the change during the period in deferred tax assets and liabilities. Components of the income tax provision are as follows:

		Years ended December 31,	
	2004	2003	2002
		amounts in thousands	
Current			
Federal	$ —	—	2,918
State	502	(1,100)	(1,302)
Foreign	(3,780)	(1,403)	202
Current	(3,278)	(2,503)	1,818
Deferred			
Federal	(25,221)	(15,628)	24,536
State	(7,774)	(3,494)	4,522
Foreign	1,303	1,469	(397)
Deferred	(31,692)	(17,653)	28,661
Total tax benefit (expense)	$ (34,970)	(20,156)	30,479

ncome tax benefit (expense) differs from the amounts computed by applying the U.S. federal income tax rate of 35% as a result of the following:

		Years ended December 31,	
	2004	2003	2002
		amounts in thousands	
Computed expected tax benefit (expense)	$ (35,377)	11,283	48,834
Impairment charges and amortization of goodwill not deductible for income tax purposes	—	—	(29,301)
State and local income taxes, net of federal income taxes	(5,311)	(2,986)	2,225
Change in valuation allowance affecting tax expense	3,575	(14,719)	(8,747)
Disallowed interest expense	—	(13,963)	(8,655)
Dividend received deduction	—	—	15,195
Disposition of nondeductible goodwill in sales transactions	—	—	8,590
Other, net	2,143	229	2,338
Income tax benefit (expense)	$ (34,970)	(20,156)	30,479

THIS PAGE INTENTIONALLY LEFT BLANK

Components of pretax income (loss), excluding change in accounting principle, are as follows:

	Years ended December 31,		
	2004	2003	2002
	amounts in thousands		
Domestic	$ 96,470	(28,772)	(149,476)
Foreign	4,608	(3,466)	9,949
	$ 101,078	(32,238)	(139,527)

Components of deferred tax assets and liabilities as of December 31 are as follows:

	2004	2003
	amounts in thousands	
Current assets:		
Accounts receivable reserves	$ 2,423	3,424
Accrued liabilities	11,987	8,552
	14,410	11,976
Noncurrent assets:		
Net operating loss carryforwards	56,689	79,587
Impairment reserves	2,370	4,747
Intangible assets	5,775	9,559
Other	6,960	5,843
	71,794	99,736
Total deferred tax assets, gross	86,204	111,712
Valuation allowance	(76,452)	(101,470)
Total deferred tax assets, net	9,752	10,242
Current liabilities:		
Prepaid expenses	(1,204)	(1,362)
Other	(2,802)	(2,040)
	(4,006)	(3,402)
Noncurrent liabilities:		
Property and equipment	(2,760)	(5,287)

Investments	(1,086,950)	(1,054,666)
	(1,089,710)	(1,059,953)
Total deferred tax liabilities	(1,093,716)	(1,063,355)
Net deferred tax liability	$ (1,083,964)	(1,053,113)

At December 31, 2004, the Company has $119,474,000 and $371,840,000 in net operating loss carryforwards for federal and state tax purposes, respectively. These net operating losses expire, for federal purposes, in 2022 and 2023.

The state NOL's begin expiring in 2005 and continue through 2021. In addition, the Company has approximately $600,000 of federal income tax credits, which may be carried f
initely. The Company has $2,510,000 of state income tax credits, of which $2,342,000 will expire in the year 2012.

During the current year, management has determined that it is more likely than not that the Company will not realize the tax benefits associated with certain cumulative net oper
carryforwards and other deferred tax assets. As such, the Company continues to maintain a valuation allowance of $76,452,000. The total valuation allowance decreased during t
ended December 31, 2004 as a result of other members in the Liberty consolidated tax group utilizing fully reserved NOLs of Ascent Media of $21,442,000 and utilization by A
a of fully reserved deferred tax assets of $3,576,000. Ascent Media has not recorded a receivable from Parent for the utilization of its NOL's since it is unlikely they will ever be
ursed by Liberty for these benefits.

During 2004, the Company provided $1,636,000 of U.S. tax expense for future repatriation of cash from its Asia operations pursuant to APB 23. This charge represents all
tributed earnings from Asia not previously taxed in the United States.

Undistributed earnings of foreign subsidiaries, other than the Asia operations, aggregated $3,372,000 on December 31, 2004, which, under existing law, will not be subject to U
distributed as dividends. Since the earnings have been, or are intended to be, indefinitely reinvested in foreign operations, no provision has been made for any U.S. taxes that ma
able thereto. Furthermore, any taxes paid to foreign governments on those earnings may be used in whole or in part as credits against the U.S. tax on any dividends distributed
earnings. It is not practicable to estimate the amount of unrecognized deferred U.S. taxes on these undistributed earnings.

mployee Benefit Plans

scent Media offers a 401(k) defined contribution plan covering most of its full-time domestic employees not covered by employees eligible to participate in the Motion Picture
ry Pension and Health Plan (MPIPHP), a multi-employer defined benefit pension plan. Contributions to the MPIPHP are determined in accordance with the provisions of negot
contracts and generally are based on the number of hours worked. Ascent Media also sponsors a pension plan for eligible employees of its foreign subsidiaries. Employer
butions are determined by Ascent Media's board of directors. The plans are funded by employee and employer contributions. Total pension plan expenses for the years ended
nber 31, 2004, 2003 and 2002 were $6,485,000, $6,380,000 and $5,794,000, respectively.

ommitments and Contingencies

uture minimum lease payments under scheduled operating leases that have initial or remaining noncancelable terms in excess of one year are as follows (in thousands):

Year ended December 31:		
2005	$	25,682
2006	$	23,462
2007	$	22,362
2008	$	19,665
2009	$	17,608
Thereafter	$	52,523

Rent expense for noncancelable operating leases for real property and equipment was $26,487,000, $21,909,000 and $29,632,000 for the years ended December 31, 2004, 2003 respectively. Various lease arrangements contain options to extend terms and are subject to escalation clauses.

At December 31, 2004, the Company is committed to compensation under long-term employment agreements with its certain executive officers of Ascent Media as follows: 200 2,000; 2006, $1,778,000; and 2007, $296,000.

The Company is involved in litigation and similar claims incidental to the conduct of its business. In management's opinion, none of the pending actions is likely to have a mate se impact on the Company's financial position or results of operations.

Related Party Transactions

ces Agreement Between Ascent Media and On Command Corporation

Since October 1, 2002, Ascent Media has provided uplink and satellite transport services to On Command Corporation ("On Command"), a wholly owned subsidiary of LMC. U rms of short-term services agreement and a content preparation and distribution services agreement, from October 1, 2002 through March 31, 2008, Ascent Media has provided, ontinue to provide, uplink and satellite transport services. The content preparation and distribution services agreement also provides that Ascent Media may supply content prep es. During the period from April 2003 to October 2004, Ascent Media also installed satellite equipment at On Command's downlink sites at hotels pursuant to a separate servic ment. All agreements were entered into in the ordinary course of business on arm's-length terms. Ascent Media has provided $449,000, $691,000 and $75,000 in services to On mand for the years ended December 31, 2004, 2003 and 2002, respectively.

Related Party Balances and Transactions

scent Media provides services, such as satellite uplink, systems integration, origination, and post-production, to various affiliates of Liberty including DCI and Court Televisio rk, LLC. Revenue recorded by Ascent Media for these services for the years ended December 31, 2004, 2003 and 2002 aggregated $41,785,000, $13,355,000 and $14,043,000 tively.

nformation About Operating Segments

he Company's business units have been aggregated into four reportable segments: the Creative Services Group, the Media Management Services Group, and the Network Servi , which are all operating segments of Ascent Media, and DCI, which is an equity affiliate. Corporate related items and unallocated income and expenses are reflected in the Cor her column listed below.

he Creative Services Group provides post-production services, which are comprised of services necessary to complete the creation of original content including feature films, ion shows, movies of the week/mini series, television commercials, music videos, promotional and identity campaigns and corporate communications programming. The Medi gement Services Group provides content storage services, which are comprised of facilities and services necessary to optimize, archive, manage and repurpose media assets for ution via freight, satellite, fiber and the Internet; access to all forms of content, duplication and formatting services, language conversions and laybacks, restoration and preserva or damaged content, mastering from motion picture film to high resolution or data formats, digital audio and video encoding services and digital media management services fo

l home video, broadcast, pay-per-view and emerging new media distribution channels. The Network Services Group provides broadcast services, which are comprised of servic
sary to assemble and distribute programming for cable and broadcast networks via fiber and satellite to viewers in North America, Europe and Asia. Additionally, the networks
ces group provides systems integration, design, consulting, engineering and project management services.

The Company's chief operating decision maker, or his designee (the "CODM"), has identified the Company's reportable segments based on (i) financial information reviewed by
M and (ii) those operating segments that represent more than 10% of the Company's combined revenue or earnings before taxes. In addition, those equity investments whose sh
ngs represent more than 10% of the Company's earnings before taxes are considered reportable segments.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies and are consistent with GAAP.

The Company evaluates the performance of these operating segments based on financial measures such as revenue and operating cash flow. The Company defines operating cas
venue less operating expenses and selling, general and administrative expenses (excluding stock and other equity-based compensation). The Company believes this is an importa
ator of the operational strength and performance of its businesses, including the ability to service debt and capital expenditures. In addition, this measure allows management to
ting results and perform analytical comparisons and identify strategies to improve performance. This measure of performance excludes depreciation and amortization, stock and
-based compensation and restructuring and impairment charges that are included in the measurement of operating income pursuant to GAAP. Accordingly, operating cash flow
d be considered in addition to, but not as a substitute for, operating income, cash flow provided by operating activities and other measures of financial performance prepared in
dance with GAAP.

;ummarized financial information concerning the Company's reportable segments is presented in the following tables:

Media		Creative Services Group	Media Management Services Group	Network Services Group(1)	DCI	Corporate and Other and eliminations	Total
				amounts in thousands			
Ended December 31, 2004							
evenue from external customers	$	295,841	109,982	225,392	2,365,346	(2,365,346)	631,215
perating cash flow	$	55,847	17,430	62,163	662,690	(700,764)	97,366
pital expenditures	$	18,677	4,142	23,114	88,100	(84,741)	49,292
epreciation and amortization	$	31,026	7,750	27,074	129,011	(117,256)	77,605
tal assets	$	298,613	171,588	294,328	3,235,686	1,564,613	5,564,828
Ended December 31, 2003							
evenue from external customers	$	270,830	107,070	128,203	1,995,047	(1,995,047)	506,103
perating cash flow	$	43,786	22,074	43,221	508,452	(542,771)	74,762
pital expenditures	$	13,132	4,751	5,207	109,956	(107,183)	25,863
epreciation and amortization	$	28,975	11,481	22,171	120,172	(112,274)	70,526
tal assets	$	305,576	174,916	239,939	3,194,211	1,481,985	5,396,627
Ended December 31, 2002							
evenue from external customers	$	275,119	105,091	159,123	1,716,775	(1,716,775)	539,333
perating cash flow	$	50,150	27,682	45,673	378,633	(413,083)	89,055
pital expenditures	$	22,825	15,406	9,958	138,777	(130,608)	56,358
epreciation and amortization	$	38,778	7,483	18,863	112,841	(110,693)	67,272

Included in Network Services Group revenue is broadcast services revenue of $135,883,000, $89,065,000 and $114,400,000 and systems integration revenue of $89,509,000, $39,138,000 and $44,723,000 in 2004, 2003 and 2002, respectively.

'he Company's reportable segments are strategic business units that offer different products and services. They are managed separately because each segment requires different ›logies, distribution channels and marketing strategies.

he following table provides a reconciliation of segment operating cash flow to earnings (loss) before income taxes, minority interest and change in accounting principle.

	Years ended December 31,		
	2004	2003	2002
	amounts in thousands		
Segment operating cash flow	$ 97,366	74,762	89,055
Stock compensation	(2,775)	(2,602)	48
Depreciation and amortization	(77,605)	(70,526)	(67,272)
Impairment of goodwill	(51)	(562)	(83,718)
Share of earnings (losses) of DCI	84,011	37,271	(32,046)
Interest expense	—	(72,178)	(64,820)
Other, net	132	(655)	17,674
Earnings (loss) before income taxes, minority interest and change in accounting principle	$ 101,078	(34,490)	(141,079)

formation as to the Company's operations in different geographic areas is as follows:

	Years ended December 31,		
	2004	2003	2002
	amounts in thousands		
Revenue			
United States	$ 460,070	390,220	420,827
United Kingdom	148,002	92,523	93,797
Other countries	23,143	23,360	24,709
	$ 631,215	506,103	539,333

Report of Independent Registered Public Accounting Firm

e Board of Directors and Stockholders of
very Communications, Inc.:

n our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, of changes in stockholders' deficit, and of cash flows preser , in all material respects, the financial position of Discovery Communications, Inc. and its subsidiaries at December 31, 2004 and 2003, and the results of their operations and th lows for each of the three years in the period ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America. These fin nents are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audi statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to able assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and sures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement present elieve that our audits provide a reasonable basis for our opinion.

vaterhouseCoopers LLP
an, Virginia
ary 22, 2005

Discovery Communications, Inc.

Consolidated Balance Sheets

	December 31, 2004	December 31, 2003
	In thousands, except share data	
S		
assets		
h and cash equivalents	$ 24,282	$ 34,075
ounts receivable, less allowances of $24,375 and $40,213	527,659	466,747
entories	32,567	37,004
erred income taxes	144,606	232,693
gramming rights, net	50,578	46,364
er current assets	55,758	41,500
rrent assets	835,450	858,383
perty and equipment, net	380,290	360,411
gramming rights, net, less current portion	1,027,379	881,735
erred launch incentives	314,601	373,579
dwill	257,460	253,308
ngibles, net	187,761	213,660
stments in and advances to unconsolidated affiliates	74,450	60,765
erred income taxes	114,673	146,768
er assets	43,622	45,602
ASSETS	$ 3,235,686	$ 3,194,211
ITIES AND STOCKHOLDERS' DEFICIT		
liabilities		
ounts payable and accrued liabilities	$ 338,182	$ 356,320
nch incentives payable	33,509	62,841
gramming rights payable	94,969	73,340
rent portion of long-term incentive plan liabilities	261,627	427,755
rent portion of long-term debt	9,736	517,750
ome taxes payable	21,123	10,564
er current liabilities	126,207	90,228
rrent liabilities	885,353	1,538,798
m debt, less current portion	2,498,287	1,833,942
ve financial instruments, less current portion	46,541	88,781
incentives payable, less current portion	34,328	45,422
m incentive plan liabilities, less current portion	60,735	63,844
ming *rights payable, less current* portion	8,027	3,668
bilities	10,774	11,269
bilities	3,544,045	3,585,724
rily redeemable *interests in subsidiaries*	319,567	410,252
ments and contingencies		
lders' deficit		
s A common stock; $.01 par value; *100,000 shares authorized*; 51,119 shares issued, less 719 and 504 shares of treasury stock	1	1

Class B common stock; $.01 par value; 60,000 shares authorized; 50,615 shares issued and held in treasury stock at December 31, 2004 and 2003	—	—
Additional paid-in capital	21,093	21,093
Accumulated deficit	(672,931)	(840,953)
Accumulated other comprehensive income	23,911	18,094
Total stockholders' deficit	(627,926)	(801,765)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT	$ 3,235,686	$ 3,194,211

The accompanying notes are an integral part of these consolidated financial statements.

Discovery Communications, Inc.

Consolidated Statements of Operations

		Year ended December 31,	
	2004	2003	2002
		In thousands	
RATING REVENUE			
tising	$ 1,133,807	$ 1,010,585	$ 829,936
riber fees	976,362	747,927	646,500
	255,177	236,535	240,339
operating revenue	2,365,346	1,995,047	1,716,775
f revenue	846,316	751,578	699,737
g, general & administrative	856,340	735,017	638,405
ses arising from long-term incentive plans	71,515	74,119	96,865
ciation & amortization	129,011	120,172	112,841
n sale of patents	(22,007)	—	—
operating expenses	1,881,175	1,680,886	1,547,848
ME FROM OPERATIONS	484,171	314,161	168,927
ER INCOME (EXPENSE)			
t, net	(167,420)	(159,409)	(163,315)
lized gains (losses) from derivative instruments, net	45,540	21,405	(11,607)
ity interests in consolidated subsidiaries	(54,940)	(35,965)	(45,977)
in earnings (losses) of unconsolidated affiliates	171	(4,477)	(2,716)
	2,299	2,307	(3,425)
other expense, net	(174,350)	(176,139)	(227,040)
ME (LOSS) BEFORE INCOME TAXES	309,821	138,022	(58,113)
e tax expense (benefit)	141,799	74,785	(10,057)
NCOME (LOSS)	$ 168,022	$ 63,237	$ (48,056)

The accompanying notes are an integral part of these consolidated financial statements.

Discovery Communications, Inc.

Consolidated Statements of Cash Flows

	Year ended December 31, 2004	2003	2002
		In thousands	
TING ACTIVITIES			
me (loss)	$ 168,022	$ 63,237	$ (48,056)
ents to reconcile net income (loss) to cash provided by operations			
reciation and amortization	129,011	120,172	112,841
rtization of *deferred launch incentives and representation rights*	107,757	131,980	132,495
vision for losses on accounts receivable, net	959	11,413	20,787
enses arising from long-term incentive plans	71,515	74,119	96,865
ity in (earnings) losses of unconsolidated affiliates	(171)	4,477	2,716
erred income taxes	105,522	42,280	(37,801)
alized (gains) *losses on derivative financial instruments*, net	(45,540)	(21,405)	11,607
cash minority interest charges	54,940	35,965	45,977
on sale of patents	(22,007)	—	—
r non-cash charges	8,300	5,584	14,325
nges in assets and liabilities, net of business combinations			
Accounts receivable	(60,841)	(52,753)	(46,553)
Inventories	4,555	22,978	(30,504)
Other assets	(14,706)	(10,212)	(8,435)
Programming rights, net of payables	(122,433)	(139,387)	(86,103)
Accounts payable and accrued liabilities	55,734	27,646	79,565
Representation rights	(479)	(11,250)	(10,750)
Deferred launch incentives	(74,696)	(99,630)	(72,963)
Long-term incentive plan liabilities	(240,752)	(51,023)	(37,003)
vided by operations	124,690	154,191	139,010
TING ACTIVITIES			
ion of property and equipment	(88,100)	(109,956)	(138,777)
combinations, net of cash acquired	(17,218)	(46,541)	—
ents in and advances to unconsolidated *affiliates*	(14,884)	(11,754)	(27,389)
tions from minority shareholders	3,146	21,652	12,478
(redemption) of interests in subsidiaries	(148,880)	—	92,874
from sale of patents, net	22,007	—	—
d by investing activities	(243,929)	(146,599)	(60,814)
CING ACTIVITIES			
from issuance of long-term debt	1,848,000	—	391,924
payments of long-term debt	(1,699,215)	(12,638)	(330,165)
financing fees	(8,499)	(56)	(1,358)
in note receivable from stockholder	—	(5,238)	(10,246)
on of note receivable from stockholder	—	23,600	—
ase of Class A common stock	—	(55,334)	—
ase of Class B common stock	—	—	(109,000)
ancing	(30,840)	42,325	(23,415)
vided (used) by financing activities	109,446	(7,341)	(82,260)
GE IN CASH AND CASH EQUIVALENTS	(9,793)	251	(4,064)
l cash equivalents, beginning of year	34,075	33,824	37,888
ND CASH EQUIVALENTS, END OF YEAR	$ 24,282	$ 34,075	$ 33,824

The accompanying notes are an integral part of these consolidated financial statements.

Discovery Communications, Inc.

Consolidated Statements of Changes in Stockholders' Deficit

	Class A		Class B			Other Comprehensive Income (Loss)		
	At Par	Redeemable	At Par	Additional Paid-In Capital	Accumulated Deficit	Foreign Currency Translation	Unrealized Gain (Loss) on Investments	TOTAL
					In thousands			
ce, December 31, 2001	$ 1	$ 52,791	$ 1	$ 121,092	$ (852,707)	$ (2,272)	$ (334)	$ (681,4
rehensive loss								
Net loss					(48,056)			
Foreign currency translation, net of tax of $2.7 million						6,568		
Realized loss on investments, net of tax of $0.2 million							334	
comprehensive loss								(41,1
se in loan to stockholder		(10,246)						(10,2
pensation from redeemable Class A common		2,324						2,3
tion of redeemable Class A common stock		5,827			(5,827)			
chase of Class B common stock treasury shares			(1)	(99,999)	(9,000)			(109,0
ce, December 31, 2002	$ 1	$ 50,696	$ —	$ 21,093	$ (915,590)	$ 4,296	$ —	$ (839,5
rehensive income								
Net income					63,237			
Foreign currency translation, net of tax of $5.7 million						10,027		
Unrealized gain on investments, net of tax of $2.4 million							3,771	
comprehensive income								77,0
ase in loan to stockholder		18,362						18,3
ction of compensation from redeemable Class A non stock		(2,324)						(2,3
tion of redeemable Class A common stock		(11,400)			11,400			
chase of Class A common stock treasury shares		(55,334)						(55,3
nce, December 31, 2003	$ 1	$ —	$ —	$ 21,093	$ (840,953)	$ 14,323	$ 3,771	$ (801,7
rehensive income								
Net income					168,022			
Foreign currency translation, net of tax of $5.2 million						8,409		
Unrealized loss on investments, net of tax of $1.7 million							(2,592)	
comprehensive income								173,8
nce, December 31, 2004	$ 1	$ —	$ —	$ 21,093	$ (672,931)	$ 22,732	$ 1,179	$ (627,9

The accompanying notes are an integral part of these consolidated financial statements.

THIS PAGE INTENTIONALLY LEFT BLANK

Discovery Communications, Inc.

Notes to Consolidated Financial Statements

Description of Business

Discovery Communications, Inc. (the "Company") is a privately held, diversified worldwide entertainment company whose operations are organized into four business units: U.S. works, International Networks, Commerce and Education. U.S. Networks operates cable and satellite television networks in the United States, including Discovery Channel, TLC, mal Planet, The Travel Channel and Discovery Health Channel. International Networks operates cable and satellite television networks worldwide, including regional variants of covery Channel, Animal Planet, People & Arts, Travel & Adventure, and Discovery Health Channel. Commerce operates 115 Discovery Channel retail stores as well as direct-to- umer sales in the United States, and manages licensing for the Company. Education provides products and services to educational institutions.

Summary of Significant Accounting Policies

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned and controlled subsidiaries. The equity method of accounting is used for onsolidated affiliates in which the Company's ownership interests range from 20% to 50% and the Company exercises significant influence over operating and financial policies. All ificant intercompany transactions and balances among the consolidated entities have been eliminated.

Use of Estimates

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported unts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reportin ods. Actual results may differ from those estimates and could have a material impact on the consolidated financial statements.

The Company has issued redeemable interests in a number of its consolidated subsidiaries for which the redemption events are outside of the Company's control. Estimating the mption values of these interests requires making assumptions regarding fair value, future performance, comparing to similar transactions, and complex contract interpretation.

Other significant estimates include the recoverability of programming rights, the amortization period and method of programming rights, valuation and recoverability of intangible ts and other long-lived assets, the fair value of derivative financial instruments, and the adequacy of reserves associated with accounts receivable and retail inventory.

Recent Accounting Pronouncements

In December 2003 the Financial Accounting Standards Board (FASB) issued *Consolidation of Variable Interest Entities: an Interpretation of FASB No. 51 (FIN 46R)* , which was ctive as of March 31, 2004. Variable interest entities (VIEs) are primarily entities that lack sufficient equity to finance their activities without additional financial support from other ies or whose equity holders possess governance rights that are not proportionate with their equity holdings. All VIEs with which the Company is involved must be evaluated to rmine the primary beneficiary of the risks and rewards of the VIE. The primary beneficiary is required to consolidate the VIE for financial reporting purposes.

The Company has minority interests in certain entities as discussed in Note 9. In connection with the adoption of FIN 46R, the Company's preliminary assessment is that certain of its aterial unconsolidated international joint ventures may be VIEs in which the Company is the primary beneficiary. Pursuant to the transition provisions of FIN 46R, the Company will n consolidating such ventures commencing 2005, however the impact on the consolidated financial statements is not expected to be material. See Note 9 for summarized balance shee ments of operations and cash flows of all equity method investments.

FASB Statement No. 150 *Financial Instruments with Characteristics of Both Liabilities and Equity* , (FAS 150) establishes standards for classifying and measuring as liabilities certa ncial instruments that embody obligations of the issuer and have traditionally been characterized as equity. The Financial Accounting Standards Board delayed the FAS 150 effective for nonpublic companies with respect to instruments that are mandatorily redeemable on fixed dates for amounts that are either fixed or determined by reference to an index to ary 1, 2005. If the Company were a public registrant, mandatorily redeemable minority interests in the amount of $142.9 million would be classified as current liabilities.

Revenue Recognition

The Company derives revenues from five primary sources: (1) advertising revenue for commercial spots aired on the Company's networks, (2) subscriber revenue from cable system ators (affiliates), (3) retail sales of consumer product inventory, (4) licensing of the Company's programming and other intellectual property, and (5) product and service sales to ational institutions.

Advertising revenue is recorded net of agency commissions and audience deficiency liabilities in the period when the advertising spots are broadcast. Subscriber revenue is recognize e period the service is provided, net of launch incentives and other vendor consideration. Retail revenues are recognized either at the point-of-sale or upon product shipment. Program sing revenues are recognized when the programming is available to broadcast and upon satisfaction of other revenue recognition conditions. Trademarks and other non-programming sing are generally recognized ratably over the term of the agreement. Product and service sales to educational institutions are generally recognized ratably over the term of the ement or as the product is delivered.

Advertising Costs

The Company expenses advertising costs as incurred. The Company incurred advertising costs of $170.3 million, $140.2 million and $111.9 million in 2004, 2003 and 2002.

Cash and Cash Equivalents

Highly liquid investments with original maturities of ninety days or less are recorded as cash equivalents. The Company had $4.3 million and $3.9 million in restricted cash included r assets as of December 31, 2004 and 2003 due to foreign currency restrictions.

Derivative Financial Instruments

Derivative financial instruments are recorded on the balance sheet at fair value. The Company did not apply hedge accounting during 2004, 2003 and 2002, and therefore changes in air values of derivative financial instruments are recorded in the statements of operations.

Inventories

Inventories are carried at the lower of cost or market and include inventory acquisition costs. Cost is determined using the weighted average cost method.

Programming Rights

Costs incurred in the direct production or licensing of programming rights are capitalized and stated at the lower of unamortized cost, fair value, or net realizable value. The Company uates the net realizable value of programming by considering the fair value and net realizable values of the underlying produced and licensed programs, respectively. The costs of uced programming are capitalized and amortized based on the expected realization of revenues, resulting in an accelerated basis over four years for developed networks (Discovery nnel, TLC, Animal Planet, and The Travel Channel) in the United States, a straight-line basis over three to five years for developing networks in the United States, and a straight-line s over three years for all International networks.

The cost of licensed programming is capitalized and amortized over the term of the license period based on the expected realization of revenues, resulting in an accelerated basis for loped networks in the United States, and a straight-line basis for all International networks and developing networks in the United States.

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Depreciation is recognized on a straight-line basis over the estimated useful lives of three to seven years for pment, furniture and fixtures, five to forty years for building structure and construction, and six to fifteen years for satellite transponders. Leasehold improvements are amortized on a ght-line basis over the lesser of their estimated useful lives or the terms of the related leases. Equipment under capital lease represents the present value of the minimum lease paymen e inception of the lease, net of accumulated depreciation.

Capitalized Software Costs

Capitalization of software development costs occurs during the application development stage. Costs incurred during the pre and post implementation stages are expensed as incurred talized software is amortized on a straight-line basis over its estimated useful lives of one to five years. Unamortized computer software costs totaled $55.2 million and $49.6 million ember 31, 2004 and 2003.

Recoverability of Long-Lived Assets, Goodwill, and Intangible Assets

The Company periodically reviews the carrying value of its acquired intangible assets, including goodwill, and its other long-lived assets, including deferred launch incentives, to rmine whether an impairment may exist. Goodwill impairment is determined by comparing the fair value of the reporting unit to its carrying value. If the fair value of the reporting un s than its carrying value, an impairment loss is recorded to the extent that the fair value of the goodwill within the reporting unit is less than its carrying value. Intangible assets and long-lived assets are grouped for purposes of evaluating recoverability at the lowest level for which independent cash flows are identifiable. If the carrying amount of an intangible , long-lived asset, or asset grouping exceeds its fair value, an impairment loss is recognized. Fair values for reporting units, goodwill and other intangible assets are rmined based on discounted cash flows, market multiples, or comparable assets as appropriate. Generally, the Company's reporting units and asset groups consist of the individual vorks or other operating units.

The determination of recoverability of goodwill and other intangible and long lived assets requires significant judgment and estimates regarding future cash flows, fair values, and th opriate grouping of assets. Such estimates are subject to change and could result in impairment losses being recognized in the future. If different reporting units, asset groupings, or erent valuation methodologies had been used, the impairment test results could have differed.

Deferred Launch Incentives

Consideration issued to cable affiliates in connection with the execution of long-term network distribution agreements is deferred and amortized on a straight-line basis as a reductior venue over the terms of the agreements. Obligations for fixed launch incentives are recorded at the inception of the agreement. Obligations for performance-based arrangements are rded when performance thresholds have been achieved. Following the extension or renewal of an original launch agreement, remaining deferred consideration is amortized over the period. Amortization of deferred launch incentives and interest on unpaid deferred launch incentives was $98.4 million, $122.7 million and $122.8 million in 2004, 2003 and 2002.

Foreign Currency Translation

The Company's foreign subsidiaries' assets and liabilities are translated at exchange rates in effect at the balance sheet date, while results of operations are translated at average ange rates for the respective periods. The resulting translation adjustments are included as a separate component of stockholders' equity in accumulated other comprehensive income. effect of exchange rate changes on cash balances held in foreign currencies impacting the Consolidated Statements of Cash Flows totals $2.5 million, $1.2 million, and $0.2 million ir , 2003 and 2002.

Long-term Compensation Programs

The Company grants unit awards under its long-term incentive plans. These unit awards, which vest over a period of years, are granted to employees and increase or decrease in valu d on a specified formula of certain business metrics of the Company. The Company accounts for these units similar to stock appreciation rights and applies the guidance in FASB rpretation Number 28, "Accounting for Stock Issued to Employees." The Company adjusts compensation expense for the changes in the accrued value of these awards over the vestin od.

Mandatorily Redeemable Interests in Subsidiaries

Mandatorily redeemable interests in subsidiaries are initially recorded at fair value and accreted or decreted to the estimated redemption value ratably over the period to the redempti , as appropriate. The Company records accretion and decretion on these instruments in minority interest expense.

Treasury Stock

Treasury stock is accounted for using the cost method. The repurchased shares are held in treasury and are presented as if retired. Treasury stock activity for the three years ended ember 31, 2004 is presented in the Consolidated Statements of Stockholders' Deficit.

Income Taxes

Income taxes are recorded using the asset and liability method of accounting for income taxes. Deferred income taxes reflect the net tax effect of temporary differences between the ying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. A valuation allowance is provided for deferred tax assets if it is e likely than not such assets will not be realized.

Reclassifications

Certain prior period financial statement amounts have been reclassified to conform to the 2004 presentation.

During 2004, the Company reclassified book overdrafts at December 31, 2003 and 2002. These reclassifications increased cash and current liabilities by $42.9 million and $0.6 millic ecember 31, 2003 and 2002. Additionally, the Company reclassified approximately $15.5 million and $6.0 million in restricted cash and other assets previously reported as cash at ember 31, 2003 and 2002. As a result of these reclassifications, cash flows from operating activities decreased $9.5 million and $1.9 million for the years ended December 31, 2003 ar , and cash flows from financing activities increased $42.3 million and decreased $23.4 million for the same year ends.

Supplemental Disclosures to Consolidated Statements of Cash Flows

Year ended December 31,	2004	2003	2002
		In thousands	
Cash paid for acquisitions:			
Fair value of assets acquired	$ 21,414	$ 50,509	$ —
Net liabilities assumed	(4,196)	(3,968)	—
Cash paid for acquisitions, net of cash acquired	17,218	46,541	—
Cash paid for interest, net of capitalized interest	166,584	162,904	154,288
Cash paid for income taxes	28,999	32,395	25,537

Business Combinations

During 2004, the Company completed two acquisitions in its Education division, in which the Company acquired customer lists valued at $14.6 million, covenants not to compete ed at $0.6 million and trademarks valued at $0.1 million, which are being amortized over their useful lives, of three years for the customer lists and covenants not to compete.

During 2003, the Company completed two acquisitions, one in its Education division and one in its International Networks division. In connection with these acquisitions, the pany acquired customer lists valued at $27.7 million, which are being amortized over their useful lives of three years. The Company also acquired deferred launch incentives valued a 7 million. Of these, $13.2 million are amortized over the five-year term of the agreements, and $3.5 million relate to a penalty for non-renewal in 2008. If no renewal is effectuated in 2008, the acquiree will refund the pany. If renewed, the Company will amortize this amount over the renewal period.

Purchase price in excess of the fair value of the assets and liabilities acquired of $1.1 million and $6.0 million was recorded to goodwill in 2004 and 2003.

Programming Rights

Programming Rights, December 31,		2004		2003
		In thousands		
Produced programming rights				
Completed	$	1,099,483	$	892,867
In process		100,086		77,062
Co-produced programming rights				
Completed		698,758		626,934
In process		38,575		44,464
Licensed programming rights				
Acquired		189,662		243,541
Prepaid		4,232		7,719
Programming rights, at cost		2,130,796		1,892,587
Accumulated amortization		(1,052,839)		(964,488)
Programming rights, net		1,077,957		928,099
Current portion, licensed programming rights		(50,578)		(46,364)
Non-current portion	$	1,027,379	$	881,735

Amortization of programming rights was $494.2 million, $413.9 million and $365.4 million in 2004, 2003 and 2002, and is recorded as a cost of revenue.

The Company estimates that 91.1% of unamortized costs of programming rights at December 31, 2004 will be amortized within the next three years. The Company expects to amorti .0 million of unamortized programming rights, not including in-process and prepaid productions, during the next twelve months.

Property and Equipment

Property and Equipment, December 31,		2004		2003
		In thousands		
Equipment and software	$	344,525	$	346,438
Land		28,781		27,575
Buildings		136,088		137,190
Furniture, fixtures, leasehold improvements and other assets		160,418		160,744
Assets in progress		60,806		29,582
Property and equipment, at cost		730,618		701,529
Accumulated depreciation and amortization		(350,328)		(341,118)

Property and equipment, net	$ 380,290	$ 360,411

The cost and accumulated depreciation of satellite transponders under capital leases were $23.5 million and $4.1 million at December 31, 2004, and $64.3 million and $45.4 million a ember 31, 2003. Depreciation and amortization of property and equipment, including equipment under capital lease, was $85.4 million, $86.4 million and $96.3 million in 2004, 2003 2002.

Through December 31, 2004, total capitalized costs associated with facility construction projects include land costs of $2.3 million, and building and leasehold improvement costs of 8 million. The Company expects these facilities to be completed in 2005.

The Company completed construction of its worldwide headquarters facility in Silver Spring, Maryland, in the first quarter of 2003. The final facility is comprised of land costs of 5 million, building structure and construction costs of $121.4 million, and interest costs of $14.7 million.

Sale of Long-lived Assets

In 2004, the Company recorded a net gain of $22.0 million on the sale of certain of the Company's television technology patents. The transaction closed August 19, 2004 and the gair esents the sale price less costs to sell. The Company expensed all of the costs to develop this technology in prior years.

Goodwill and Intangible Assets

Goodwill and Intangible Assets, December 31,		2004		2003
		In thousands		
Goodwill	$	257,460	$	253,308
Trademarks		13,383		13,230
Customer relationships and lists, net of amortization of $86,406 and $64,393		64,109		72,153
Non-compete and other, net of amortization of $43,021 and $33,229		33,068		42,343
Representation rights, net of amortization of $60,528 and $51,198		77,201		85,934
Goodwill and intangible assets, net	$	445,221	$	466,968

Goodwill and trademarks are not amortized. Customer relationships and lists are amortized on a straight-line basis over estimated useful lives of three to seven years. Non-compete ts are amortized on a straight-line basis over the contractual term of five to seven years. Other intangibles are amortized on a straight-line basis over estimated useful lives of ten years resentation rights are amortized on a straight-line basis over the contractual term of fifteen years.

During 2004 and 2003 the Company reduced its estimate of certain pre-acquisition contingencies associated with certain subscriber contractual arrangements acquired as part of the isition of The Health Network. These revisions resulted in a reduction of goodwill of $8.0 million and $26.7 million at December 31, 2004 and 2003.

The $4.2 million net increase in goodwill results from 1) a $8.0 million reduction related to an adjustment for pre-acquisition contingent liabilities (discussed above), 2) a $9.5 millio stment to increase goodwill for recognition of certain deferred tax liabilities, 3) a $1.1 million addition related to current year acquisitions and 4) a $1.6 million increase for foreign ency translation effect.