television stations in their market. DBS systems are also subject to their own must-carry rules. The FCC’s implementation of “must-carry” obligations requires cable operators and DBS providers to give broadcasters preferential access to channel space. This reduces the amount of channel space that is available for carriage of our networks by cable and DBS operators. The Act also established retransmission consent, which refers to a broadcaster’s right to require consent from MVPDs, such as cable and satellite operators, before distributing its signal to their subscribers. Broadcasters have traditionally used the resulting leverage from demand for their must-have broadcast content to obtain carriage for their affiliated networks. Increasingly, broadcasters are additionally seeking substantial monetary compensation for granting carriage rights for their must-have broadcast content. Such increased financial demands on distributors reduce the content funds available for independent programmers not affiliated with broadcasters, such as us.

#### Closed Captioning and Advertising Restrictions

Certain of our networks must provide closed-captioning of content. Our content and websites intended primarily for children 12 years of age and under must comply with certain limits on advertising, and commercials embedded in our networks’ content stream adhere to certain standards for ensuring that those commercials are not transmitted at louder volumes than our program material. The 21<sup>st</sup> Century Communications and Video Accessibility Act of 2010 requires us to provide closed captioning on certain IP-delivered video content that we offer.

#### Obscenity Restrictions

Network distributors are prohibited from transmitting obscene content, and our affiliation agreements generally require us to refrain from including such content on our networks.

#### Violent Programming

In 2007, the FCC issued a report on violence in programing that recommended Congress prohibit the availability of violent programming, including cable programming, during hours when children are likely to be watching. Recent events have led to a renewed interest by some members of Congress in the alleged effects of violent programming, which could lead to a renewal of interest in limiting the availability of such programming or prohibiting it.

#### Regulation of the Internet

We operate several websites which we use to distribute information about our programs and to offer consumers the opportunity to purchase consumer products and services. Internet services are now subject to regulation in the U.S. relating to the privacy and security of personally identifiable user information and acquisition of personal information from children under 13, including the federal Children's Online Privacy Protection Act and the federal Controlling the Assault of Non-Solicited Pornography and Marketing Act. In addition, a majority of states have enacted laws that impose data security and security breach obligations. Additional federal and state laws and regulations may be adopted with respect to the Internet or other on-line services, covering such issues as user privacy, child safety, data security, advertising, pricing, content, copyrights and trademarks, access by persons with disabilities, distribution, taxation and characteristics and quality of products and services. In addition, to the extent we offer products and services to on-line consumers outside the U.S., the laws and regulations of foreign jurisdictions, including, without limitation, consumer protection, privacy, advertising, data retention, intellectual property, and content limitations, may impose additional compliance obligations on us.

#### EMPLOYEES

As of December 31, 2013, we had approximately 5,700 employees, including full-time and part-time employees of our wholly-owned subsidiaries and consolidated ventures.

#### AVAILABLE INFORMATION

All of our filings with the U.S. Securities and Exchange Commission (the “SEC”), including reports on Form 10-K, Form 10-Q and Form 8-K, and all amendments to such filings are available free of charge at the investor relations

section of our website, [www.discoverycommunications.com](http://www.discoverycommunications.com), as soon as reasonably practical after such material is filed with, or furnished to, the SEC. Our annual report, corporate governance guidelines, code of business ethics, audit committee charter, compensation

committee charter, and nominating and corporate governance committee charter are also available on our website. In addition, we will provide a printed copy of any of these documents, free of charge, upon written request at: Investor Relations, Discovery Communications, Inc., 850 Third Avenue, 8th Floor, New York, NY 10022-7225. The information contained on our website is not part of this Annual Report on Form 10-K and is not incorporated by reference herein.

#### ITEM 1A. Risk Factors.

Investing in our securities involves risk. In addition to the other information contained in this report, you should consider the following risk factors before investing in our securities.

Our success is dependent upon U.S. and foreign audience acceptance of our entertainment content, which is difficult to predict.

The production and distribution of entertainment content are inherently risky businesses because the revenue we derive and our ability to distribute our content depend primarily on consumer tastes and preferences that often change in unpredictable ways. Our success depends on our ability to consistently create and acquire content that meets the changing preferences of viewers in general, in special interest groups, in specific demographic categories and in various international marketplaces. The commercial success of our content also depends upon the quality and acceptance of competing content available in the applicable marketplace. At the same time, certain of our consolidated and equity method investee networks are new. There is no assurance of audience acceptance of the programming available on these new brands. Other factors, including the availability of alternative forms of entertainment and leisure time activities, general economic conditions, piracy, and growing competition for consumer discretionary spending may also affect the audience for our content. Audience sizes for our media networks are critical factors affecting both the volume and pricing of advertising revenue that we receive, and the extent of distribution and the license fees we receive under agreements with our distributors. Consequently, reduced public acceptance of our entertainment content may decrease our audience share and adversely affect our results of operations. Changes in consumer behavior resulting from new technologies and distribution platforms may impact the performance of our businesses.

Our business is focused on television, and we face emerging competition from other providers of digital media, some of which have greater financial, marketing and other resources than we do. In particular, content offered over the Internet has become more prevalent as the speed and quality of broadband networks have improved. Providers such as Hulu, Netflix, Apple TV, Amazon, Google TV and Intel, as well as gaming and other consoles such as Microsoft's Xbox and Xbox One, Sony's PS3 and PS4, Nintendo's Wii and Roku, are aggressively establishing themselves as alternative providers of video services. These services and the growing availability of online content, coupled with an expanding market for mobile devices and tablets that allow users to view content on an on-demand basis and Internet-connected televisions, may impact our traditional distribution methods for our services and content. Additionally, devices that allow users to view television programs on a time-shifted basis and technologies that enable users to fast-forward or skip programming, including commercials, such as DVRs and portable digital devices and systems that enable users to store or make portable copies of content, have caused changes in consumer behavior that may affect the attractiveness of our offerings to advertisers and could therefore adversely affect our revenues. If we cannot ensure that our distribution methods and content are responsive to our target audiences, our business could be adversely affected.

We operate in increasingly competitive industries.

The entertainment and media programming industries in which we operate are highly competitive. We compete with other programming networks for distribution, viewers and advertising. We also compete for viewers with other forms of media entertainment, such as home video, movies, periodicals and on-line and mobile activities. In particular, websites and search engines have seen significant advertising growth, a portion of which is derived from traditional cable network and satellite advertisers. In addition, there has been consolidation in the media industry and our competitors include market participants with interests in multiple media businesses which are often vertically integrated. Our on-line businesses compete for users and advertising in the broad and diverse market of free Internet-delivered services. Our commerce business competes against a wide range of competitive retailers selling

similar products. Our curriculum-based video business competes with other providers of education products to schools. If our distributors have to pay higher rates to holders of sports broadcasting rights, it might be difficult for us to negotiate higher rates for distribution of our networks. Our ability to compete successfully depends on a number of factors, including our ability to consistently supply high quality and popular content, access our niche viewership with appealing category-specific content, adapt to new technologies and distribution platforms and achieve widespread distribution. There can be no assurance that we will be able to compete successfully in the future against existing or new competitors, or that increasing competition will not have a material adverse effect on our business, financial condition or results of operations.

Further consolidation among cable and satellite providers could adversely affect our revenue and profitability. Consolidation among cable and satellite operators has given the largest operators considerable leverage in their relationships with programmers, including us. In the U.S., approximately 90% of our distribution revenues come from the top 10 distributors. We currently have agreements in place with the major U.S. cable and satellite operators which expire at various times beginning in 2014 through 2020. In addition, many of the countries and territories in which we distribute our networks also have a small number of dominant distributors. Continued consolidation within the industry could further reduce the number of distributors available to carry our content and increase the negotiating leverage of our distributors which could adversely affect our revenue.

The loss of our affiliation agreements, or renewals with less advantageous terms, could cause our revenue to decline. Because our networks are licensed on a wholesale basis to distributors such as cable and satellite operators which in turn distribute them to consumers, we are dependent upon the maintenance of affiliation agreements with these operators. These affiliation agreements generally provide for the level of carriage our networks will receive, such as channel placement and programming package inclusion (widely distributed, broader programming packages compared to lesser distributed, specialized programming packages) and for payment of a license fee to us based on the number of subscribers that receive our networks. While the number of subscribers associated with our networks impacts our ability to generate advertising revenue, these per subscriber payments also represent a significant portion of our revenue. Our affiliation agreements generally have a limited term which varies by market and distributor, and there can be no assurance that these affiliation agreements will be renewed in the future, or renewed on terms that are favorable to us. A reduction in the license fees that we receive per subscriber or in the number of subscribers for which we are paid, including as a result of a loss or reduction in carriage for our networks, could adversely affect our distribution revenue. Such a loss or reduction in carriage could also decrease the potential audience for our programs thereby adversely affecting our advertising revenue. In addition, our affiliation agreements are complex and individually negotiated. If we were to disagree with one of our counterparties on the interpretation of an affiliation agreement, our relationship with that counterparty could be damaged and our business could be negatively affected. Some terms of our agreements with distributors could be interpreted in a manner that could adversely affect distribution revenue payable to us under those agreements.

Some of our distribution agreements contain “most favored nation” clauses. These clauses typically provide that if we enter into an agreement with another distributor which contains certain more favorable terms, we must offer some of those terms to our existing distributors. We have entered into a number of distribution agreements with terms that differ in some respects from those contained in other agreements. While we believe that we have appropriately complied with the most favored nation clauses included in our distribution agreements, these agreements are complex and other parties could reach a different conclusion that, if correct, could have an adverse effect on our financial condition or results of operations.

We may pursue acquisitions and other strategic transactions to complement or expand our business that may not be successful and we may lose up to the entire value of our investment in these acquisitions and transactions.

Our success may depend on opportunities to buy other businesses or technologies that could complement, enhance or expand our current business or products or that might otherwise offer us growth opportunities. We may not be able to complete any transactions and these transactions, if executed, pose significant risks and could have a negative effect on our operations. Any transactions that we are able to identify and complete may involve a number of risks, including:

- the diversion of our management’s attention from our existing business to integrate the operations and personnel of the acquired or combined business or equity method investee;
- possible adverse effects on our operating results during the integration process;
- a high degree of risk involved in these transactions, which could become substantial over time, and higher exposure to significant financial losses if the underlying ventures are not successful; and
- our possible inability to achieve the intended objectives of the transaction.

In addition, we may not be able to integrate, operate, maintain and manage our newly acquired operations or employees successfully or profitably. We may not be able to maintain uniform standards, controls, procedures and



policies, and this may lead to operational inefficiencies. The integration of the SBS Nordic business, following the completion of that acquisition, and other recently acquired businesses and assets, including Eurosport, Discovery Japan and Switchover Media, may not be successful, may divert management attention and could have an adverse effect on our results of operations.

New acquisitions, equity method investments and other transactions may require the commitment of significant capital that would otherwise be directed to investments in our existing businesses or be distributed to shareholders.

The financial performance of our equity method investments may differ from current estimates.

We have equity investments in certain entities and the accounting treatment applied for these investments varies depending on a number of factors, including, but not limited to, our percentage ownership and whether we have any influence or control over the relevant entity. Any losses experienced by these entities could adversely impact our results of operations and the value of our investment. In addition, if these entities were to fail and cease operations, we may lose the entire value of our investment and the stream of any shared profits. Some of our ventures are recently launched networks, which may require significant funding before achieving profitability.

Our business could be adversely affected by any worsening of economic conditions.

We derive substantial revenues from the sale of advertising on our networks. Expenditures by advertisers tend to be cyclical, reflecting overall economic conditions, as well as budgeting and buying patterns. A deterioration in the current economic conditions may adversely affect the economic prospects of advertisers and could alter current or prospective advertisers' spending priorities. A decrease in advertising expenditures would have an adverse effect on our business. A decline in economic conditions usually impacts consumer discretionary spending. A reduction in consumer spending may impact pay television subscriptions, particularly to the more expensive digital service tiers, which could lead to a decrease in our distribution fees and may reduce the rates we can charge for advertising.

Our substantial leverage and debt service obligations may adversely affect us.

As of December 31, 2013, we had approximately \$6.5 billion of consolidated debt, including capital leases. Our substantial level of indebtedness increases the possibility that we may be unable to generate cash sufficient to pay when due the principal of, interest on, or other amounts associated with our indebtedness. In addition, we have the ability to draw down our revolving credit facility in the ordinary course, which would have the effect of increasing our indebtedness. We are also permitted, subject to certain restrictions under our existing indebtedness, to obtain additional long-term debt and working capital lines of credit to meet future financing needs. This would have the effect of increasing our total leverage.

Our substantial leverage could have significant negative consequences on our financial condition and results of operations, including:

- impairing our ability to meet one or more of the financial ratio covenants contained in our debt agreements or to generate cash sufficient to pay interest or principal, which could result in an acceleration of some or all of our outstanding debt in the event that an uncured default occurs;
- increasing our vulnerability to general adverse economic and market conditions;
- limiting our ability to obtain additional debt or equity financing;
- requiring the dedication of a substantial portion of our cash flow from operations to service our debt, thereby reducing the amount of cash flow available for other purposes;
- requiring us to sell debt or equity securities or to sell some of our core assets, possibly on unfavorable terms, to meet payment obligations;
- limiting our flexibility in planning for, or reacting to, changes in our business and the markets in which we compete; and
- placing us at a possible competitive disadvantage with less leveraged competitors and competitors that may have better access to capital resources.

The loss of key talent could disrupt our business and adversely affect our revenue.

Our business depends upon the continued efforts, abilities and expertise of our corporate and divisional executive teams and entertainment personalities. We employ or contract with entertainment personalities who may have loyal audiences. These individuals are important to audience endorsement of our programs and other content. There can be no assurance that these individuals will remain with us or retain their current audiences. If we fail to retain key individuals or if our entertainment personalities lose their current audience base, our operations could be adversely affected.

Restrictive covenants in the loan agreement for our revolving credit facility could adversely affect our business by limiting our flexibility.

The loan agreement for our revolving credit facility contains restrictive covenants, as well as requirements to comply with certain leverage and other financial maintenance tests. These covenants and requirements could limit our ability to take various actions, including incurring additional debt, guaranteeing indebtedness and engaging in various types of transactions, including

mergers, acquisitions and sales of assets. These covenants could place us at a disadvantage compared to some of our competitors, who may have fewer restrictive covenants and may not be required to operate under these restrictions. Further, these covenants could have an adverse effect on our business by limiting our ability to take advantage of financing, mergers and acquisitions or other opportunities.

We are a holding company and could be unable in the future to obtain cash in amounts sufficient to service our financial obligations or meet our other commitments.

Our ability to meet our financial obligations and other contractual commitments will depend upon our ability to access cash. We are a holding company, and our sources of cash include our available cash balances, net cash from the operating activities of our subsidiaries, any dividends and interest we may receive from our investments, availability under our credit facility or any credit facilities that we may obtain in the future and proceeds from any asset sales we may undertake in the future. The ability of our operating subsidiaries, including Discovery Communications, LLC, to pay dividends or to make other payments or advances to us will depend on their individual operating results and any statutory, regulatory or contractual restrictions, including restrictions under our credit facility, to which they may be or may become subject. We are required to accrue and pay U.S. taxes for repatriation of certain cash balances held by foreign corporations. However, we intend to permanently reinvest these funds outside of the U.S. and our current plans do not demonstrate a need to repatriate them to fund our U.S. operations.

Risks associated with our international operations could harm our financial condition.

Our networks are offered worldwide, and we are focused on expanding our international operations in key markets, some of which are emerging markets. Inherent economic risks of doing business in international markets include, among other things, changes in the economic environment, exchange controls, tariffs and other trade barriers, longer payment cycles, foreign taxation, corruption, and increased risk of political instability in some markets. As we continue to expand the provision of our products and services to international markets, these risks and uncertainties may harm our results of operations.

Furthermore, some foreign markets where we and our partners operate may be more adversely affected by current economic conditions than the U.S. We also may incur substantial expense as a result of changes, including the imposition of new restrictions, in the existing economic or political environment in the regions where we do business. Acts of terrorism, hostilities, or financial, political, economic or other uncertainties could lead to a reduction in revenue or loss of investment, which could adversely affect our results of operations.

Fluctuations in foreign exchange rates could have an adverse effect on our results of operations.

We have significant operations in a number of foreign jurisdictions and certain of our operations are conducted in foreign currencies. The value of these currencies fluctuates relative to the U.S. dollar. As a result, we are exposed to exchange rate fluctuations, which could have an adverse effect on our results of operations in a given period or in specific markets.

Financial market conditions may impede access to or increase the cost of financing our operations and investments. The ongoing changes in U.S. and global financial and equity markets, including market disruptions and tightening of the credit markets, may make it more difficult for us to obtain financing for our operations or investments or increase the cost of obtaining financing. In addition, our borrowing costs can be affected by short and long-term debt ratings assigned by independent rating agencies which are based, in significant part, on our performance as measured by credit metrics such as interest coverage and leverage ratios. A low rating could increase our cost of borrowing or make it more difficult for us to obtain future financing.

Our business is subject to risks of adverse laws and regulations, both domestic and foreign.

Programming services like ours, and the distributors of our services, including cable operators, satellite operators and other multichannel video programming distributors, are highly regulated by U.S. federal laws and regulations issued and administered by various federal agencies, including the FCC, as well as by state and local governments, in ways that affect the daily conduct of our video content business. See the discussion under “Business – Regulatory Matters” above. The U.S. Congress, the FCC and the courts currently have under consideration, and may adopt in the future, new laws, regulations and policies regarding a wide variety of matters that could, directly or indirectly, affect the operations of our U.S. media properties or modify the terms under which we offer our services and operate. For

example, any changes to the laws and regulations that govern the services or signals that are carried by cable television operators or our other distributors may result in less capacity for other content services, such as our networks, which could adversely affect our revenue.

Similarly, the foreign jurisdictions in which our networks are offered have, in varying degrees, laws and regulations governing our businesses. Programming businesses are subject to regulation on a country-by-country basis. Changes in regulations imposed by foreign governments could also adversely affect our business, results of operations and ability to expand our operations beyond their current scope.

Piracy of our entertainment content, including digital piracy, may decrease revenue received from our entertainment content and adversely affect our business and profitability.

The success of our business depends in part on our ability to maintain the intellectual property rights to our entertainment content. We are fundamentally a content company, and piracy of our brands, television networks, digital content and other intellectual property has the potential to significantly and adversely affect us. Piracy is particularly prevalent in many parts of the world that lack copyright and other protections similar to existing law in the U.S. It is also made easier by technological advances allowing the conversion of content into digital formats, which facilitates the creation, transmission and sharing of high-quality unauthorized copies. Unauthorized distribution of copyrighted material over the Internet is a threat to copyright owners' ability to protect and exploit their property. The proliferation of unauthorized use of our content may have an adverse effect on our business and profitability because it reduces the revenue that we potentially could receive from the legitimate sale and distribution of our content.

Our directors overlap with those of Liberty Media Corporation ("Liberty Media"), Liberty Global plc ("Liberty Global"), Liberty Interactive Corporation ("Liberty Interactive") and certain related persons of Advance/Newhouse, which may lead to conflicting interests.

Our eleven-person board of directors includes two persons who are currently members of the board of directors of Liberty Media, three persons who are currently members of the board of directors of Liberty Global and two persons who are currently members of the board of directors of Liberty Interactive, all of which include John C. Malone as Chairman of the boards of those companies. In addition, our board of directors includes three designees of Advance/Newhouse, including Robert J. Miron, who was the Chairman of Advance/Newhouse until December 31, 2010, and Steven A. Miron, the Chief Executive Officer of Advance/Newhouse. The Liberty entities and the parent company of Advance/Newhouse own interests in a range of media, communications and entertainment businesses. None of the Liberty entities owns any interest in us. Dr. Malone beneficially owns stock of Liberty Media representing approximately 47% of the aggregate voting power of its outstanding stock, owns shares representing approximately 27% of the aggregate voting power of Liberty Global, shares representing approximately 35% of the aggregate voting power of Liberty Interactive, and shares representing approximately 22% of the aggregate voting power (other than with respect to the election of the common stock directors) of our outstanding stock. Dr. Malone controls approximately 29% of our aggregate voting power relating to the election of our eight common stock directors, assuming that the preferred stock owned by Advance/Newhouse has not been converted into shares of our common stock. Our directors who are also directors of the Liberty entities own Liberty Media, Liberty Global and/or Liberty Interactive stock and stock incentives and own our stock and stock incentives.

Advance/Newhouse will elect three directors annually for so long as it owns a specified minimum amount of our Series A convertible preferred stock. The Advance/Newhouse Series A convertible preferred stock, which votes with our common stock on all matters other than the election of directors, represents approximately 25% of the voting power of our outstanding shares. The Series A convertible preferred stock also grants Advance/Newhouse consent rights over a range of our corporate actions, including fundamental changes to our business, the issuance of additional capital stock, mergers and business combinations and certain acquisitions and dispositions.

These ownership interests and/or business positions could create, or appear to create, potential conflicts of interest when these individuals are faced with decisions that could have different implications for us, the Liberty entities, and/or Advance/Newhouse. For example, there may be the potential for a conflict of interest when we, on the one hand, or a Liberty entity, and/or Advance/Newhouse, on the other hand, look at acquisitions and other corporate opportunities that may be suitable for the other.

The members of our board of directors have fiduciary duties to us and our stockholders. Likewise, those persons who serve in similar capacities at Liberty Media, Liberty Global, Liberty Interactive or Advance/Newhouse have fiduciary duties to those companies. Therefore, such persons may have conflicts of interest or the appearance of conflicts of interest with respect to matters involving or affecting both respective companies, and there can be no assurance that the terms of any transactions will be as favorable to us or our subsidiaries as would be the case in the absence of a conflict of interest.

Our overlapping directors with Liberty Media, Liberty Global and Liberty Interactive may result in the diversion of business opportunities and other potential conflicts.

Liberty Media, Liberty Global and Liberty Interactive own interests in various U.S. and international companies that have subsidiaries that own or operate domestic or foreign content services that may compete with the content services we offer. We have no rights in respect of U.S. or international content opportunities developed by or presented to the subsidiaries of Liberty Media, Liberty Global and Liberty Interactive, and the pursuit of these opportunities by such subsidiaries may adversely affect our interests and those of our stockholders. Because we and these Liberty entities have overlapping directors, the pursuit of business opportunities may serve to intensify the conflicts of interest or appearance of conflicts of interest faced by the respective management teams. Our charter provides that none of our directors or officers will be liable to us or any of our subsidiaries for

breach of any fiduciary duty by reason of the fact that such individual directs a corporate opportunity to another person or entity (including Liberty Media, Liberty Global or Liberty Interactive), for which such individual serves as a director or officer, or does not refer or communicate information regarding such corporate opportunity to us or any of our subsidiaries, unless (x) such opportunity was expressly offered to such individual solely in his or her capacity as a director or officer of us or any of our subsidiaries and (y) such opportunity relates to a line of business in which we or any of our subsidiaries is then directly engaged.

The personal educational media, lifelong learning, and travel and automotive industry investments by John S. Hendricks, a common stock director and our Founder, may conflict with or compete with our business activities. Our Founder, John S. Hendricks, manages his non-Discovery, personal business investments through Hendricks Investment Holdings LLC (“HIH”), a Delaware limited liability company of which he is the sole owner and member. HIH owns a travel club and travel-related properties including a resort in Gateway, Colorado and has created a learning academy for guests that includes on-line and advanced media offerings in the area of informal and lifelong learning. Certain video productions and offerings of this academy may compete with our educational media offerings. We and the academy may enter into a business arrangement for the offering of our video products for sale by the academy and/or for the joint-production of new educational media products or co-production agreements for content to be aired on our networks, such as the Curiosity series. In addition, from time to time, HIH or its subsidiaries may enter into transactions with us or our subsidiaries. For example, through HIH, Mr. Hendricks owns a number of business interests in the automotive field, some of which are involved in content offered by us, in particular on our Velocity network. There can be no assurance that the terms of any such transactions will be as favorable to us or our subsidiaries as would be the case in the absence of a conflict of interest.

It may be difficult for a third party to acquire us, even if doing so may be beneficial to our stockholders.

Certain provisions of our charter and bylaws may discourage, delay or prevent a change in control that a stockholder may consider favorable. These provisions include the following:

- authorizing a capital structure with multiple series of common stock: a Series B that entitles the holders to ten votes per share, a Series A that entitles the holders to one vote per share and a Series C that, except as otherwise required by applicable law, entitles the holders to no voting rights;
- authorizing the Series A convertible preferred stock with special voting rights, which prohibits us from taking any of the following actions, among others, without the prior approval of the holders of a majority of the outstanding shares of such stock:
  - increasing the number of members of the Board of Directors above 11;
  - making any material amendment to our charter or by-laws;
  - engaging in a merger, consolidation or other business combination with any other entity; and
  - appointing or removing our Chairman of the Board or our Chief Executive Officer;
- authorizing the issuance of “blank check” preferred stock, which could be issued by our Board of Directors to increase the number of outstanding shares and thwart a takeover attempt;
- classifying our common stock directors with staggered three-year terms and having three directors elected by the holders of the Series A convertible preferred stock, which may lengthen the time required to gain control of our Board of Directors;
- limiting who may call special meetings of stockholders;
- prohibiting stockholder action by written consent (subject to certain exceptions), thereby requiring stockholder action to be taken at a meeting of the stockholders;
  - establishing advance notice requirements for nominations of candidates for election to our Board of Directors or for proposing matters that can be acted upon by stockholders at stockholder meetings;
- requiring stockholder approval by holders of at least 80% of our voting power or the approval by at least 75% of our board of directors with respect to certain extraordinary matters, such as a merger or consolidation, a sale of all or substantially all of our assets or an amendment to our charter;
- requiring the consent of the holders of at least 75% of the outstanding Series B common stock (voting as a separate class) to certain share distributions and other corporate actions in which the voting power of the Series B common



stock would be diluted by, for example, issuing shares having multiple votes per share as a dividend to holders of Series A common stock; and

the existence of authorized and unissued stock which would allow our Board of Directors to issue shares to persons friendly to current management, thereby protecting the continuity of our management, or which could be used to dilute the stock ownership of persons seeking to obtain control of us.

We have also adopted a shareholder rights plan in order to encourage anyone seeking to acquire us to negotiate with our Board of Directors prior to attempting a takeover. While the plan is designed to guard against coercive or unfair tactics to gain control of us, the plan may have the effect of making more difficult or delaying any attempts by others to obtain control of us.

Holders of any single series of our common stock may not have any remedies if any action by our directors or officers has an adverse effect on only that series of common stock.

Principles of Delaware law and the provisions of our charter may protect decisions of our Board of Directors that have a disparate impact upon holders of any single series of our common stock. Under Delaware law, the Board of Directors has a duty to act with due care and in the best interests of all of our stockholders, including the holders of all series of our common stock. Principles of Delaware law established in cases involving differing treatment of multiple classes or series of stock provide that a board of directors owes an equal duty to all common stockholders regardless of class or series and does not have separate or additional duties to any group of stockholders. As a result, in some circumstances, our directors may be required to make a decision that is adverse to the holders of one series of common stock. Under the principles of Delaware law referred to above, stockholders may not be able to challenge these decisions if our Board of Directors is disinterested and adequately informed with respect to these decisions and acts in good faith and in the honest belief that it is acting in the best interests of all of our stockholders.

The exercise by Advance/Newhouse of its registration rights may cause our stock price to decline significantly, even if our business is doing well.

Advance/Newhouse has been granted registration rights covering all of the shares of common stock issuable upon conversion of the convertible preferred stock held by Advance/Newhouse. Advance/Newhouse's preferred stock is currently convertible into shares of our Series A and Series C common stock on a 1-for-1 basis, subject to certain anti-dilution adjustments. The registration rights, which are immediately exercisable, are transferable with the sale or transfer by Advance/Newhouse of blocks of shares representing 10% or more of the preferred stock it holds. The exercise of the registration rights, and subsequent sale of possibly large amounts of our common stock in the public market, could materially and adversely affect the market price of our common stock.

John C. Malone and Advance/Newhouse each have significant voting power with respect to corporate matters considered by our stockholders.

For corporate matters other than the election of directors, Dr. Malone and Advance/Newhouse each beneficially own shares of our stock representing approximately 22% and 25%, respectively, of the aggregate voting power represented by our outstanding stock. With respect to the election of directors, Dr. Malone controls approximately 29% of the aggregate voting power relating to the election of the eight common stock directors (assuming that the convertible preferred stock owned by Advance/Newhouse (the "A/N Preferred Stock") has not been converted into shares of our common stock). The A/N Preferred Stock carries with it the right to designate three preferred stock directors to our board (subject to certain conditions), but does not vote with respect to the election of the eight common stock directors. Also, under the terms of the A/N Preferred Stock, Advance/Newhouse has special voting rights as to certain enumerated matters, including material amendments to the restated charter and bylaws, fundamental changes in our business, mergers and other business combinations, certain acquisitions and dispositions and future issuances of capital stock. Although