

IDEARC INC.  
Form 10-Q  
November 06, 2009  
**Table of Contents**







**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
WASHINGTON, DC 20549









# FORM 10-Q



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

**FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2009**

**Commission file number: 1-32939**

**IDEARC INC.**

(Exact Name of Registrant as Specified in Its Charter)

**Delaware**  
(State of Incorporation)

**20-5095175**  
(I.R.S. Employer Identification No.)

**2200 West Airfield Drive, P.O. Box 619810**  
**D/FW Airport, TX**  
(Address of Principal Executive Offices)

**75261**  
(Zip Code)

Registrant's telephone number, including area code: **(972) 453-7000**

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 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 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.

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

**As of November 2, 2009, there were 148,111,009 shares of the Registrant's common stock outstanding.**













**Table of Contents**



**TABLE OF CONTENTS**

			<b>Page No.</b>
		<u>Forward-Looking Statements</u>	1
<u>PART I - FINANCIAL INFORMATION</u>			
<u>Item</u>	<u>1.</u>	<u>Financial Statements</u>	2
<u>Item</u>	<u>2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	23
<u>Item</u>	<u>3.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	31
<u>Item</u>	<u>4.</u>	<u>Controls and Procedures</u>	32
<u>PART II - OTHER INFORMATION</u>			
<u>Item</u>	<u>1.</u>	<u>Legal Proceedings</u>	34
<u>Item</u>	<u>1A.</u>	<u>Risk Factors</u>	35
<u>Item</u>	<u>2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	41
<u>Item</u>	<u>3.</u>	<u>Defaults Upon Senior Securities</u>	41
<u>Item</u>	<u>4.</u>	<u>Submission of Matters to a Vote of Security Holders</u>	41
<u>Item</u>	<u>5.</u>	<u>Other Information</u>	41
<u>Item</u>	<u>6.</u>	<u>Exhibits</u>	42





**Table of Contents**





**FORWARD-LOOKING STATEMENTS**



## Edgar Filing: IDEARC INC. - Form 10-Q

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. You should not place undue reliance on these statements. These forward-looking statements include statements that reflect the current views of our senior management with respect to our financial performance and future events with respect to our business and industry in general. Statements that include the words may, could, should, would, believe, anticipate, forecast, estimate, expect, preliminary, intend, plan, project, outlook and similar statements of a future or forward-looking nature identify forward-looking statements. Forward-looking statements address matters that involve risks and uncertainties. Accordingly, there are or will be important factors that could cause our actual results to differ materially from those indicated in these statements. We believe that these factors include, but are not limited to, the following:

- risks related to the impact of our ongoing Chapter 11 bankruptcy could have on our corporate image, normal business operations, financial condition, liquidity or cash flow;
- risks related to our ability to successfully execute, confirm and consummate a plan of reorganization with respect to the Chapter 11 bankruptcy in a timely manner that will provide assurance for the long-term continued viability of our business;
- limitations on our operating and strategic flexibility during the pendency of the bankruptcy proceedings or under the terms of new debt agreements that may result from the reorganization;
- access to capital markets and increased borrowing costs resulting from our risks related to our Chapter 11 bankruptcy;
- risks associated with third-parties seeking and obtaining court approval to terminate or shorten the exclusivity period for us to propose and confirm a plan of reorganization, to appoint a Chapter 11 trustee or to convert the case to a Chapter 7 bankruptcy;
- risks related to our declining revenue, including a reduction in customer advertising spend and contract cancellations resulting from the current economic downturn;
- changes in our competitive position due to competition from other yellow pages directories publishers and other traditional and new media and our ability to anticipate or respond to changes in technology and user preferences;
- declining use of print yellow pages directories;
- changes in the availability and cost of paper and other raw materials used to print our directories and our reliance on third-party providers for printing and distribution services;

## Edgar Filing: IDEARC INC. - Form 10-Q

- increased credit risk associated with our reliance on small- and medium-sized businesses as clients, in particular in the current economic downturn;
- changes in our operating performance;
- our ability to attract and retain qualified executives;
- our ability to maintain good relations with our unionized employees;
- changes in U.S. labor, business, political and/or economic conditions;
- changes in governmental regulations and policies and actions of regulatory bodies;
- the outcome of pending or future litigation and other claims; and
- risks associated with our obligations under agreements entered into with Verizon in connection with our spin-off.

The foregoing factors should not be construed as exhaustive and should be read together with the other cautionary statements included in this and other reports we file with the Securities and Exchange Commission, including the information in Item 1A. Risk Factors in Part I of our Annual Report on Form 10-K for the year ended December 31, 2008 and as updated in this Quarterly Report on Form 10-Q for the period ending September 30, 2009. If one or more events related to these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may differ materially from what we anticipate.

---

Table of Contents

**PART I - FINANCIAL INFORMATION**



**Item 1. Financial Statements.**





## Idearc Inc. and Subsidiaries

## Debtor and Debtor-In-Possession

## Consolidated Statements of Operations

(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2009	2008	2009	2008
	(in millions, except per share amounts)			
<b>Operating Revenue</b>				
Print products	\$ 543	\$ 659	\$ 1,723	\$ 2,038
Internet	68	75	211	223
Other		1	2	3
<b>Total Operating Revenue</b>	<b>611</b>	<b>735</b>	<b>1,936</b>	<b>2,264</b>
<b>Operating Expense</b>				
Selling	167	176	528	541
Cost of sales (exclusive of depreciation and amortization)	137	151	436	461
General and administrative	104	110	334	306
Depreciation and amortization	17	19	51	59
<b>Total Operating Expense</b>	<b>425</b>	<b>456</b>	<b>1,349</b>	<b>1,367</b>
<b>Operating Income</b>	<b>186</b>	<b>279</b>	<b>587</b>	<b>897</b>
Interest expense (income), net	(3)	162	148	491
<b>Income Before Reorganization Items and Provision</b>				
<b>(Benefit) for Income Taxes</b>	<b>189</b>	<b>117</b>	<b>439</b>	<b>406</b>
Reorganization items	35		440	
<b>Income (Loss) Before Provision (Benefit) for Income Taxes</b>	<b>154</b>	<b>117</b>	<b>(1)</b>	<b>406</b>
Provision (benefit) for income taxes	53	44	(1)	146
<b>Net Income</b>	<b>\$ 101</b>	<b>\$ 73</b>	<b>\$</b>	<b>\$ 260</b>
<b>Basic and diluted earnings per common share</b>	<b>\$ 0.69</b>	<b>\$ 0.50</b>	<b>\$</b>	<b>\$ 1.78</b>
<b>Basic and diluted weighted-average common shares outstanding</b>	<b>147</b>	<b>146</b>	<b>147</b>	<b>146</b>
<b>Dividends declared per common share</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$ 0.3425</b>

See Notes to Consolidated Financial Statements.

Table of Contents**Idearc Inc. and Subsidiaries****Debtor and Debtor-In-Possession****Consolidated Balance Sheets****(Unaudited)**

	At September 30, 2009	At December 31, 2008
	(in millions)	
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 722	\$ 510
Accounts receivable, net of allowances of \$138 and \$108	283	366
Accrued taxes receivable	39	
Deferred directory costs	248	282
Debt issuance costs		75
Deferred tax asset	155	49
Prepaid expenses and other	12	18
Total current assets	1,459	1,300
Property, plant and equipment	462	475
Less: accumulated depreciation	370	373
	92	102
Goodwill	76	73
Intangible assets, net	57	66
Pension assets	87	147
Non-current deferred tax assets	146	126
Other non-current assets	10	1
Total assets	\$ 1,927	\$ 1,815
<b>Liabilities and Stockholders Equity (Deficit)</b>		
Current liabilities:		
Current maturities of long-term debt	\$	\$ 9,267
Derivative liabilities		248
Accounts payable and accrued liabilities	156	242
Deferred revenue	111	155
Other	20	21
Total current liabilities	287	9,933
Employee benefit obligations	266	287
Unrecognized tax benefits		85
Other liabilities	3	1
Total liabilities not subject to compromise	556	10,306
Liabilities subject to compromise	9,769	
Stockholders' equity (deficit):		
Common stock (\$.01 par value; 225 million shares authorized, 148,111,009 and 148,262,447 shares issued and outstanding in 2009 and 2008, respectively)	1	1
Additional paid-in capital (deficit)	(8,757)	(8,764)
Retained earnings	494	494
Accumulated other comprehensive loss	(136)	(222)
Total stockholders' equity (deficit)	(8,398)	(8,491)

Edgar Filing: IDEARC INC. - Form 10-Q

Total liabilities and stockholders' equity (deficit)	\$	<b>1,927</b>	\$	1,815
--	----	--------------	----	-------

See Notes to Consolidated Financial Statements.

Table of Contents**Idearc Inc. and Subsidiaries****Debtor and Debtor-In-Possession****Consolidated Statements of Cash Flows****(Unaudited)**

	Nine Months Ended September 30,	
	2009	2008
	(in millions)	
<b>Cash Flows from Operating Activities</b>		
Net income	\$	\$ 260
Adjustments to reconcile net income to net cash provided by operating activities:		
Non-cash reorganization items	424	
Depreciation and amortization	51	59
Employee retirement benefits	18	1
Deferred income taxes	(170)	17
Provision for uncollectible accounts	178	147
Stock-based compensation	6	3
Changes in current assets and liabilities		
Accounts receivable	(94)	(101)
Deferred directory costs	34	29
Other current assets	7	6
Accounts payable and accrued liabilities	6	(21)
Other, net	(24)	(23)
Net cash provided by operating activities	436	377
<b>Cash Flows from Investing Activities</b>		
Capital expenditures (including capitalized software)	(33)	(37)
Acquisitions	(3)	
Proceeds from sale of assets		2
Net cash used in investing activities	(36)	(35)
<b>Cash Flows from Financing Activities</b>		
Repayment of long-term debt	(188)	(36)
Dividends paid to Idearc stockholders		(50)
Net cash used in financing activities	(188)	(86)
Increase in cash and cash equivalents	212	256
Cash and cash equivalents, beginning of year	510	48
Cash and cash equivalents, end of period	\$ 722	\$ 304

See Notes to Consolidated Financial Statements.

Table of Contents

**Idearc Inc. and Subsidiaries**

**Notes to Consolidated Financial Statements**

**(Unaudited)**

**Note 1**

**Chapter 11 Bankruptcy Filings**

Idearc Inc. and its subsidiaries (collectively, "Idearc", "We", "Our" or the "Company") is one of the nation's largest providers of yellow and white pages directories and related advertising products. On March 31, 2009 (the "Petition Date"), the Company and its domestic subsidiaries filed voluntary petitions for reorganization under Chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division (the "Bankruptcy Court"). The cases are being jointly administered under Case No. 09-31828.

Subject to certain exceptions under the Bankruptcy Code, the Company's Chapter 11 bankruptcy filings automatically enjoined, or stayed, the continuation of any judicial or administrative proceedings or other actions against the Company or its property to recover on, collect or secure a claim arising prior to the Petition Date. Thus, for example, most creditor actions to obtain possession of property from the Company, or to create, perfect or enforce any lien against the property of the Company, or to collect on monies owed or otherwise exercise rights or remedies with respect to a pre-petition claim are enjoined unless and until the Bankruptcy Court lifts the automatic stay.

The filing of the Chapter 11 bankruptcy petitions constituted an event of default under the Company's senior secured credit facility and the indenture governing the 8% senior unsecured notes due in 2016, and the debt obligations under those instruments became automatically and immediately due and payable, although any actions to enforce such payment obligations are automatically stayed under the applicable bankruptcy law. In anticipation of this action, the total outstanding debt obligations of \$9,267 million were classified as current maturities of long-term debt in the accompanying consolidated balance sheet at December 31, 2008. Based on the bankruptcy petition, the total outstanding debt obligations as of September 30, 2009 are included in liabilities subject to compromise in the accompanying consolidated balance sheet.

Likewise, the filing of Chapter 11 bankruptcy constituted an event of default under the Company's interest rate swap agreements. As a result, these interest rate swap agreements are no longer deemed financial instruments required to be remeasured at fair value each reporting period, but are now liabilities which are recorded based on management's estimate of the amount to settle the obligations. The Company recorded these net liabilities as of the bankruptcy Petition Date in the amount of \$496 million. These net liabilities are classified under liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009. See Note 6 for additional information related to liabilities subject to compromise.

**Reorganization Process**

## Edgar Filing: IDEARC INC. - Form 10-Q

The Company is currently operating as a debtor-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Bankruptcy Court. In general, a debtor-in-possession is authorized under Chapter 11 to continue to operate as an ongoing business, but may not engage in transactions outside the ordinary course of business without the prior approval of the Bankruptcy Court. The Company continues to generate positive cash flow necessary for daily operations and as such, it is not expected that debtor-in-possession financing will be needed.

Immediately after filing the Chapter 11 bankruptcy petitions, the Company began notifying all known current or potential creditors of the bankruptcy filing. Vendors are, however, being paid for goods furnished and services provided after the Petition Date in the ordinary course of business.

Table of Contents

Several bankruptcy hearings have been held since the Company filed for Chapter 11 bankruptcy. The Bankruptcy Court granted interim approval of several of the Company's first day motions, including the payment of certain pre-petition and post-petition obligations of the Company related to employee wages, salaries and benefits and certain customer obligations, as well as the continuation of certain customer programs. Also, the Bankruptcy Court authorized the banks to pay outstanding obligations (checks, EFTs, etc.) without interruption in the usual and normal course of business. Additionally, the Company paid an adequacy protection payment of \$250 million (\$188 million of secured debt principal and \$62 million of accrued interest) to the agent of its secured lenders under its senior secured credit facilities (the Lenders) for pro rata distribution to the Lenders and holders of the swap agreements that reduced pre-petition obligations. The Company retained legal and financial professionals to advise and assist the Company with the bankruptcy proceedings. From time to time, the Company has sought and may continue to seek Bankruptcy Court approval for the retention of additional professionals.

As required by the Bankruptcy Code, the United States Trustee for the Northern District of Texas appointed an official committee of unsecured creditors (the Creditors Committee). The Creditors Committee and its legal representatives have a right to be heard on all matters that come before the Bankruptcy Court with respect to the Company. There can be no assurance that the Creditors Committee will support the Company's positions on matters to be presented to the Bankruptcy Court in the future or on any proposed plan of reorganization. Disagreements between the Company and the Creditors Committee could protract the Chapter 11 proceedings, delaying the Company's emergence from the Chapter 11 bankruptcy proceedings, and thus negatively impact the Company's ongoing operations.

Under Section 365 and other relevant sections of the Bankruptcy Code, the Company may assume, assume and assign, or reject certain executory contracts and unexpired leases, including, without limitation, leases of real property and equipment, subject to the approval of the Bankruptcy Court and certain other conditions. Any description of an executory contract or unexpired lease in this report, including, where applicable, the Company's express termination rights or a quantification of obligations, must be read in conjunction with, and is qualified by, any overriding rejection rights under Section 365 of the Bankruptcy Code.

**Plan of Reorganization**

On May 15, 2009, the Company submitted a joint plan of reorganization (the Plan) and disclosure statement for consideration by the Bankruptcy Court and the affected creditors. The Plan and disclosure statement described the anticipated organization, operations and financing of the reorganized entity. Among other things, the Plan resolved the Company's pre-petition obligations, set forth the revised capital structure of the newly reorganized entity and provided for the corporate governance subsequent to emergence from bankruptcy. Specifically, the disclosure statement contained certain information about the Company's pre-petition operating and financial history, the events which led up to the commencement of bankruptcy and significant events that have occurred while operating under Chapter 11 of the Bankruptcy Code. The disclosure statement also described the terms and provisions of the Plan, including certain effects of confirmation of the Plan, certain risk factors associated with securities to be issued under the Plan, certain alternatives to the Plan, the manner in which distribution would be made under the Plan, and the confirmation process and the voting procedures that holders of claims and interests entitled to vote under the Plan must follow for their votes to be counted.

On September 8, 2009, the Company filed the first amended joint plan of reorganization (the Amended Plan) and disclosure statement with revised financial forecasts and the capital structure anticipated at emergence from bankruptcy. The Bankruptcy Court approved the Company's disclosure statement, as it related to the Amended Plan, on September 10, 2009. With the approval of the disclosure statement, the Company has begun soliciting votes from its creditors to accept or reject the Amended Plan. The Bankruptcy Court has set the voting deadline for 6:00 p.m. (CST) on November 13, 2009. The hearing at which the Bankruptcy Court will consider confirmation of the Amended Plan is scheduled to commence on December 9, 2009. However, there can be no assurance at this time that the Amended Plan will be confirmed by the Bankruptcy Court or that any such plan will be implemented successfully and on a timely basis.





Table of Contents

Under the Amended Plan, if ultimately confirmed by the Bankruptcy Court, allowed secured credit facilities claims will become parties to and be bound by a new term loan agreement in exchange for the cancellation of outstanding debt obligations. The new term loans will be in an aggregate principal amount equal to \$2.75 billion and will mature on the sixth anniversary of the bankruptcy emergence date. The new term loans will bear interest at an annual rate of LIBOR plus 800 basis points with a LIBOR floor of 3.0%. In addition, new issue common stock will be distributed to the holders of allowed secured credit facility claims, which will represent 95% of the new common stock to be issued and outstanding on the bankruptcy emergence date. New issue common stock will also be distributed to holders of allowed unsecured note claims, allowed unsecured credit facilities claims and allowed general unsecured claims, which will represent 5% of the new common stock to be issued and outstanding on the bankruptcy emergence date. Finally, under the priority order of claims established in the Amended Plan, any claim for damages arising from the purchase or sale of any old securities, or any claim for reimbursement, contribution, or indemnification on account of any such claim will be impaired and will receive no distributions.

The ultimate recovery to the holders of claims will not be finalized until confirmation of the Amended Plan. No assurance can be given as to what values, if any, will be ascribed in the Chapter 11 proceedings to each constituency or what types or amounts of distributions, if any, they would ultimately receive. The confirmed Amended Plan could result in holders of the Company's liabilities and/or securities, including common stock, receiving no distribution and cancellation of their holdings. Due to these uncertainties, the value of the Company's liabilities and securities, including its common stock, is highly speculative. Appropriate caution should be exercised with respect to existing and future investments in any of the liabilities and securities of the Company. At this time, there is no assurance the Company will be able to restructure as a going concern or successfully implement the Amended Plan.

For periods subsequent to the Chapter 11 bankruptcy filings, the guidance under the applicable reorganization accounting rules has been applied in preparing the accompanying consolidated financial statements. This guidance requires that the financial statements distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Accordingly, certain expenses (including professional fees), realized gains and losses and provisions for losses that are realized from the reorganization process will be classified as reorganization items in the accompanying consolidated statement of operations. See Note 2 for additional information related to reorganization items. Additionally, in the accompanying consolidated balance sheet, liabilities are segregated between liabilities not subject to compromise and liabilities subject to compromise. Liabilities subject to compromise are reported at their pre-petition amounts or current unimpaired values, even if they may be settled for lesser amounts. See Note 6 for additional information related to liabilities subject to compromise.

**Going Concern Matters**

The accompanying consolidated financial statements and related notes have been prepared assuming that the Company will continue as a going concern, although the Chapter 11 bankruptcy raises substantial doubt about the Company's ability to continue as a going concern. The accompanying consolidated financial statements do not include any adjustments related to the recoverability and classification of recorded assets or to the amounts classified as liabilities or any other adjustments that might be necessary should the Company be unable to continue as a going concern.

The Company continues to be operationally profitable and provide positive operating cash flows. As such, debtor-in-possession financing is not expected to be required. However, the Company has incurred and will continue to incur significant costs associated with its reorganization process. These costs are being expensed as incurred. In addition, during 2008, the Company began implementing strategic organizational and market exit initiatives to improve ongoing operational efficiencies. These reorganization efforts have continued throughout 2009. See Note 3 for additional information related to restructuring.

**Basis of Presentation**

The Company prepares its financial statements in accordance with accounting principles generally accepted in the United States. Pursuant to the rules and regulations of the United States Securities and

Table of Contents

Exchange Commission (the SEC), the accompanying unaudited consolidated financial statements contain all adjustments, consisting of normal recurring items and accruals, necessary to fairly present the financial position, results of operations and cash flows of Idearc Inc. and its subsidiaries. These interim condensed financial statements do not contain all information and footnote disclosures normally included in financial statements and should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2008. The results for the interim periods are not necessarily indicative of results for the full year. The preparation of these consolidated financial statements requires management to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of the financial statements. Certain prior period amounts have been reclassified to conform to current year presentation.

The accompanying unaudited consolidated financial statements do not purport to reflect or provide for the consequences of the Chapter 11 bankruptcy proceedings. In particular, the financial statements do not purport to show (i) as to assets, their realizable value on a liquidation basis or their availability to satisfy liabilities; (ii) as to pre-petition liabilities, the amounts that may be allowed for claims or contingencies, or the status and priority thereof; (iii) as to shareholders' equity (deficit) accounts, the effects of any changes that may be made in the Company's capitalization; or (iv) as to operations, the effects of any changes that may be made to the Company's business.

**Recent Accounting Pronouncements**

*Enhanced Disclosures for Postretirement Benefit Plan Assets*

In December 2008, the Financial Accounting Standards Board (FASB) amended the disclosure requirement of assets held in an employer's defined benefit pension or other postretirement plan. Effective for periods after December 15, 2009, the Company will disclose for each major category of plan assets, its valuation within the fair value hierarchy.

*Interim Disclosures about Fair Value of Financial Instruments*

In April 2009, the FASB amended the disclosure requirements for the fair value of financial instruments. The guidance requires publicly traded companies to disclose the fair value of financial instruments in interim reporting periods and in the annual financial statements. The guidance enhances consistency in financial reporting by increasing the frequency of fair value disclosures to a quarterly basis for any financial instruments. The Company adopted the new disclosure requirements effective for the quarter ended June 30, 2009. See Note 5 for additional information on fair value disclosures.

*Subsequent Events*

In June 2009, the FASB issued accounting guidance that requires companies to recognize in the financial statements the effects of subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. An entity shall disclose the date through which subsequent events have been evaluated, as well as whether that date is the date the financial statements were issued. Companies are not permitted to recognize subsequent events that provide

## Edgar Filing: IDEARC INC. - Form 10-Q

evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before financial statements are issued. Some non-recognized subsequent events must be disclosed to keep the financial statements from being misleading. For such events a company must disclose the nature of the event, an estimate of its financial effect, or a statement that such an estimate cannot be made. The accounting guidance applies prospectively for interim or annual financial periods ending after June 15, 2009. The Company adopted the new accounting rules associated with subsequent events effective for the quarter ended June 30, 2009 consolidated financial statements and disclosures.

The Company evaluates events and transactions that occur after the balance sheet date as potential subsequent events. This evaluation was performed through November 6, 2009, the date on which the Company's accompanying consolidated financial statements were issued.

Table of Contents**Note 2****Reorganization Items**

During the three and nine months ended September 30, 2009, the Company recorded \$35 million and \$440 million, respectively, of reorganization items on a separate line item in the consolidated statements of operations, in accordance with provisions established by the applicable reorganization accounting rules. Reorganization items represent charges that are directly associated with the process of reorganizing the business under Chapter 11 of the Bankruptcy Code, and include certain expenses, realized gains and losses, and provisions for losses resulting from the reorganization of the business.

The following table displays the details of reorganization items for the three and nine months ended September 30, 2009:

	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2009
	(in millions)	
Fair value adjustment associated with interest rate swap derivatives	\$ 279	\$ 279
Write-off of deferred losses associated with interest rate swap derivatives	21	145
Other	14	16
Total reorganization items	\$ 35	\$ 440

The filing of Chapter 11 bankruptcy constituted an event of default under our interest rate swap agreements. As a result, these interest rate swap agreements are no longer deemed financial instruments required to be remeasured at fair value each reporting period, but are now liabilities which are recorded based on management's estimate of the amount to settle the obligations. This resulted in a non-cash charge of \$279 million that was recognized as a reorganization item in the accompanying consolidated statement of operations.

Deferred losses in accumulated other comprehensive loss associated with the interest rate swaps were remeasured to reflect the component of forecasted interest rate payments that are likely to occur. This resulted in non-cash charges of \$21 million and \$145 million that were recognized as reorganization items in the accompanying consolidated statement of operations for the three and nine months ended September 30, 2009, respectively.

Other reorganization expenses of \$14 million and \$16 million for the three and nine months ended September 30, 2009, respectively, primarily consist of professional fees incurred directly associated with the reorganization of the business under Chapter 11 of the Bankruptcy Code.

Cash paid for reorganization items for the nine months ended September 30, 2009 totaled \$13 million, primarily representing payment of professional fees directly associated with the reorganization of the business under Chapter 11 of the Bankruptcy Code.

**Note 3**

**Restructuring**

During the three and nine months ended September 30, 2009, the Company recorded \$6 million and \$19 million, respectively, of restructuring charges associated with its ongoing strategic organizational, market exit and pre-petition capital restructuring initiatives, which began during 2008. The \$19 million includes \$10 million of professional fees associated with pre-petition capital restructuring costs.

Table of Contents

The following table sets forth the restructuring costs that are included in general and administrative expense in the accompanying consolidated statements of operations for the three and nine months ended September 30, 2009, and 2008:

	Three Months Ended			Nine Months Ended		
	September 30,			September 30,		
	2009	2008	(in millions)	2009	2008	
Severance pay and benefits	\$ 5	\$	\$	6	\$	7
Facilities charges	1		3	2		3
Capital restructuring - pre-petition				10		
Other			1	1		1
Total restructuring expense	\$ 6	\$	\$ 4	\$ 19	\$	11

The following table sets forth the balance of the restructuring accrual at September 30, 2009, and details the changes in the accrued liability through the first nine months of 2009:

	Beginning	Restructuring	Payments	Ending
	Balance at			Expense
	January 1, 2009	(in millions)		September 30, 2009
Severance pay and benefits	\$ 3	\$ 6	\$ (4)	\$ 5
Facilities charges		2	(2)	
Capital restructuring - pre-petition		10	(10)	
Other		1	(1)	
Total	\$ 3	\$ 19	\$ (17)	\$ 5

The Company anticipates there will be additional restructuring charges in subsequent periods.

**Note 4**

**Earnings Per Share**

Basic earnings per share are computed by dividing net income by the number of weighted-average common shares outstanding during the reporting period. Diluted earnings per share are calculated to give effect to all potentially dilutive common shares that were outstanding during the reporting period. The effect of potentially dilutive common shares for the three and nine months ended September 30, 2009 and the three and nine months ended September 30, 2008 was not material.

The following table illustrates the calculation of basic and diluted earnings per share for the three and nine months ended September 30, 2009 and the three and nine months ended September 30, 2008:



Edgar Filing: IDEARC INC. - Form 10-Q

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2009	2008	2009	2008
	(in millions, except per share amounts)			
Income available to common stockholders	\$ 101	\$ 73	\$ 260	\$ 260
Weighted-average common shares outstanding	147	146	147	146
Basic and diluted earnings per share	\$ 0.69	\$ 0.50	\$ 1.78	\$ 1.78

Table of Contents

**Note 5**

**Additional Financial Information**

The tables that follow provide additional financial information related to the Company's consolidated financial statements.

***Balance Sheet***

As a result of the Company filing for Chapter 11 bankruptcy, there has been a reclassification of certain liabilities from accounts payable and accrued liabilities to liabilities subject to compromise. See Note 6 for additional information related to liabilities subject to compromise.

The following table displays the components of accounts payable and accrued liabilities:

	At September 30, 2009	At December 31, 2008
	(in millions)	
Accounts payable and accrued liabilities		
Accounts payable	\$ 25	\$ 34
Accrued expenses	23	48
Accrued vacation pay	18	19
Accrued salaries and wages	85	66
Accrued taxes	5	45
Accrued interest		30
Total accounts payable and accrued liabilities	\$ 156	\$ 242

The following table displays items previously classified as accounts payable and accrued liabilities at December 31, 2008 that are now categorized as liabilities subject to compromise:

	At September 30, 2009
	(in millions)
Accounts payable and accrued liabilities classified as liabilities subject to compromise	
Accounts payable	\$ 13
Accrued expenses	3
Accrued taxes	41
Accrued interest	118
Accounts payable and accrued liabilities classified as liabilities subject to compromise	\$ 175

***Comprehensive Income***

Edgar Filing: IDEARC INC. - Form 10-Q

The following table displays the computation of total comprehensive income (loss):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2009	2008	2009	2008
	(in millions)			
Net income	\$ 101	\$ 73	\$ 260	\$ 260
Other comprehensive income (loss), net of taxes				
Unrealized gain on cash flow hedges		10		34
Reclassification adjustment associated with cash flow hedge losses realized in net income	13		113	
Adjustments for pension and post-employment benefits	(16)	(3)	(27)	(3)
Other comprehensive income (loss), net of taxes	(3)	7	86	31
Total comprehensive income	\$ 98	\$ 80	\$ 86	\$ 291

Table of Contents

As of December 31, 2008, the Company discontinued hedge accounting associated with its interest rate swap agreements and as a result, all 2009 activities related to the interest rate swap agreements were recorded to the consolidated statement of operations. See Note 7 for further discussion of debt obligations and interest rate swap agreements.

As of September 30, 2009, the balance in accumulated other comprehensive loss of \$136 million includes an unrealized loss of \$53 million (net of tax of \$30 million) related to the unrealized losses on cash flow hedges and ineffectiveness and an unrealized loss of \$83 million (net of tax of \$51 million) associated with adjustments for pension and post-employment benefits.

As of December 31, 2008, the balance in accumulated other comprehensive loss of \$222 million includes an unrealized loss of \$166 million (net of tax of \$87 million) related to the unrealized losses on cash flow hedges and ineffectiveness and an unrealized loss of \$56 million (net of tax of \$36 million) associated with adjustments for pension and post-employment benefits.

***Fair Values of Financial Instruments***

The fair values of cash and cash equivalents, trade receivables, short-term investments and accounts payable approximate their carrying amounts due to their short-term nature. The fair values of debt instruments are determined based on debt with similar maturities and credit quality discounted at current quoted market rates. The filing of Chapter 11 bankruptcy constituted an event of default under the Company's interest rate swap agreements. As a result, these interest rate swap agreements are no longer deemed financial instruments required to be remeasured at fair value each reporting period, but are now liabilities which are recorded based on management's estimate of the amount to settle the obligations. The Company recorded these net liabilities as of the bankruptcy Petition Date in the amount of \$496 million. These net liabilities are classified under liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009.

The following table sets forth the carrying amount and fair value for total debt obligations and derivative liabilities at September 30, 2009 and December 31, 2008:

	At September 30, 2009		At December 31, 2008	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
		(in millions)		
Total debt obligations	\$ 9,079	\$ 2,780	\$ 9,267	\$ 2,391
Derivative liabilities	496	496	248	248

**Note 6****Liabilities Subject To Compromise**

Liabilities subject to compromise refers to both secured and unsecured obligations that will be settled under the plan of reorganization. The applicable reorganization accounting rules require pre-petition liabilities, including those that became known after filing the bankruptcy petitions

## Edgar Filing: IDEARC INC. - Form 10-Q

that are subject to compromise to be reported at the amounts expected to be allowed, even if they may be settled for lesser amounts. These liabilities represent the estimated amount expected to be resolved on known or potential claims through the Chapter 11 process, and remain subject to future adjustments from negotiated settlements, actions of the Bankruptcy Court and non-acceptance of certain executory contracts and unexpired leases. Liabilities subject to compromise also include items that may be assumed under the plan of reorganization, and may be subsequently reclassified to liabilities not subject to compromise. The Company has classified all of its debt obligations of \$9,079 million, including its secured debt, as liabilities subject to compromise. Liabilities subject to compromise also include certain pre-petition liabilities, including certain accrued taxes, accrued interest and accrued expenses. The Company's cash from operations was favorably impacted by the stay of payment of interest.

Table of Contents

The table below identifies the principal categories of liabilities subject to compromise:

	<b>At September 30, 2009</b>
	<b>(in millions)</b>
Debt obligations	\$ 9,079
Derivative liabilities, net	496
Debt issuance costs	(73)
Accounts payable and accrued liabilities	175
Other current liabilities	2
Unrecognized tax benefits	90
Total liabilities subject to compromise	\$ 9,769

**Note 7****Debt Obligations and Derivative Instruments****Chapter 11 Bankruptcy Filings**

On March 31, 2009, the Company and its domestic subsidiaries filed voluntary petitions in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division seeking reorganization relief under the provisions of Chapter 11 of Title 11 of the United States Code. The filing of the Chapter 11 petitions constituted an event of default under certain of the Company's debt obligations and interest rate swap agreements, and those debt obligations and interest rate swap agreements became automatically and immediately due and payable. However, under applicable bankruptcy law, an automatic stay of action to collect, assert, or recover a claim against the Company is now in effect. The Company's debt obligations of \$9,079 million are classified as liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009. The debt obligations balance reflects the payment of a court approved adequacy protection payment of \$250 million (\$188 million of secured debt principal and \$62 million of accrued interest) made in April 2009 to the agent of the Company's secured lenders under its senior secured credit facilities.

Other than the adequacy protection payment of principal and interest discussed above, the Company did not make any scheduled principal payments in 2009 or any interest payments since February 2009. As stipulated in the debt credit agreement, the interest rate was automatically changed to the Prime Rate (called the Alternative Base Rate or ABR) plus a basis point spread on the revolving credit facility, Tranche A Facility, and Tranche B Facility which equates to an all-in interest rate of 5.75%, 5.75% and 6.25%, respectively. However, since the filing of the bankruptcy petitions, interest associated with the debt and interest rate swap agreements is not being accrued.

In accordance with guidance under the applicable reorganization accounting rules, the debt issuance costs should be viewed as valuations of the related debt obligations. When the debt obligations become allowed claims and the allowed claims differ from the net carrying amount of the debt obligations, the recorded amount should be adjusted to the amount of the allowed claims (thereby adjusting existing debt issuance costs to the extent necessary to report debt obligations at this allowed amount). Through September 30, 2009, the Bankruptcy Court had not classified any of the debt obligations as allowed claims. Therefore, the debt obligations have been categorized under liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009. The debt issuance costs of \$73 million as of September 30, 2009 have not been adjusted. The Company may be required to record these amounts or a portion thereof in the consolidated statement of operations as a reorganization item if the Bankruptcy Court ultimately determines that a portion of the debt obligation is subject to compromise. See Note 6 for

## Edgar Filing: IDEARC INC. - Form 10-Q

additional information related to liabilities subject to compromise.

Due to the bankruptcy filing, the Company's interest rate swap agreements are no longer deemed financial instruments required to be remeasured at fair value each reporting period, but are now liabilities which are recorded based on management's estimate of the amount to settle the obligations. The Company recorded these net liabilities as of the bankruptcy Petition Date in the amount of \$496 million. These liabilities are classified under liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009. Accordingly, the Company recorded a loss of \$279 million which represented the difference in the carrying amount of the liability

Table of Contents

prior to the bankruptcy Petition Date and the expected amount of the allowed claim. The loss was recognized during the three months ended March 31, 2009 in the consolidated statement of operations as a reorganization item. See Note 2 for a further explanation of reorganization items.

On September 10, 2009, the Bankruptcy Court approved the Company's disclosure statement, as it relates to the Amended Plan. Under the Amended Plan, if ultimately confirmed by the Bankruptcy Court, allowed secured credit facilities claims will become parties to and be bound by a new term loan agreement in exchange for the cancellation of outstanding debt obligations. The new term loans will be in aggregate principal amount equal to \$2.75 billion and will mature on the sixth anniversary of the bankruptcy emergence date. As such, a portion of the forecasted interest payments on the original, higher principal debt are not probable of occurring, therefore, the deferred losses in accumulated other comprehensive loss associated with the interest rate swaps were remeasured from \$228 million to \$83 million as of September 30, 2009. The \$145 million remeasurement difference was recognized as a reorganization item in the accompanying consolidated statement of operations during 2009. The remaining deferred balance of \$83 million (\$53 million net of tax) in accumulated other comprehensive loss will be amortized to the statement of operations using the effective interest method over the remaining period of the forecasted interest payments, once interest payments on the debt obligations resume, or upon emergence from bankruptcy, it will be evaluated in accordance with the applicable reorganization accounting rules. Any additional reduction in the proposed debt level would result in deferred losses recorded in accumulated other comprehensive loss being remeasured and recognized as reorganization expense in the consolidated statement of operations. See Note 2 for a further explanation of reorganization items.

**Debt Obligations**

Outstanding debt obligations are as follows:

	Interest Rates	Maturities	At September 30, 2009	At December 31, 2008
(in millions)				
<b>Senior secured credit facilities:</b>				
Revolving credit facility	ABR+ 0.50%	2011	\$ 240	\$ 247
Tranche A facility	ABR+ 0.50%	2009-2013	1,470	1,515
Tranche B facility	ABR+ 1.00%	2007-2014	4,519	4,655
<b>Total senior secured credit facilities</b>			<b>6,229</b>	<b>6,417</b>
Senior unsecured notes	8.0%	2016	2,850	2,850
<b>Debt obligations</b>			<b>9,079</b>	<b>9,267</b>
Less: current maturities of long-term debt				(9,267)
<b>Debt obligations subject to compromise</b>			<b>\$ 9,079</b>	<b>\$</b>

**Senior Secured Credit Facilities**

On November 17, 2006, the Company entered into senior secured credit facilities totaling \$6,265 million, which consisted of: (a) Tranche A term loan facility of approximately \$1,515 million (the Tranche A Facility), (b) Tranche B term loan facility of \$4,750 million (the Tranche B Facility), and (c) a \$250 million revolving credit facility. The revolving credit facility originally matured on November 17, 2011. The senior secured credit facilities are guaranteed by substantially all of Idearc's subsidiaries and are secured by substantially all present and future assets of Idearc Inc. and its subsidiaries.



## Edgar Filing: IDEARC INC. - Form 10-Q

On October 24, 2008, the Company initiated borrowings of \$247 million under its existing \$250 million revolving credit facility, leaving available funds at December 31, 2008 of approximately \$0.3 million (\$250 million revolving credit facility less \$247 million in initiated borrowings less \$2.7 million in letters of credit outstanding). The borrowing under the revolving credit facility allowed the Company to increase its cash position in order to preserve financial flexibility in light of the uncertainty in the credit markets. In accordance with the terms of the senior secured credit facility, the proceeds from the borrowing are intended for general corporate purposes. The

Table of Contents

agreement calls for the Company to pay a commitment fee of 0.375% for the unused portion of the revolving credit facility, calculated based on the daily unused amount and payable on a quarterly basis.

Payments of principal under the Tranche A Facility were originally due quarterly beginning in 2009, and a final payment due at maturity on November 15, 2013. Principal payments under the Tranche A Facility originally amortized as a percentage of the total term loan in an amount per quarter equal to the following: 2009 1.25%; 2010 2.50%; 2011 3.75%; 2012 5.00%; 2013 (first three quarters) 12.50%; Maturity 12.50%. The Tranche B Facility was originally payable in equal quarterly installments beginning in 2007 in an amount equal to 0.25% per quarter, with the balance due on the maturity date of November 17, 2014.

*Derivative Instruments and Hedging Activities*

The Company has interest rate swap agreements with major financial institutions with notional amounts totaling \$5,500 million. These interest rate swap agreements consist of four separate swap transactions with \$2,700 million originally maturing on June 29, 2012, \$1,100 million originally maturing on September 30, 2010, \$800 million originally maturing on March 31, 2012 and \$900 million with annual notional reductions of \$200 million originally maturing on March 31, 2012. Under the interest rate swap agreements, the Company paid fixed rate interest at rates ranging from 4.86% to 5.15% and received floating rate interest based on the three month LIBOR to hedge the variability in cash flows attributable to changes in the benchmark interest rate. These swap agreements comply with debt covenants under the senior secured credit facilities that required at least 50% of total outstanding debt be subject to fixed interest rates through June 2009. The Company does not enter into derivative financial instruments for trading or speculative purposes.

In addition, on August 18, 2008, the Company entered into an interest rate swap arrangement which resulted in the de-designation of the \$1,100 million swap maturing on September 30, 2010. In this arrangement, the remaining life of the \$1,100 million swap was combined with a basis swap and re-designated as a cash flow hedge. In the interest rate swap agreement, the Company paid interest based on the three month LIBOR rate and received interest based on the one month LIBOR rate plus an 8.5 basis point spread. The interest rate swap agreement was intended to hedge the variability in cash flows attributable to changes in interest rates on the remaining monthly variable interest payments on borrowings under the Tranche A facility through the original maturity of the swap agreement on September 30, 2010.

As of December 31, 2008, the Company determined the interest rate swap agreements no longer qualified for hedge accounting as the future payments on the underlying debt were no longer probable of occurring but reasonably possible of occurring beyond the maturity of the existing swaps. As such, the deferred interest rate swaps losses in accumulated other comprehensive loss were frozen and on January 1, 2009, the Company began amortizing these losses using the effective interest method over the remaining life of the interest rate swaps. As of the bankruptcy Petition Date, the Company ceased amortization because interest payments on the underlying debt were stopped. As of September 30, 2009, \$28 million was amortized from accumulated other comprehensive loss to interest expense (\$18 million net of tax) in the accompanying consolidated statements of operations. As previously mentioned, the Company remeasured the interest rate swaps deferred losses in accumulated other comprehensive loss from \$228 million to \$83 million to reflect the component of forecasted interest payments that are likely to occur. The \$145 million remeasurement difference, which represents the component of forecasted interest payments that are unlikely to occur, was recognized as a reorganization item in the consolidated statement of operations during 2009. The remaining deferred balance of \$83 million (\$53 million net of tax) in accumulated other comprehensive loss will be amortized to the statement of operations using the effective interest method over the remaining period of the forecasted interest payments, once interest payments on the debt obligations resume, or upon emergence from bankruptcy, it will be evaluated in accordance with the applicable reorganization accounting rules. See Note 2 for a further explanation of reorganization items.

*Senior Unsecured Notes*

The outstanding senior unsecured notes of \$2,850 million were originally issued under an indenture dated November 17, 2006. During the second quarter of 2007, the Company completed an offer to exchange substantially all of the outstanding senior unsecured notes, which were originally issued in a private placement pursuant to Rule 144A and Regulation S under the Securities Act of 1933, as amended (the Securities Act ), for an equal principal amount of a new issue of senior unsecured notes registered under the Securities Act. The senior unsecured notes

Table of Contents

originally matured on November 17, 2016. Interest was payable semiannually (at 8% per year) in cash to holders of record of senior unsecured notes. The senior unsecured notes were guaranteed by substantially all subsidiaries of Idearc Inc. The senior unsecured notes are general unsecured obligations of Idearc Inc. and are effectively subordinated to all secured indebtedness of Idearc Inc. to the extent of the value of the assets securing this secured indebtedness. Idearc Inc. has no independent assets or operations. The guarantees by its subsidiaries are full and unconditional and joint and several and any subsidiaries of Idearc Inc., other than the subsidiary guarantors, are minor.

**Note 8****Pension and Other Post-Employment Benefit Costs**

The Company provides pension and post-employment benefits to many of its employees. The Company's pension plans are noncontributory defined benefit pension plans. The post-employment health care and life insurance plans for the Company's retirees and their dependents are both contributory and non-contributory and include a limit on the Company's share of cost for recent and future retirees.

*Net Periodic Cost (Income)*

The following tables summarize the benefit costs (income) related to the Company's pension and post-employment health care and life insurance plans for the three and nine months ended September 30, 2009 and 2008:

	Three Months Ended		Pension		Nine Months Ended	
	September 30,				September 30,	
	2009	2008	(in millions)		2009	2008
Service cost	\$ 1	\$ 1	\$ 1	\$ 4	\$ 5	
Interest cost	8	8	8	24	24	
Expected return on plan assets	(10)	(13)	(13)	(33)	(41)	
Amortization of prior service costs			1	1	1	
Amortization of unrecognized net loss (gain)	1			1		
Settlement loss/(gain)	2			9	(3)	
Net periodic benefit (income) cost	\$ 2	\$ (3)	\$ (3)	\$ 6	\$ (14)	

The Company recorded pension settlement losses of \$2 million and \$9 million for the three and nine months ended September 30, 2009, respectively, and settlement gains of \$3 million for the nine months ended September 30, 2008, related to employees that received lump-sum distributions. These charges were recorded in accordance with the applicable accounting rules for settlements and curtailments of defined benefit pension plans and for termination benefits, which require that settlement (gains) losses be recorded once prescribed payment thresholds have been reached. This activity represents a pro rata recognition of the previously unrecognized (gains) losses associated with separated and retired employees.

**Health Care and Life**

Edgar Filing: IDEARC INC. - Form 10-Q

	Three Months Ended				Nine Months Ended			
	September 30,		September 30,		September 30,		September 30,	
	2009	2008	2009	2008	2009	2008	2009	2008
	(in millions)							
Service cost	\$		\$	1	\$	1	\$	2
Interest cost		5		4		13		13
Amortization of prior service costs		(2)		(1)		(4)		(4)
Amortization of unrecognized net loss		1		1		2		4
Net periodic benefit cost	\$	4	\$	5	\$	12	\$	15

Table of Contents

**Note 9**

**Employee Benefits**

*Savings Plans Benefits*

The Company sponsors defined contribution savings plans to provide opportunities for eligible employees to save for retirement on a tax-deferred basis. Substantially all of the Company's employees are eligible to participate in these plans. The Company previously offered three defined contribution plans for the benefit of current and former employees. These three plans were collectively merged effective December 31, 2008 into one plan, and renamed The Idearc Savings Plan. Under this plan, a certain percentage of eligible employee contributions are matched with Company cash allocated to the participants' current investment elections. The Company recognizes savings plan expenses based on its matching obligation attributable to participating employees. For the three and nine months ended September 30, 2009, the Company recorded savings plan expenses of \$6 million and \$18 million, respectively. For the three and nine months ended September 30, 2008, the Company recorded savings plan expenses of \$6 million and \$22 million, respectively.

*Severance Benefits*

For the three and nine months ended September 30, 2009, the Company paid severance benefits of \$2 million and \$5 million, respectively. For the three and nine months ended September 30, 2008, the Company paid severance benefits of \$6 million and \$16 million, respectively.

**Note 10**

**Stock-Based Compensation**

Effective March 4, 2008, the Company adopted the Idearc Inc. 2008 Incentive Compensation Plan (the "2008 Plan"), subject to the approval of the Company's stockholders. The 2008 Plan was approved by the Company's stockholders on May 1, 2008. The 2008 Plan permits the grant of cash and equity-based incentive compensation awards, including restricted stock and restricted stock units, performance shares and performance share units, stock options, stock appreciation rights, deferred stock units and other stock-based awards and performance-based cash incentive awards. The maximum number of shares of Idearc common stock authorized for issuance under the 2008 Plan is 12 million. During 2008, the Company granted awards under the 2008 Plan to employees and non-management directors.

Effective November 16, 2006, the Company adopted the Idearc Inc. Long-Term Incentive Plan (the "2006 Plan"). The 2006 Plan permits the grant of cash and equity-based incentive compensation awards, including restricted stock, restricted stock units, performance shares, performance units, stock options, and other awards, such as stock appreciation rights and cash incentive awards. The maximum number of shares of Idearc common stock authorized for issuance under the 2006 Plan was 2.5 million. Pursuant to the terms of the 2008 Plan, the Company will not issue more than 350,000 shares under the 2006 Plan after December 31, 2007. During 2007 and 2008, the Company granted awards under the 2006 Plan to employees and non-management directors.

*Restricted Stock*

The 2006 and 2008 Plans provide for grants of restricted stock. These awards are classified as equity awards. The fair value of the restricted unit is determined based on the price of Idearc common stock on the date of the grant.

During 2008, certain employees were granted restricted stock awards as part of the Company's 2008 long-term incentive compensation program. These restricted stock awards under the 2008 Plan vest in two equal installments on December 31, 2009, and December 31, 2010. Additionally, our non-management directors were granted restricted stock awards that vested on May 1, 2009.

During 2007, certain employees and our non-management directors were granted restricted stock awards. These employee awards vest in three equal annual installments beginning on the first anniversary of the grant date. The non-management director awards vest on the third anniversary of the grant date.

Dividends are not payable on unvested restricted stock awards. However, if the Company declares and pays a dividend on Idearc common stock, dividend equivalents are granted in an amount equal to the dividend that would have been paid on the unvested restricted stock awards as if they were vested. Dividend equivalents on employee

Table of Contents

restricted stock awards are granted in the form of restricted stock units. Each restricted stock unit will be settled for one share of Idearc common stock on the applicable vesting date. Dividend equivalents on non-management director restricted stock awards are paid in cash on the applicable vesting date. Dividend equivalents are subject to the same vesting, forfeiture and other terms applicable to the corresponding restricted stock awards.

A portion of the cost related to these restricted stock awards is included in the Company's stock-based compensation expense for the three and nine months ended September 30, 2009 and 2008.

Changes in the Company's outstanding restricted stock awards for the nine months ended September 30, 2009, were as follows:

	<b>Number of Restricted Stock Awards (in thousands)</b>	<b>Weighted-Average Grant-Date Fair Value</b>
Outstanding restricted stock at January 1, 2009	2,094	\$ 7.35
Granted	6	1.70
Vested	(367)	15.43
Forfeitures	(82)	7.61
Outstanding restricted stock at September 30, 2009	1,651	\$ 5.52

***Performance Units and Performance Share Units***

The 2006 and 2008 Plans provide for grants of performance units and performance share units that can be settled in cash, shares of Idearc common stock, or a combination thereof. These awards are classified as either liability or equity awards based on the criteria established by the applicable accounting rules for stock-based compensation.

During 2008, certain employees were granted a target number of performance share units under the 2008 Plan as part of the Company's 2008 long-term incentive compensation program. The target number of performance share units may be increased (to a maximum of 200% of the target) or decreased (to zero) based on the Company's total stockholder return (TSR) relative to the TSR of the individual stocks comprising a market benchmark (weighted 80%) and a competitor (weighted 20%) over a three-year measurement period. The measurement period began on March 8, 2008, and will end in 2011 on the 20th trading day following the date the Company releases to the public its annual earnings for the year ending December 31, 2010. Each performance share unit will be settled for one share of Idearc common stock.

Dividends are not payable on performance share units. However, if the Company declares and pays a dividend on Idearc common stock, dividend equivalents are granted in an amount equal to the dividend that would have been paid on an equivalent number of shares of Idearc common stock. Dividend equivalents are granted in the form of additional performance share units and are subject to the same vesting, forfeiture and other terms applicable to the performance share unit award.



## Edgar Filing: IDEARC INC. - Form 10-Q

This award is classified as an equity award. All payments are subject to approval by the Human Resources Committee of the Company's Board of Directors. The performance share unit award liability is measured at its fair value at the time of grant, which, for this purpose, was the date on which the Company's stockholders approved the 2008 Plan. A portion of the cost related to this performance share unit liability is included in the Company's stock-based compensation expense for the three and nine months ended September 30, 2009 and 2008.

During 2007, certain employees were granted a target number of performance units as part of the Company's 2006 long-term incentive compensation program. The target number of performance units may be increased (to a maximum of 150% of the target) or decreased (to zero) based on the Company's TSR relative to the TSR of a market benchmark over a measurement period beginning on January 1, 2007, and ending on December 31, 2009. Each performance unit will be settled in cash upon vesting in an amount equal to the closing price of Idearc common stock on the last trading day in the measurement period.

Dividends are not payable on performance units. However, if the Company declares and pays a dividend on Idearc common stock, dividend equivalents are granted in an amount equal to the dividend that would have been paid on an equivalent number of shares of Idearc common stock. Dividend equivalents are granted in the form of additional performance units and are subject to the same vesting, forfeiture and other terms applicable to the performance unit award.

Table of Contents

This award is classified as a liability award. All payments are subject to approval by the Human Resources Committee of the Company's Board of Directors. The performance unit award liability is measured at its fair value at the end of each reporting period and will fluctuate based on the performance of Idearc common stock and Idearc's TSR relative to the TSR of the market benchmark. A portion of the cost related to this performance unit liability is included in the Company's stock-based compensation expense for the three and nine months ended September 30, 2009 and 2008.

Changes in the Company's outstanding performance units and performance share units for the nine months ended September 30, 2009, were as follows:

	<b>Performance Units / Performance Share Units (in thousands)</b>		<b>Weighted- Average Fair Value</b>
Outstanding performance units/performance share units at January 1, 2009	3,449	\$	2.84
Granted			
Forfeitures	(19)		2.74
Outstanding performance units/performance share units at September 30, 2009	3,430	\$	2.75

***Stock Options***

The 2006 and 2008 Plans provide for grants of stock options. These awards are classified as equity awards.

During 2008, certain employees were granted stock option awards under the 2006 and 2008 Plans. The stock option awards vest on the third anniversary of the grant date and have a ten year term.

A stock option holder may pay the option exercise price in cash by delivering unrestricted shares to the Company having a value at the time of exercise equal to the exercise price, by a cashless broker-assisted exercise, by a combination of these methods or by any other method approved by the Human Resources Committee of the Company's Board of Directors. Options may not be re-priced without the approval of the Company's stockholders.

The fair value of each option award is estimated on the grant date using the Black-Scholes option pricing model. The model incorporates assumptions regarding inputs as follows:

- Expected volatility is a blend of implied volatility based on market-traded options on Idearc common stock and the historical volatility of Idearc stock over its history;

## Edgar Filing: IDEARC INC. - Form 10-Q

- Expected life is based on the SEC shortcut method as described in the SEC's guidance on the valuation of equity share option grants;  
and
- The risk-free interest rate is determined using the U.S. Treasury zero-coupon issue with a remaining term equal to the expected life of the option.

A portion of the cost related to these stock option awards is included in the Company's stock-based compensation expense for the three and nine months ended September 30, 2009 and 2008.

Table of Contents

Changes in the Company's outstanding stock option awards for the nine months ended September 30, 2009 were as follows:

	Number of Stock Option Awards (in thousands)	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (per share)
Outstanding stock option awards at January 1, 2009	650	\$ 3.51	9.46	\$
Granted				
Exercises				
Forfeitures/expirations				
Outstanding stock option awards at September 30, 2009	650	\$ 3.51	8.71	\$

The stock-based compensation expense recognized for the three and nine months ended September 30, 2009, was \$1 million and \$6 million, respectively. For the three and nine months ended September 30, 2008, stock-based compensation expense was \$2 million and \$3 million, respectively. These costs are recorded as part of general and administrative expenses in the accompanying consolidated statements of operations.

As of September 30, 2009, unrecognized compensation expense related to the unvested portion of the Company's restricted stock, performance units, performance share units and stock options was approximately \$5 million and is expected to be recognized over a weighted-average period of approximately 1.1 years.

**Note 11****Income Taxes**

Income taxes for the nine months ended September 30, 2009 and 2008 have been included in the accompanying consolidated financial statements on the basis of an estimated annual effective tax rate. In determining the estimated annual effective tax rate, the Company included interest expense and the tax effect of other discrete items. The Company anticipates the effective tax rate, including interest expense and other discrete items, to approximate 29% for 2009. The full year effective tax rate for 2008 was 34.4%. The decline in the effective tax rate is primarily due to a more favorable permanent tax deduction. The Company's effective tax rate may be subject to changes in future periods as a result of potential changes in business operations and events related to the Chapter 11 bankruptcy proceedings.

**Note 12****Litigation**

On March 31, 2009, (the Petition Date), the Company and all of its domestic subsidiaries filed voluntary petitions in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division (the Bankruptcy Court) seeking reorganization relief under the provisions of Chapter 11 of Title 11 of the United States Code (the Bankruptcy Code). These Chapter 11 cases are being jointly administered under the caption *In re: Idearc Inc. et al*, Case No. 09-31828 (the Chapter 11 Case). The Company continues to operate its business as a

## Edgar Filing: IDEARC INC. - Form 10-Q

debtor-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code. As of the Petition Date, virtually all pending litigation wherein the Company or any of its domestic subsidiaries is named as a defendant is stayed as to the Company and its domestic subsidiaries, and absent further order of the Bankruptcy Court, no party, subject to certain exceptions, may take any action, also subject to certain exceptions, to recover on pre-petition claims against the Company. At this time, it is not possible to predict the outcome of the Chapter 11 Case or its effect on our business or the actions described below.

The Company is subject to various lawsuits and other claims in the normal course of business. In addition, from time to time, the Company receives communications from government or regulatory agencies concerning investigations or allegations of noncompliance with laws or regulations in jurisdictions in which the Company operates.

The Company establishes reserves for the estimated losses on specific contingent liabilities, including the matters described below, for regulatory and legal actions where the Company deems a loss to be probable and the

Table of Contents

amount of the loss can be reasonably estimated. In other instances, the Company is not able to make a reasonable estimate of liability because of the uncertainties related to the outcome and/or the amount or range of loss. The Company does not expect that the ultimate resolution of pending regulatory and legal matters in future periods, including the matters described below, will have a material effect on its financial condition or results of operations.

In October 2007, the Company received a proposed assessment from the State of New York related to sales and use tax on printing and mailing charges. The proposed assessment relates to the audit period March 1998 through May 2005. On May 5, 2008, the State of New York issued a Notice of Determination to the Company for approximately \$28 million. The Company filed its response on July 25, 2008 and any further action has been stayed beyond the outcome of a related matter. The State of New York has also filed multiple proofs of claims in the Bankruptcy Court.

In late December 2008, the Company received tax assessments from the State of Washington related to operating taxes allegedly due on the Company's inter-company transactions. The proposed assessments totaling approximately \$12.5 million relate to the audit period January 1, 2003 through June 30, 2008. On February 19, 2009, the Company filed appeals to these assessments. The first hearing on the Company's appeals was held on October 20, 2009, before a Washington administrative law judge. The Company does not expect a ruling on its appeals before the first quarter of 2010. The State of Washington has also filed multiple proofs of claims in the Bankruptcy Court.

The Company was served with a lawsuit on January 29, 2009, originally filed on January 13, 2009, in the U.S. District Court for the Southern District of California. The plaintiff in this case claims that the Company used plaintiff's copyrighted material without a license in multiple publications across the country. Plaintiff seeks an injunction and both statutory and actual damages. As of February 6, 2009, the time for filing a responsive pleading had not yet run. This matter has been stayed by Idearc's petition for relief filed with the United States Bankruptcy Court on March 31, 2009.

On April 20, 2009, a lawsuit was filed in the District Court of Tarrant County, Texas, against certain of the Company's officers and directors (but not against the Company or its subsidiaries) on behalf of Jack B. Corwin as Trustee of The Jack B. Corwin Revocable Trust, and Charitable Remainder Stewardship Company of Nevada, and as Trustee of the Jack B. Corwin 2006 Charitable Remainder Unitrust. The suit generally alleges that at various times in 2008 and 2009, the named Company officers and directors made false and misleading representations, or failed to state material facts which made their statements misleading, regarding the Company's financial performance and condition. The suit brings fraud and negligent misrepresentation claims and alleges violations of the Texas Securities Act and Section 27 of the Texas Business Commerce Code. The plaintiffs seek unspecified compensatory damages, exemplary damages, and reimbursement for litigation expenses. On June 3, 2009, the plaintiffs filed an amended complaint with the same allegations adding two additional Company directors as party defendants. On June 26, 2009, the Bankruptcy Court entered an injunction prohibiting the prosecution of the Corwin litigation while the Company remains in bankruptcy. The Company plans to honor its indemnification obligations and vigorously defend the lawsuit on the defendants' behalf.

On April 30, 2009, May 21, 2009 and June 5, 2009, three separate putative class action securities lawsuits were filed in the U.S. District Court for the Northern District of Texas, Dallas Division, against certain of the Company's current and former officers (but not on the Company or its subsidiaries). The suits were filed by Jan Buettgen, John Heffner, and Alan Goldberg as three separate named plaintiffs on behalf of purchasers of the Company's common stock between August 10, 2007 and March 31, 2009, inclusive. On May 22, 2009, a putative class action securities lawsuit was filed in the U.S. District Court for the Eastern District of Arkansas, against two of the Company's current officers (but not on the Company or its subsidiaries). The suit was filed by Wade L. Jones on behalf of purchasers of the Company's bonds between March 27, 2008 and March 30, 2009, inclusive. On August 18, 2009, the Wade Jones case from Arkansas federal district court was transferred to be consolidated with this case. The complaints are virtually identical and generally allege that the defendants violated federal securities laws by issuing false and misleading statements regarding the Company's financial performance and condition. Specifically, the complaints allege violations by the defendants of Section 10(b) of the Exchange Act, Rule 10b-5 under the Exchange Act, and Section 20 of the Exchange Act. The plaintiffs are

## Edgar Filing: IDEARC INC. - Form 10-Q

seeking unspecified compensatory damages and reimbursement for litigation expenses. A class has not been certified. Since filing the complaints, all four cases have been consolidated into one court in the Northern District. Each of the plaintiffs have filed motions to be named lead plaintiff and each of the plaintiffs attorneys have filed motions to be named lead plaintiffs counsel. The

Table of Contents

Company's response will not be due until after the motions are resolved. The Company plans to honor its indemnification obligations and vigorously defend the lawsuits on the defendants' behalf.

On July 14, 2009, an unsecured creditor of the Company filed an adversary proceeding against certain of the Company's current and former officers and directors (but not against the Company or its subsidiaries). Other defendants include Verizon Communications Inc. and certain of Verizon's current and former officers and directors. The complaint is a request by this creditor to subordinate all the secured and unsecured claims in the bankruptcy to his claim. The only count aimed at the Company's current and former officers and directors alleges that the individuals breached their fiduciary duty to the plaintiff by allowing Verizon to "loot" the Company and seeks unspecified damages to include recovery of the amount of plaintiff's claim against the Company. The Court granted the Idearc defendants' motion to dismiss the complaint on September 24, 2009, however the plaintiff has asked the court to reconsider that decision. The time for appeal has not yet run. The Company plans to honor its indemnification obligations and vigorously defend the lawsuit on the defendants' behalf.



Table of Contents

**Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.**



## Overview

We are one of the largest yellow pages directories publishers in the United States as measured by revenues, and we believe that we are one of the nation's leading online local search providers. Our products include print yellow pages, print white pages, Superpages.com, our online local search resource, and Superpages Mobile, our information directory for wireless subscribers. We are the exclusive official publisher of Verizon print directories in the markets in which Verizon is currently the incumbent local exchange carrier. We use the Verizon brand on our print directories in these and other specified markets. We are also the exclusive official publisher of print directories in the Maine, New Hampshire, and Vermont markets where FairPoint Communications, Inc. purchased local exchange assets from Verizon.

## Chapter 11 Bankruptcy Filings

On March 31, 2009 (the Petition Date), the Company and its domestic subsidiaries filed voluntary petitions for reorganization under Chapter 11 of Title 11 of the United States Code (the Bankruptcy Code) in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division (the Bankruptcy Court). The cases are being jointly administered under Case No. 09-31828.

Subject to certain exceptions under the Bankruptcy Code, our Chapter 11 bankruptcy filing automatically enjoined, or stayed, the continuation of any judicial or administrative proceedings or other actions against Idearc or our property to recover on, collect or secure a claim arising prior to the Petition Date. Thus, for example, most creditor actions to obtain possession of property from Idearc, or to create, perfect or enforce any lien against the property of Idearc, or to collect on monies owed or otherwise exercise rights or remedies with respect to a pre-petition claim are enjoined unless and until the Bankruptcy Court lifts the automatic stay.

The filing of the Chapter 11 bankruptcy petitions constituted an event of default under our senior secured credit facility and the indenture governing the 8% senior unsecured notes due in 2016, and the debt obligations under those instruments became automatically and immediately due and payable, although any actions to enforce such payment obligations are automatically stayed under the applicable bankruptcy law. In anticipation of this action, the total outstanding debt obligations of \$9,267 million were classified as current maturities of long-term debt in the accompanying consolidated balance sheet at December 31, 2008. Based on the bankruptcy petition, our total outstanding debt obligations as of September 30, 2009 are included in liabilities subject to compromise in the accompanying consolidated balance sheet.

Likewise, the filing of Chapter 11 bankruptcy constituted an event of default under our interest rate swap agreements. As a result, these interest rate swap agreements are no longer deemed financial instruments required to be remeasured at fair value each reporting period, but are now liabilities which are recorded based on management's estimate of the amount to settle the obligations. We recorded these net liabilities as of the bankruptcy Petition Date in the amount of \$496 million. These net liabilities are classified under liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009. See Note 6 to our consolidated financial statements included in this report for additional information related to liabilities subject to compromise.

## Reorganization Process

We are currently operating as a debtor-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code and orders of the Bankruptcy Court. In general, a debtor-in-possession is authorized under Chapter 11 to continue to operate as an ongoing business, but may not engage in transactions outside the ordinary course of business without the prior approval of the Bankruptcy Court. Our business continues to generate positive cash flow necessary for daily operations and as such, it is not expected that debtor-in-possession financing will be needed.

Immediately after filing the Chapter 11 bankruptcy petitions, we began notifying all known current or potential creditors of the bankruptcy filing. Vendors are, however, being paid for goods furnished and services provided after the Petition Date in the ordinary course of business.

Table of Contents

Several bankruptcy hearings have been held since the Company filed for Chapter 11 bankruptcy. The Bankruptcy Court granted interim approval of several of Idearc's first day motions, including the payment of certain pre-petition and post-petition obligations of Idearc related to employee wages, salaries and benefits and certain customer obligations, as well as the continuation of certain customer programs. Also, the Bankruptcy Court authorized the banks to pay outstanding obligations (checks, EFTs, etc.) without interruption in the usual and normal course of business. Additionally, we paid an adequacy protection payment of \$250 million (\$188 million of secured debt principal and \$62 million of accrued interest) to the agent of secured lenders under its senior secured credit facilities (the Lenders) for pro rata distribution to the Lenders and holders of the swap agreements that reduced pre-petition obligations. We have retained legal and financial professionals to advise and assist us with the bankruptcy proceedings. From time to time, we have sought and may continue to seek Bankruptcy Court approval for the retention of additional professionals.

As required by the Bankruptcy Code, the United States Trustee for the Northern District of Texas appointed an official committee of unsecured creditors (the Creditors Committee). The Creditors Committee and its legal representatives have a right to be heard on all matters that come before the Bankruptcy Court with respect to Idearc. There can be no assurance that the Creditors Committee will support Idearc's positions on matters to be presented to the Bankruptcy Court in the future or on any proposed plan of reorganization. Disagreements between Idearc and the Creditors Committee could protract the Chapter 11 proceedings, delaying our emergence from the Chapter 11 bankruptcy proceedings, and thus negatively impact our ongoing operations.

Under Section 365 and other relevant sections of the Bankruptcy Code, we may assume, assume and assign, or reject certain executory contracts and unexpired leases, including, without limitation, leases of real property and equipment, subject to the approval of the Bankruptcy Court and certain other conditions. Any description of an executory contract or unexpired lease in this report, including, where applicable, our express termination rights or a quantification of obligations, must be read in conjunction with, and is qualified by, any overriding rejection rights under Section 365 of the Bankruptcy Code.

**Plan of Reorganization**

On May 15, 2009, the Company submitted a joint plan of reorganization (the Plan) and disclosure statement for consideration by the Bankruptcy Court and the affected creditors. The Plan and disclosure statement described the anticipated organization, operations and financing of the reorganized entity. Among other things, the Plan resolved the Company's pre-petition obligations, set forth the revised capital structure of the newly reorganized entity and provided for the corporate governance subsequent to emergence from bankruptcy. Specifically, the disclosure statement contained certain information about the Company's pre-petition operating and financial history, the events which led up to the commencement of bankruptcy and significant events that have occurred while operating under Chapter 11 of the Bankruptcy Code. The disclosure statement also described the terms and provisions of the Plan, including certain effects of confirmation of the Plan, certain risk factors associated with securities to be issued under the Plan, certain alternatives to the Plan, the manner in which distribution would be made under the Plan, and the confirmation process and the voting procedures that holders of claims and interests entitled to vote under the Plan must follow for their votes to be counted.

On September 8, 2009, Idearc filed the first amended joint plan of reorganization (the Amended Plan) and disclosure statement with revised financial forecasts and the capital structure anticipated at emergence from bankruptcy. The Bankruptcy Court approved our disclosure statement, as it related to the Amended Plan, on September 10, 2009. With the approval of the disclosure statement, we began soliciting votes from our creditors to accept or reject the Amended Plan. The Bankruptcy Court has set the voting deadline for 6:00 p.m. (CST) on November 13, 2009. The hearing at which the Bankruptcy Court will consider confirmation of the Amended Plan is scheduled to commence on December 9, 2009. However, there can be no assurance at this time that the Amended Plan will be confirmed by the Bankruptcy Court or that any such plan will be implemented successfully and on a timely basis.

Under the Amended Plan, if ultimately confirmed by the Bankruptcy Court, allowed secured credit facilities claims will become parties to and be bound by a new term loan agreement in exchange for the cancellation of outstanding debt obligations. The new term loans will be in an aggregate principal amount equal to \$2.75 billion and will mature on the sixth anniversary of the bankruptcy emergence date. The new term loans will bear interest at an annual rate of LIBOR plus 800 basis points with a LIBOR floor of 3.0%. In addition, new issue common stock will

Table of Contents

be distributed to the holders of allowed secured credit facility claims, which will represent 95% of the new common stock to be issued and outstanding on the bankruptcy emergence date. New issue common stock will also be distributed to holders of allowed unsecured note claims, allowed unsecured credit facilities claims and allowed general unsecured claims, which will represent 5% of the new common stock to be issued and outstanding on the bankruptcy emergence date. Finally, under the priority order of claims established in the Amended Plan, any claim for damages arising from the purchase or sale of any old securities, or any claim for reimbursement, contribution, or indemnification on account of any such claim will be impaired and will receive no distributions.

The ultimate recovery to the holders of claims will not be finalized until confirmation of the Amended Plan. No assurance can be given as to what values, if any, will be ascribed in the Chapter 11 proceedings to each constituency or what types or amounts of distributions, if any, they would ultimately receive. The confirmed Amended Plan could result in holders of the Company's liabilities and/or securities, including common stock, receiving no distribution and cancellation of their holdings. Due to these uncertainties, the value of the Company's liabilities and securities, including its common stock, is highly speculative. Appropriate caution should be exercised with respect to existing and future investments in any of the liabilities and securities of the Company. At this time, there is no assurance the Company will be able to restructure as a going concern or successfully implement the Amended Plan.

For periods subsequent to the Chapter 11 bankruptcy filings, the guidance under the applicable reorganization accounting rules has been applied in preparing the accompanying consolidated financial statements. This guidance requires that the financial statements distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Accordingly, certain expenses (including professional fees), realized gains and losses and provisions for losses that are realized from the reorganization process will be classified as reorganization items in the accompanying consolidated statement of operations. See Note 2 to our consolidated financial statements included in this report for additional information related to reorganization items. Additionally, in the accompanying consolidated balance sheet, liabilities are segregated between liabilities not subject to compromise and liabilities subject to compromise. Liabilities subject to compromise are reported at their pre-petition amounts or current unimpaired values, even if they may be settled for lesser amounts. See Note 6 to our consolidated financial statements included in this report for additional information related to liabilities subject to compromise.

**Going Concern Matters**

The accompanying consolidated financial statements and related notes have been prepared assuming that Idearc will continue as a going concern, although the Chapter 11 bankruptcy raises substantial doubt about our ability to continue as a going concern. The accompanying consolidated financial statements do not include any adjustments related to the recoverability and classification of recorded assets or to the amounts classified as liabilities or any other adjustments that might be necessary should Idearc be unable to continue as a going concern.

Idearc continues to be operationally profitable and continues to provide positive operating cash flows. As such, debtor-in-possession financing is not expected to be required. However, we have incurred and will continue to incur significant costs associated with our reorganization process. These costs are being expensed as incurred. In addition, during 2008, we began implementing strategic organizational and market exit initiatives to improve ongoing operational efficiencies. These restructuring efforts have continued throughout 2009. See Note 3 to our consolidated financial statements included in this report for additional information related to restructuring.

**Basis of Presentation**

## Edgar Filing: IDEARC INC. - Form 10-Q

The Company prepares its financial statements in accordance with accounting principles generally accepted in the United States. Pursuant to the rules and regulations of the United States Securities and Exchange Commission (the SEC), the accompanying unaudited consolidated financial statements contain all adjustments, consisting of normal recurring items and accruals, necessary to fairly present the financial position, results of operations and cash flows of Idearc Inc. and its subsidiaries. These interim condensed financial statements do not contain all information and footnote disclosures normally included in financial statements and should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2008. The results for the interim periods are not necessarily indicative of results for the full year. The preparation of these consolidated financial statements requires management to make estimates and judgments that affect the reported amount of assets and



Table of Contents

liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of the financial statements. Certain prior period amounts have been reclassified to conform to current year presentation.

The accompanying unaudited consolidated financial statements do not purport to reflect or provide for the consequences of the Chapter 11 bankruptcy proceedings. In particular, the financial statements do not purport to show (i) as to assets, their realizable value on a liquidation basis or their availability to satisfy liabilities; (ii) as to pre-petition liabilities, the amounts that may be allowed for claims or contingencies, or the status and priority thereof; (iii) as to shareholders' equity (deficit) accounts, the effects of any changes that may be made in the Company's capitalization; or (iv) as to operations, the effects of any changes that may be made to the Company's business.

**New Initiatives**

During 2009, we introduced several marketing initiatives, including the new SuperGuarantee program and its associated national advertising program. The SuperGuarantee program is a consumer focused program designed to make it easier and faster for consumers to find businesses they trust so that when a consumer chooses a client of Idearc, they can count on them to do the job right or we will step in and help to make it right.

**Print Products Advertising Sales**

Our print products advertising sales have continued to decline due to weaker economic conditions and competition from other advertising media. These declines in print products advertising sales will also impact print products revenue into 2010 due to the amortization method of accounting. For the three and nine months ended September 30, 2009, net print products advertising sales declined 22.4% and 19.5%, compared to the same periods in 2008, with multi-product advertising sales declining 20.8% and 17.9% for the same periods, respectively.

**Results of Operations**

*Three Months Ended September 30, 2009 Compared to Three Months Ended September 30, 2008*

The following table sets forth our operating results for the three months ended September 30, 2009 and 2008:

Three months ended September 30,	2009	2008	Change	% Change
	(in millions, except %)			
<b>Operating Revenue</b>				
Print products	\$ 543	\$ 659	\$ (116)	(17.6)%
Internet	68	75	(7)	(9.3)

Edgar Filing: IDEARC INC. - Form 10-Q

Other		1	(1)	(100.0)
<b>Total operating revenue</b>	611	735	(124)	(16.9)
<b>Operating Expense</b>				
Selling	167	176	(9)	(5.1)
Cost of sales (exclusive of depreciation and amortization)	137	151	(14)	(9.3)
General and administrative	104	110	(6)	(5.5)
Depreciation and amortization	17	19	(2)	(10.5)
<b>Total operating expense</b>	425	456	(31)	(6.8)
<b>Operating income</b>	186	279	(93)	(33.3)
Interest expense (income), net	(3)	162	(165)	NM
<b>Income before reorganization items and provision for income taxes</b>				
Reorganization items	189	117	72	61.5
<b>Income before provision for income taxes</b>	154	117	37	31.6
Provision for income taxes	53	44	9	20.5
<b>Net income</b>	\$ 101	\$ 73	\$ 28	38.4%

Table of Contents

***Operating Revenue***

Operating revenue of \$611 million for the three months ended September 30, 2009 decreased \$124 million, or 16.9%, compared to \$735 million for the three months ended September 30, 2008 for the reasons described below.

*Print Products.* Revenue from print products of \$543 million for the three months ended September 30, 2009 decreased \$116 million, or 17.6%, compared to \$659 million for the three months ended September 30, 2008. This decline resulted from reduced advertiser renewals, partially offset by the addition of new advertisers and revenue from new product offerings. We continued to face competition in the print directory market and from other advertising media, including cable television, radio and the Internet. In addition, the impacts of weaker economic conditions have also contributed to declines in our print products revenue.

*Internet.* Internet revenue of \$68 million for the three months ended September 30, 2009 decreased \$7 million, or 9.3%, compared to \$75 million for the three months ended September 30, 2008, primarily driven by declines in fixed fee advertising and weaker economic conditions.

***Operating Expense***

Operating expense of \$425 million for the three months ended September 30, 2009 decreased \$31 million, or 6.8%, compared to \$456 million for the three months ended September 30, 2008 for the reasons described below.

*Selling.* Selling expense of \$167 million for the three months ended September 30, 2009 decreased \$9 million, or 5.1%, compared to \$176 million for the three months ended September 30, 2008. This decrease resulted primarily from lower employee related costs and sales commissions, partially offset by increased costs associated with our national advertising campaign.

*Cost of Sales.* Cost of sales of \$137 million for the three months ended September 30, 2009 decreased \$14 million, or 9.3%, compared to \$151 million for the three months ended September 30, 2008. This decrease was primarily related to lower employee related costs, lower printing and distribution costs, and lower Internet traffic costs.

*General and Administrative.* General and administrative expense of \$104 million for the three months ended September 30, 2009 decreased \$6 million, or 5.5%, compared to \$110 million for the three months ended September 30, 2008. The decrease was largely the result of lower bad debt expense in 2009 and a contract settlement with a former reseller in the third quarter of 2008. These decreases were partially offset by increased employee severance costs related to our ongoing strategic organizational and market exit initiatives, and the impact of recording settlement losses in the three months ended September 30, 2009. Bad debt expense of \$56 million for the three months ended September 30, 2009, decreased by \$4 million, or 6.7%, compared to \$60 million for the three months ended September 30, 2008. The decreased bad debt expense was influenced by reductions in revenue for 2009 as the result of the current weak economic environment. Bad debt expense as a percent of total operating revenue was 9.2% for the three months ended September 30, 2009 compared to 8.2% for the three months ended September 30, 2008.

***Interest Expense (Income), Net***

Interest expense, net of interest income, of (\$3) million for the three months ended September 30, 2009 decreased \$165 million compared to \$162 million for the three months ended September 30, 2008. Since the bankruptcy filing date, interest associated with our debt and interest rate swap agreements is not being accrued.

***Reorganization Items***

During the three months ended September 30, 2009, we recorded \$35 million of reorganization items on a separate line item in the accompanying consolidated statement of operations, in accordance with provisions established by the applicable reorganization accounting rules. Reorganization items represent charges that are directly associated with the process of reorganizing the business under Chapter 11 of the Bankruptcy Code, and include certain expenses (including professional fees), realized gains and losses, and provisions for losses resulting from the reorganization of the business.

Deferred losses in accumulated other comprehensive loss associated with the interest rate swap agreements were remeasured to reflect the component of forecasted interest rate payments that are likely to occur. This resulted

Table of Contents

in a non-cash charge of \$21 million that was recognized as a reorganization item in the accompanying consolidated statement of operations for the three months ended September 30, 2009.

Other reorganization expenses of \$14 million for the three months ended September 30, 2009, primarily consists of professional fees incurred directly associated with the reorganization of the business under Chapter 11 of the Bankruptcy Code.

***Provision for Income Taxes***

Provision for income taxes of \$53 million for the three months ended September 30, 2009 increased \$9 million, or 20.5%, compared to \$44 million for the three months ended September 30, 2008, primarily due to higher pre-tax income as discussed above, offset by the impact of discrete items. The effective tax rate was 34.4% for the three months ended September 30, 2009 compared to 37.6% for the three months ended September 30, 2008. The results for the three months ended September 30, 2009 and 2008 include the effects of discrete items. The Company anticipates the effective tax rate, including interest expense and other one-time discrete items, to approximate 29% for 2009. The full year effective tax rate for 2008 was 34.4%.

***Nine Months Ended September 30, 2009 Compared to Nine Months Ended September 30, 2008***

The following table sets forth our operating results for the nine months ended September 30, 2009 and 2008:

Nine months ended September 30,	2009	2008 (in millions, except %)	Change	% Change
<b>Operating Revenue</b>				
Print products	\$ 1,723	\$ 2,038	\$ (315)	(15.5)%
Internet	211	223	(12)	(5.4)
Other	2	3	(1)	(33.3)
<b>Total operating revenue</b>	<b>1,936</b>	<b>2,264</b>	<b>(328)</b>	<b>(14.5)</b>
<b>Operating Expense</b>				
Selling	528	541	(13)	(2.4)
Cost of sales (exclusive of depreciation and amortization)	436	461	(25)	(5.4)
General and administrative	334	306	28	9.2
Depreciation and amortization	51	59	(8)	(13.6)
<b>Total operating expense</b>	<b>1,349</b>	<b>1,367</b>	<b>(18)</b>	<b>(1.3)</b>
<b>Operating income</b>	<b>587</b>	<b>897</b>	<b>(310)</b>	<b>(34.6)</b>
Interest expense, net	148	491	(343)	(69.9)
<b>Income before reorganization items and provision (benefit) for income taxes</b>				
Reorganization items	439	406	33	8.1
<b>Income (loss) before provision (benefit) for income taxes</b>	<b>440</b>	<b>440</b>	<b>0</b>	<b>NM</b>
Provision (benefit) for income taxes	(1)	406	(407)	NM
<b>Provision (benefit) for income taxes</b>	<b>(1)</b>	<b>146</b>	<b>(147)</b>	<b>NM</b>

Edgar Filing: IDEARC INC. - Form 10-Q

<b>Net income</b>	\$	\$	260	\$	(260)	(100.0)%
-------------------	----	----	-----	----	-------	----------

***Operating Revenue***

Operating revenue of \$1,936 million for the nine months ended September 30, 2009 decreased \$328 million, or 14.5%, compared to \$2,264 million for the nine months ended September 30, 2008 for the reasons described below.

*Print Products.* Revenue from print products of \$1,723 million for the nine months ended September 30, 2009 decreased \$315 million, or 15.5%, compared to \$2,038 million for the nine months ended September 30, 2008. This decline resulted from reduced advertiser renewals, partially offset by the addition of new advertisers and revenue from new product offerings. We continued to face competition in the print directory market and from other advertising media, including cable television, radio and the Internet. In addition, the impacts of weaker economic conditions have also contributed to declines in our print products revenue.

Table of Contents

*Internet.* Internet revenue of \$211 million for the nine months ended September 30, 2009 decreased \$12 million, or 5.4%, compared to \$223 million for the nine months ended September 30, 2008, primarily driven by declines in fixed fee advertising and weaker economic conditions.

***Operating Expense***

Operating expense of \$1,349 million for the nine months ended September 30, 2009 decreased \$18 million, or 1.3%, compared to \$1,367 million for the nine months ended September 30, 2008 for the reasons described below.

*Selling.* Selling expense of \$528 million for the nine months ended September 30, 2009 decreased \$13 million, or 2.4%, compared to \$541 million for the nine months ended September 30, 2008. This decrease resulted primarily from lower employee related costs and sales commission costs, partially offset by increased advertising costs associated with our national advertising campaign.

*Cost of Sales.* Cost of sales of \$436 million for the nine months ended September 30, 2009 decreased \$25 million, or 5.4%, compared to \$461 million for the nine months ended September 30, 2008. This decrease was primarily due to lower printing and distribution costs and reduced employee related costs.

*General and Administrative.* General and administrative expense of \$334 million for the nine months ended September 30, 2009 increased \$28 million, or 9.2%, compared to \$306 million for the nine months ended September 30, 2008. The increase was the result of higher bad debt expense, the impact of recording settlement losses in 2009 associated with our pension plans, while recording settlement gains in 2008, higher stock-based compensation costs and increased employee related costs resulting from a favorable adjustment in 2008. Additionally, we recorded \$19 million of restructuring charges associated with our ongoing strategic organizational, market exit and pre-petition capital restructuring initiatives, of which \$10 million related to pre-petition capital restructuring costs. These increases were partially offset by lower transition costs associated with our spin off from Verizon, lower employee severance costs and a contract settlement with a former reseller in the third quarter of 2008. Bad debt expense of \$178 million for the nine months ended September 30, 2009, increased by \$31 million, or 21.1%, compared to \$147 million for the nine months ended September 30, 2008. Bad debt expense as a percent of total operating revenue was 9.2% for the nine months ended September 30, 2009 compared to 6.5% for the nine months ended September 30, 2008.

***Interest Expense, Net***

Interest expense, net of interest income, of \$148 million for the nine months ended September 30, 2009 decreased \$343 million, or 69.9%, compared to \$491 million for the nine months ended September 30, 2008. Since the bankruptcy filing date, interest associated with our debt and interest rate swap agreements is not being accrued.

***Reorganization Items***

## Edgar Filing: IDEARC INC. - Form 10-Q

During the nine months ended September 30, 2009, we recorded \$440 million of reorganization items on a separate line item in the accompanying consolidated statement of operations, in accordance with provisions established by the applicable reorganization accounting rules. Reorganization items represent charges that are directly associated with the process of reorganizing the business under Chapter 11 of the Bankruptcy Code, and include certain expenses (including professional fees), realized gains and losses, and provisions for losses resulting from the reorganization of the business.

The filing of Chapter 11 bankruptcy constituted an event of default under our interest rate swap agreements. As a result, these interest rate swap agreements are no longer deemed financial instruments required to be remeasured at fair value each reporting period, but are now liabilities which are recorded based on management's estimate of the amount to settle the obligations. This resulted in a non-cash charge of \$279 million that was recognized as a reorganization item in the consolidated statement of operations for the three months ended March 31, 2009.

Deferred losses in accumulated other comprehensive loss associated with the interest rate swaps were remeasured to reflect the component of forecasted interest rate payments that are likely to occur. This resulted in non-cash charges of \$145 million that were recognized as a reorganization item in the accompanying consolidated statement of operations for the nine months ended September 30, 2009.



Table of Contents

Other reorganization expenses of \$16 million for the nine months ended September 30, 2009, primarily consists of professional fees incurred directly associated with the reorganization of the business under Chapter 11 of the Bankruptcy Code.

***Provision (Benefit) for Income Taxes***

Provision (benefit) for income taxes of (\$1) million for the nine months ended September 30, 2009 decreased \$147 million compared to \$146 million for the nine months ended September 30, 2008, primarily due to lower pre-tax income as discussed above. The provision for income taxes reflects an effective tax rate of 36.0% for the nine months ended September 30, 2008, which includes the effects of discrete items. The Company anticipates the effective tax rate, including interest expense and other one-time discrete items, to approximate 29% for 2009. The full year effective tax rate for 2008 was 34.4%.

**Liquidity and Capital Resources**

The following table sets forth a summary of cash flows for the nine months ended September 30, 2009 and 2008:

Nine Months Ended September 30,	2009	2008	Change
		(in millions)	
<b>Cash Flows Provided By (Used In):</b>			
Operating activities	\$ 436	\$ 377	\$ 59
Investing activities	(36)	(35)	(1)
Financing activities	(188)	(86)	(102)
<b>Increase In Cash and Cash Equivalents</b>	<b>\$ 212</b>	<b>\$ 256</b>	<b>\$ (44)</b>

Our primary source of funds continues to be cash generated from operations. Net cash from operations of \$436 million for the nine months ended September 30, 2009, increased \$59 million compared to the nine months ended September 30, 2008. This increase was the result of reduced interest payments on debt associated with our bankruptcy filings, partially offset by increased income tax payments and lower collections associated with declines in revenue.

In April 2009, we made a pre-petition obligation adequacy protection payment to the agent of secured lenders under the Company's senior secured credit facilities of \$250 million, of which \$62 million represented interest payments and is reflected in operating activities. The remaining \$188 million represented secured debt principal payments and is reflected in financing activities.

Net cash used in financing activities of \$188 million for the nine months ended September 30, 2009 increased \$102 million compared to \$86 million for the nine months ended September 30, 2008. This increase is primarily due to the portion of the pre-petition obligation adequacy protection payment which represented debt principal of \$188 million compared to prior year transactions for debt principal payments of \$36 million and dividend payments of \$50 million.

**Critical Accounting Policies**

For periods subsequent to the Chapter 11 bankruptcy filings, the guidance under the applicable reorganization accounting rules has been applied in preparing the accompanying consolidated financial statements. This guidance requires that the financial statements distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Accordingly, certain expenses (including professional fees), realized gains and losses and provisions for losses that are realized from the reorganization process will be classified as reorganization items in the accompanying consolidated statement of operations. See Note 2 to our consolidated financial statements included in this report for additional information related to reorganization items. Additionally, in the consolidated balance sheet, liabilities are segregated between liabilities not subject to compromise and liabilities subject to compromise. Liabilities subject to compromise are reported at their pre-petition amounts or current unimpaired values, even if they may be settled for lesser amounts. See Note 6 to our consolidated financial statements included in this report for additional information related to liabilities subject to compromise.

Table of Contents

For the Company's other critical accounting policies, see Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2008.

**Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements that are material to our results of operations, financial condition or liquidity.

**Recent Accounting Pronouncements**

*Enhanced Disclosures for Postretirement Benefit Plan Assets*

In December 2008, the Financial Accounting Standards Board ( FASB ) amended the disclosure requirement of assets held in an employer's defined benefit pension or other postretirement plan. Effective for periods after December 15, 2009, the Company will disclose for each major category of plan assets, its valuation within the fair value hierarchy.

*Interim Disclosures about Fair Value of Financial Instruments*

In April 2009, the FASB amended the disclosure requirements for the fair value of financial instruments. The guidance requires publicly traded companies to disclose the fair value of financial instruments in interim reporting periods and in the annual financial statements. The guidance enhances consistency in financial reporting by increasing the frequency of fair value disclosures to a quarterly basis for any financial instruments. The Company adopted the new disclosure requirements effective for the quarter ended June 30, 2009. See Note 5 to our consolidated financial statements included in this report for additional information on fair value disclosures.

*Subsequent Events*

In June 2009, the FASB issued accounting guidance that requires companies to recognize in the financial statements the effects of subsequent events that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. An entity shall disclose the date through which subsequent events have been evaluated, as well as whether that date is the date the financial statements were issued. Companies are not permitted to recognize subsequent events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after the balance sheet date and before financial statements are issued. Some non-recognized subsequent events must be disclosed to keep the financial statements from being misleading. For such events a company must disclose the nature of the event, an estimate of its financial effect, or a statement that such an estimate cannot be made. The accounting guidance applies prospectively for interim or annual financial periods ending after June 15, 2009. The Company adopted the new accounting rules associated with subsequent events effective for the quarter ended June 30, 2009 consolidated financial statements and

disclosures.

The Company evaluates events and transactions that occur after the balance sheet date as potential subsequent events. This evaluation was performed through November 6, 2009, the date on which the Company's accompanying consolidated financial statements were issued.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk.**



*Chapter 11 Bankruptcy Filings*

On March 31, 2009, the Company and its domestic subsidiaries filed voluntary petitions in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division seeking reorganization relief under the provisions of Chapter 11 of Title 11 of the United States Code. The filing of the Chapter 11 petitions constituted an event of default under certain of the Company's debt obligations and interest rate swap agreements, and those debt obligations and interest rate swap agreements became automatically and immediately due and payable. However, under applicable bankruptcy law, an automatic stay of action to collect, assert, or recover a claim against the Company is now in effect. The Company's debt obligations of \$9,079 million are classified as liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009. The debt obligations balance reflects the payment of a court approved adequacy protection payment of \$250 million (\$188 million of

Table of Contents

secured debt principal and \$62 million of accrued interest) made in April 2009 to the agent of secured lenders under the Company's senior secured credit facilities.

Other than the adequacy protection payment of principal and interest discussed above, the Company did not make any scheduled principal payments in 2009 or any interest payments since February 2009. As stipulated in the debt credit agreement, the interest rate was automatically changed to the Prime Rate (called the Alternative Base Rate or ABR) plus a basis point spread on the revolving credit facility, Tranche A Facility, and Tranche B Facility which equates to an all-in interest rate of 5.75%, 5.75% and 6.25%, respectively. However, since the filing of the bankruptcy petitions, interest associated with the debt and interest rate swap agreements is not being accrued.

In accordance with guidance under the applicable reorganization accounting rules, the debt issuance costs should be viewed as valuations of the related debt obligations. When the debt obligations become allowed claims and the allowed claims differ from the net carrying amount of the debt obligations, the recorded amount should be adjusted to the amount of the allowed claims (thereby adjusting existing debt issuance costs to the extent necessary to report debt obligations at this allowed amount). Through September 30, 2009, the Bankruptcy Court had not classified any of the debt obligations as allowed claims. Therefore, the debt obligations have been categorized under liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009. The debt issuance costs of \$73 million as of September 30, 2009 have not been adjusted. The Company may be required to record these amounts or a portion thereof in the consolidated statement of operations as a reorganization item if the Bankruptcy Court ultimately determines that a portion of the debt obligation is subject to compromise. See Note 6 to our consolidated financial statements included in this report for additional information related to liabilities subject to compromise.

Due to the bankruptcy filing, the Company's interest rate swap agreements are no longer deemed financial instruments required to be remeasured at fair value each reporting period, but are now liabilities which are recorded based on management's estimate of the amount to settle the obligations. The Company recorded these net liabilities as of the bankruptcy Petition Date in the amount of \$496 million. These liabilities are classified under liabilities subject to compromise in the accompanying consolidated balance sheet as of September 30, 2009. Accordingly, the Company recorded a loss of \$279 million which represented the difference in the carrying amount of the liability prior to the bankruptcy Petition Date and the expected amount of the allowed claim. The loss was recognized during the three months ended March 31, 2009 in the consolidated statement of operations as a reorganization item. See Note 2 to our consolidated financial statements included in this report for a further explanation of reorganization items.

On September 10, 2009, the Bankruptcy Court approved the Company's disclosure statement, as it relates to the Amended Plan. Under the Amended Plan, if ultimately confirmed by the Bankruptcy Court, allowed secured credit facilities claims will become parties to and be bound by a new term loan agreement in exchange for the cancellation of outstanding debt obligations. The new term loans will be in aggregate principal amount equal to \$2.75 billion and will mature on the sixth anniversary of the bankruptcy emergence date. As such, a portion of the forecasted interest payments on the original, higher principal debt are not probable of occurring, therefore, the deferred losses in accumulated other comprehensive loss associated with the interest rate swaps were remeasured from \$228 million to \$83 million as of September 30, 2009. The \$145 million remeasurement difference was recognized as a reorganization item in the accompanying consolidated statement of operations during 2009. The remaining deferred balance of \$83 million (\$53 million net of tax) in accumulated other comprehensive loss will be amortized to the consolidated statement of operations using the effective interest method over the remaining period of the forecasted interest payments, once interest payments on the debt obligations resume, or upon emergence from bankruptcy, it will be evaluated in accordance with the applicable reorganization accounting rules. Any additional reduction in the proposed debt level would result in deferred losses recorded in accumulated other comprehensive loss being remeasured and recognized as reorganization expense in the consolidated statement of operations. See Note 2 to our consolidated financial statements included in this report for a further explanation of reorganization items.

**Item 4. Controls and Procedures.**





**Disclosure Controls**

Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Exchange Act) as of the end of the period covered by this

Table of Contents

report. Based on that evaluation, our chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report to provide reasonable assurance that information we are required to disclose in reports that are filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms specified by the SEC. We note that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving the stated goals under all potential future conditions.

**Changes in Internal Control Over Financial Reporting**

There have not been any changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) promulgated under the Exchange Act) during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

**PART II - OTHER INFORMATION**



**Item 1. Legal Proceedings.**



## Edgar Filing: IDEARC INC. - Form 10-Q

On March 31, 2009, (the Petition Date ), the Company and all of its domestic subsidiaries filed voluntary petitions in the United States Bankruptcy Court for the Northern District of Texas, Dallas Division (the Bankruptcy Court ) seeking reorganization relief under the provisions of Chapter 11 of Title 11 of the United States Code (the Bankruptcy Code ). These Chapter 11 cases are being jointly administered under the caption *In re: Idearc Inc. et al*, Case No. 09-31828 (the Chapter 11 Case ). The Company continues to operate its business as a debtor-in-possession under the jurisdiction of the Bankruptcy Court and in accordance with the applicable provisions of the Bankruptcy Code. As of the Petition Date, virtually all pending litigation wherein the Company or any of its domestic subsidiaries is named as a defendant is stayed as to the Company and its domestic subsidiaries, and absent further order of the Bankruptcy Court, no party, subject to certain exceptions, may take any action, also subject to certain exceptions, to recover on pre-petition claims against the Company. At this time, it is not possible to predict the outcome of the Chapter 11 Case or its effect on our business or the actions described below.

The Company is subject to various lawsuits and other claims in the normal course of business. In addition, from time to time, the Company receives communications from government or regulatory agencies concerning investigations or allegations of noncompliance with laws or regulations in jurisdictions in which the Company operates.

The Company establishes reserves for the estimated losses on specific contingent liabilities, including the matters described below, for regulatory and legal actions where the Company deems a loss to be probable and the amount of the loss can be reasonably estimated. In other instances, the Company is not able to make a reasonable estimate of liability because of the uncertainties related to the outcome and/or the amount or range of loss. The Company does not expect that the ultimate resolution of pending regulatory and legal matters in future periods, including the matters described below, will have a material effect on its financial condition or results of operations.

In October 2007, the Company received a proposed assessment from the State of New York related to sales and use tax on printing and mailing charges. The proposed assessment relates to the audit period March 1998 through May 2005. On May 5, 2008, the State of New York issued a Notice of Determination to the Company for approximately \$28 million. The Company filed its response on July 25, 2008 and any further action has been stayed beyond the outcome of a related matter. The State of New York has also filed multiple proofs of claims in the Bankruptcy Court.

In late December 2008, the Company received tax assessments from the State of Washington related to operating taxes allegedly due on the Company's inter-company transactions. The proposed assessments totaling approximately \$12.5 million relate to the audit period January 1, 2003 through June 30, 2008. On February 19, 2009, the Company filed appeals to these assessments. The first hearing on the Company's appeals was held on October 20, 2009, before a Washington administrative law judge. The Company does not expect a ruling on its appeals before the first quarter of 2010. The State of Washington has also filed multiple proofs of claims in the Bankruptcy Court.

The Company was served with a lawsuit on January 29, 2009, originally filed on January 13, 2009, in the U.S. District Court for the Southern District of California. The plaintiff in this case claims that the Company used plaintiff's copyrighted material without a license in multiple publications across the country. Plaintiff seeks an injunction and both statutory and actual damages. As of February 6, 2009, the time for filing a responsive pleading had not yet run. This matter has been stayed by Idearc's petition for relief filed with the United States Bankruptcy Court on March 31, 2009.

On April 20, 2009, a lawsuit was filed in the District Court of Tarrant County, Texas, against certain of the Company's officers and directors (but not against the Company or its subsidiaries) on behalf of Jack B. Corwin as Trustee of The Jack B. Corwin Revocable Trust, and Charitable Remainder Stewardship Company of Nevada, and as Trustee of the Jack B. Corwin 2006 Charitable Remainder Unitrust. The suit generally alleges that at various times in 2008 and 2009, the named Company officers and directors made false and misleading representations, or failed to state material facts which made their statements misleading, regarding the Company's financial performance and condition. The suit brings fraud and negligent misrepresentation claims and alleges violations of the Texas Securities Act and Section 27 of the Texas Business Commerce Code. The plaintiffs seek unspecified compensatory damages, exemplary damages, and reimbursement for litigation expenses. On June 3, 2009, the





Table of Contents

plaintiffs filed an amended complaint with the same allegations adding two additional Company directors as party defendants. On June 26, 2009, the Bankruptcy Court entered an injunction prohibiting the prosecution of the Corwin litigation while the Company remains in bankruptcy. The Company plans to honor its indemnification obligations and vigorously defend the lawsuit on the defendants' behalf.

On April 30, 2009, May 21, 2009 and June 5, 2009, three separate putative class action securities lawsuits were filed in the U.S. District Court for the Northern District of Texas, Dallas Division, against certain of the Company's current and former officers (but not on the Company or its subsidiaries). The suits were filed by Jan Buettgen, John Heffner, and Alan Goldberg as three separate named plaintiffs on behalf of purchasers of the Company's common stock between August 10, 2007 and March 31, 2009, inclusive. On May 22, 2009, a putative class action securities lawsuit was filed in the U.S. District Court for the Eastern District of Arkansas, against two of the Company's current officers (but not on the Company or its subsidiaries). The suit was filed by Wade L. Jones on behalf of purchasers of the Company's bonds between March 27, 2008 and March 30, 2009, inclusive. On August 18, 2009, the Wade Jones case from Arkansas federal district court was transferred to be consolidated with this case. The complaints are virtually identical and generally allege that the defendants violated federal securities laws by issuing false and misleading statements regarding the Company's financial performance and condition. Specifically, the complaints allege violations by the defendants of Section 10(b) of the Exchange Act, Rule 10b-5 under the Exchange Act, and Section 20 of the Exchange Act. The plaintiffs are seeking unspecified compensatory damages and reimbursement for litigation expenses. A class has not been certified. Since filing the complaints, all four cases have been consolidated into one court in the Northern District. Each of the plaintiffs have filed motions to be named lead plaintiff and each of the plaintiffs' attorneys have filed motions to be named lead plaintiffs' counsel. The Company's response will not be due until after the motions are resolved. The Company plans to honor its indemnification obligations and vigorously defend the lawsuits on the defendants' behalf.

On July 14, 2009, an unsecured creditor of the Company filed an adversary proceeding against certain of the Company's current and former officers and directors (but not against the Company or its subsidiaries). Other defendants include Verizon Communications Inc. and certain of Verizon's current and former officers and directors. The complaint is a request by this creditor to subordinate all the secured and unsecured claims in the bankruptcy to his claim. The only count aimed at the Company's current and former officers and directors alleges that the individuals breached their fiduciary duty to the plaintiff by allowing Verizon to loot the Company and seeks unspecified damages to include recovery of the amount of plaintiff's claim against the Company. The Court granted the Idearc defendants' motion to dismiss the complaint on September 24, 2009, however the plaintiff has asked the court to reconsider that decision. The time for appeal has not yet run. The Company plans to honor its indemnification obligations and vigorously defend the lawsuit on the defendants' behalf.

**Item 1A. Risk Factors.**

There are numerous factors that affect our business and results of operations, many of which are beyond our control. In addition to other information set forth in this Quarterly Report, you should carefully read and consider Item 1A. Risk Factors in Part I, and Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operation in Part II of our 2008 Annual Report on Form 10-K for the year ended December 31, 2008, which contain a description of significant factors that might cause the actual results of operations in future periods to differ materially from those currently expected or desired. Set forth below are several risk factors that have been modified or have materially changed from the risk factors discussed in our 2008 Annual Report. The risks described in this Quarterly Report and in our 2008 Annual Report are not the only risks facing our Company. Additional risks and uncertainties are currently deemed immaterial based on management's assessment of currently available information, which remains subject to change, however, new risks that are currently unknown to us may surface in the future which materially adversely affect our business, financial condition, operating results or cash flow in the future.

**Risks Related to Our Chapter 11 Bankruptcy Filings**

*We filed voluntary petitions for reorganization under the Bankruptcy Code which may have an adverse effect on our business, financial condition and results of operation.*

On March 31, 2009, the Company and all of its domestic subsidiaries (collectively, the Company ), filed voluntary petitions seeking reorganization relief under the Bankruptcy Code. During the Chapter 11 bankruptcy, our operations are subject to the risks and uncertainties associated with bankruptcy. The time and resources required to reorganize our business in bankruptcy may make it more difficult to promote our services and attract and retain

Table of Contents

customers. Our suppliers, vendors and service providers may require stricter terms and conditions. The loss of any of our customers or suppliers during the pendency of the Chapter 11 bankruptcy could have an adverse effect on our business, financial condition and results of operations. In addition, we may experience other adverse effects, including, without limitation, a loss of confidence by current and prospective suppliers. Any failure to timely obtain suitable supplies at competitive prices could materially adversely affect our businesses, financial condition and results of operations.

*We may have insufficient liquidity to successfully operate our business.*



## Edgar Filing: IDEARC INC. - Form 10-Q

We expect to incur significant costs as a result of the Chapter 11 bankruptcy and the transactions contemplated by the plan of reorganization. We expect to incur substantial costs for professional fees and other expenses. We have negotiated use of cash collateral in order to have access to existing cash balances to fund working capital expenses as well as all other expenses incurred throughout the pendency of the Chapter 11 bankruptcy. In the future, we may need to obtain additional financing to fund our operations and capital expenditures. If financing is needed in the future, there can be no assurance as to our ability to obtain sufficient financing. We are currently financing our operations and the reorganization using cash on hand. The challenges of obtaining financing are exacerbated by adverse conditions in the general economy and the tightening in the credit markets. These conditions and our Chapter 11 bankruptcy may make it more difficult for us to obtain financing.

*Our business could suffer from the loss of key personnel.*



## Edgar Filing: IDEARC INC. - Form 10-Q

We are dependent on the continued services of our senior management team and other key personnel. The loss of key personnel could have a material adverse effect on our business, financial condition and results of operations. We may be unable to retain and motivate key executives and employees through the process of reorganization and we may have difficulty attracting new employees. In addition, so long as the Chapter 11 bankruptcy continues, our senior management will be required to spend a significant amount of time and effort dealing with the reorganization instead of focusing exclusively on business operations.

*We are unable to take advantage of business opportunities during the Chapter 11 bankruptcy without Bankruptcy Court approval.*





## Edgar Filing: IDEARC INC. - Form 10-Q

Transactions outside the ordinary course of business are subject to the prior approval of the Bankruptcy Court, which may limit our ability to respond timely to certain events or take advantage of certain opportunities. In addition, the Bankruptcy Code limits our ability to incur additional indebtedness, make investments, sell assets, consolidate, merge or sell or otherwise dispose of all or substantially all of our assets or grant liens. These restrictions may place us at a competitive disadvantage. We may be unable to continue to grow our business through acquisitions and restrictions on our ability to pursue other business strategies, unless we obtain Bankruptcy Court approval for those transactions.

*Pursuit of litigation by the parties in interest could disrupt the confirmation of the plan of reorganization (the Plan ) and could have material adverse effects on the Company s business and financial condition.*



## Edgar Filing: IDEARC INC. - Form 10-Q

There can be no assurance that any parties in interest will not pursue litigation strategies to enforce any claims against the Company. Litigation is by nature uncertain and there can be no assurance of the ultimate resolution of such claims. Certain creditors have asserted the invalidity of certain liens in the bankruptcy proceedings. The pursuit of litigation in connection with objections to the Company's disclosure statement related to the invalidity of liens could delay and disrupt confirmation of the Plan and the Company's emergence from bankruptcy. Any litigation may be expensive, lengthy, and disruptive to the Company's normal business operations and the plan confirmation process, and a resolution of any such strategies that is unfavorable to the Company could have a material adverse effect on the plan confirmation process, emergence from bankruptcy or its business, results of operations, financial condition, liquidity or cash flow.

*We may not be able to consummate a successful plan of reorganization or obtain Bankruptcy Court approval.*



## Edgar Filing: IDEARC INC. - Form 10-Q

There can be no assurance that we will be able to successfully execute, confirm and consummate one or more plans of reorganization with respect to the Chapter 11 bankruptcy that are acceptable to the Bankruptcy Court and the Company's creditors and other parties in interest. Additionally, third parties may seek and obtain Bankruptcy

Table of Contents

Court approval to terminate or shorten the exclusivity period for the Company to propose and confirm one or more plans of reorganization, to appoint a Chapter 11 trustee, or to convert the case to a Chapter 7 bankruptcy.

***The Bankruptcy Court could exercise substantial discretion and could prevent the confirmation of the plan of reorganization in its current form.***

Even if we obtain enough votes in favor of the plan of reorganization, the Bankruptcy Court, which, as a court of equity, may exercise substantial discretion, may choose not to confirm the plan or reorganization. Section 1129 of the Bankruptcy Code requires, among other things, a showing that confirmation of the plan of reorganization will not be followed by liquidation or the need for further financial reorganization of the Company, and that the value of distributions to dissenting holders of claims and interests will not be less than the value such holders would receive if the Company was liquidated under Chapter 7 of the Bankruptcy Code. Although we believe that the plan of reorganization will meet such standards, there can be no assurance that the Bankruptcy Court will reach the same conclusion.

***A long and protracted restructuring process could adversely affect the Company's business and financial condition.***





## Edgar Filing: IDEARC INC. - Form 10-Q

If a liquidation or protracted reorganization process were to occur, there is a significant risk that the value of our enterprise would be substantially eroded. Our future results are dependent upon the successful confirmation and implementation of a plan of reorganization. Failure to obtain this approval in a timely manner could adversely affect our operating results, as our ability to fund operations and maintain relations with customers and suppliers may be harmed by protracted bankruptcy proceedings. Furthermore, we cannot predict the ultimate amount of all settlement terms for our liabilities that will be subject to a plan of reorganization. Once a plan of reorganization is approved and implemented, our operating results may be adversely affected by the possible reluctance of prospective customers, suppliers and other business partners to do business with a company that recently emerged from bankruptcy proceedings. Even assuming a successful emergence from bankruptcy, there can be no assurance as to the overall long-term viability of our business.

*Our inability to assume any of our key agreements with Verizon could have a material adverse effect on our business.*

On April 15, 2009, we filed a motion to assume certain on-going commercial contracts with Verizon, including assumption of the publishing agreement, the branding agreement, the non-competition agreement, the listings license agreement, and the intellectual property agreement in their current forms. However, if we are unable to assume any of these key agreements with Verizon, it could have a material adverse effect on our business.

*Adverse publicity in connection with the Chapter 11 bankruptcy or otherwise, could negatively affect our business.*



Adverse publicity or news coverage relating to us, including, but not limited to, publicity or news coverage in connection with the Chapter 11 bankruptcy, may negatively impact our efforts to establish and promote name recognition and a positive image after emergence from the Chapter 11 bankruptcy.

**Risks Related to Our Business and Our Financial Condition**

*We have defaulted under our senior secured credit facility and our senior notes.*

Our consolidated audited financial statements for the fiscal year ending December 31, 2008 contained an explanatory paragraph regarding our ability to continue as a going concern, which constituted a default under our senior secured credit facility (the Senior Credit Facility). On March 31, 2009, we failed to make scheduled payments under the Senior Credit Facility of approximately \$42 million in interest and approximately \$31 million in principal, resulting in an additional default under the Senior Credit Facility. Our voluntary filing of the bankruptcy case constituted an event of default under the Senior Credit Facility. As a result of such defaults, the commitments under the Senior Credit Facility immediately terminated and all borrowings, with accrued interest thereon, and all other amounts owed by us, including all amounts under outstanding letters of credit, became immediately due and payable. In addition, the bankruptcy filing constituted an event of default under the indenture governing the

Table of Contents

Company's 8% senior unsecured notes due in 2016 (the "Unsecured Notes"). As a result of such default, the principal amount plus accrued and unpaid interest on the Unsecured Notes is due and payable. As of September 30, 2009, the aggregate principal amounts outstanding under the Senior Credit Facility, including the termination value of interest rate swap agreements, are approximately \$6,725 million and the aggregate principal amounts outstanding under the Unsecured Notes are approximately \$2,850 million. There are multiple defaults that are continuing and uncured under the Senior Credit Facility and indenture governing the Unsecured Notes.

Since our lenders have declared the total debt outstanding to be due and payable, we do not have sufficient liquidity to satisfy our total debt obligations. However, as a result of our bankruptcy filing, the ability of creditors to seek remedies to enforce their rights under the Senior Credit Facility and the Unsecured Notes have been stayed, and creditor rights of enforcement are subject to the applicable provisions of the Bankruptcy Code. In our Chapter 11 bankruptcy, we have negotiated with the holders of the Senior Credit Facility and Unsecured Notes to restructure our total debt obligations.

We urge that caution be exercised with respect to existing and future investments in our equity securities as it is anticipated that a restructuring under a plan of reorganization will substantially change our capital structure, including, without limitation, the extinguishment of existing common stock without distribution to existing equity holders.

A restructuring consummated in a proceeding under federal bankruptcy laws could result in significant changes to our current debt and equity ownership structure. We expect a restructuring will likely result in our assets and liabilities being re-valued using "fresh start" accounting as provided by the guidance under the applicable reorganization accounting rules.

The accompanying consolidated financial statements included in this report have been prepared on a going concern basis, which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. The ability of the Company to continue as a going concern is predicated upon, among other things, our successful restructuring of our capitalization and debt service obligations. There can be no assurance that the capital restructure plans will be successfully completed; and therefore, there is uncertainty about our ability to realize our assets or satisfy our liabilities in the normal course of business. Our consolidated financial statements do not include any adjustments that might result from the resolution of this uncertainty.

***Our restructuring efforts to strengthen our balance sheet and reduce our debt will most likely adversely affect holders of our common stock through a complete loss in value.***

Our plan of reorganization to restructure our capital structure and reduce our debt service obligations will most likely include additional issuances of equity securities in exchange for our indebtedness. Any debt securities or preferred stock that might be issued will have liquidation rights, preferences and privileges senior to those of holders of our current outstanding common stock. The issuance of additional shares of our common stock may be dilutive to our stockholders, including holders who receive shares of common stock in any restructuring.

We cannot predict the extent to which this dilution and the possibility of additional issuances and sales of our common stock will negatively affect the trading price or the liquidity of our common stock. In addition, there is a strong possibility that our restructuring efforts could result in holders of our common stock receiving no value for their holdings and the holders of our existing debt receiving a significant portion or all the equity interest in the Company.

*The liquidity of any trading market that currently exists for the Unsecured Notes may be further adversely affected by our plan to restructure our balance sheet and debt service obligations. Holders of the Unsecured Notes will most likely find it more difficult to sell their Unsecured Notes when they want to, and if they do, they may not be able to receive the price they want.*

There is currently limited trading for the Unsecured Notes. The trading market for the Unsecured Notes may become more limited or may cease altogether as a result of our filing petitions seeking reorganization relief under the Bankruptcy Code. The market price of the Unsecured Notes has suffered significant declines and remains volatile, increasing the risk of loss to holders of the Unsecured Notes. The market price of the Unsecured Notes will most likely continue to be subject to significant fluctuations in response to various factors and events, including the depth and liquidity of the trading market for the Unsecured Notes, variations in our operating results and general

Table of Contents

economic and competitive conditions. The extent of the markets for the Unsecured Notes and the availability of price quotations will depend upon a number of factors, including the number of holders of Unsecured Notes and the interest of securities firms in maintaining a market in the Unsecured Notes. In addition, there is a possibility that any of our restructuring efforts may result in a substantial reduction in the principal amount of the Unsecured Notes or the holders of the Unsecured Notes receiving little or no value for their holdings in the company.

***We face widespread competition from other print directory publishers and other traditional and new media. This competition may reduce our market share or materially adversely affect our financial performance.***

The directory advertising industry in the United States is highly competitive. The incumbent publishers with which we compete include AT&T and R.H. Donnelley. Independent publishers with which we compete include Yellowbook (the U.S. business of Yell Group), Valley Yellow Pages and White Directory Publishing Inc. We compete with Yellowbook in the majority of our major markets.

Some of the incumbent publishers with which we compete are or may become larger than we are and have or may obtain greater financial resources than we have. Although we may have limited market overlap with incumbent publishers relative to the size of our overall footprint, we may not be able to compete effectively with these publishers for advertising sales in these limited markets. In addition, independent publishers may commit more resources to certain markets than we are able to commit, thus limiting our ability to compete effectively in these areas. Given the mature state of the directory advertising industry and our position in most of our markets, independent publishers are typically focused on aggressive pricing to gain market share.

We also compete for advertising sales with other traditional media, including newspapers, magazines, radio, direct mail, telemarketing, billboards and television. Many of these competitors are larger than we are and have greater financial resources. The market share of these competitors may increase and our market share may decrease. Since we have filed our Chapter 11 bankruptcy and competitors have not filed bankruptcy (except that on May 28, 2009, R.H. Donnelley and its subsidiaries filed voluntary petitions for reorganization under Chapter 11 of the Bankruptcy Code), we are at a disadvantage and our competitors may leverage our position with potential and existing customers.

We also compete for advertising sales with other new media. The Internet has become increasingly accessible as an advertising medium for businesses of all sizes. Further, the use of the Internet, including as a means to transact commerce through wireless devices, has resulted in new technologies and services that compete with our traditional products and services. Through Superpages.com, our online local search product, we compete with the Internet yellow pages directories of other major and independent directory publishers, such as Yellowpages.com, as well as other Internet sites that provide classified directory information, such as Citysearch.com.

Our Internet products also compete with search engines and portals, such as Google, Yahoo! and AOL, some of which have entered into commercial agreements with us or with other major directory publishers. We may not be able to compete effectively for advertising with these other companies, some of which have greater resources than we do. Our Internet strategy may be adversely affected if major search engines build local sales forces or otherwise begin to more effectively market to small- and medium-sized local businesses.

***Further transfers of local exchange assets by Verizon could reduce the benefit of using the Verizon brand name.***

## Edgar Filing: IDEARC INC. - Form 10-Q

In 2008, Verizon transferred rural exchange assets in three states to FairPoint Communications, Inc. In connection with this transaction, the Company entered into publishing, branding and non-competition agreements with FairPoint Communications, Inc. and its affiliates. In May 2009, Verizon entered into an agreement to transfer additional rural exchange assets in 14 states to Frontier Communications Corp. Although the purchasers of the Verizon local service areas are required to enter into publishing, branding and non-competition agreements with terms substantially the same as those contained in the corresponding Verizon agreements, transfers to third parties decrease the scope of our license to use the Verizon brand name.

*Increased competition in local telephone markets could reduce the benefit of using the Verizon brand name.*

The Federal Communications Commission rules regarding local number portability, advances in communications technology (including wireless devices and voice over Internet protocol) and demographic factors (including potential shifts from wireline telephone communications to wireless or other communications

Table of Contents

technologies) may erode the market position of telephone service providers, including Verizon. We believe that the use of traditional wireline carriers, including Verizon, is declining. We believe the loss of market share by Verizon in any particular local service area decreases the value of our license to use the Verizon brand name in particular local telephone markets. As a result, we may not realize the expected benefits of our commercial contracts with Verizon.

***Our business and financial condition would be adversely affected by a prolonged economic downturn.***

Our business is subject to the adverse economic conditions currently present in the United States, including decreased levels of business activity across many market segments, decreased advertising demand, interest rate volatility, and limited credit availability. Our total operating revenues in 2008 were negatively affected by the economic downturn, which has continued in 2009.

Substantially all of our revenues are derived from the sale of advertising. Expenditures by advertising clients are sensitive to economic conditions and tend to decline in a recession or other periods of uncertainty. A continuation of current economic conditions could further reduce the advertising spend of our clients.

***Our reliance on small- and medium-sized businesses exposes us to increased credit risks.***

As of December 31, 2008, approximately 84% of our print directory advertising revenues were derived from selling advertising to local businesses, which are generally small- and medium-sized businesses. In the ordinary course of our directory operations, we bill most of these clients over the course of a 12-month period. Full collection of delinquent accounts can take many months or may never occur. For 2008, bad debt expense represented 6.9% of our net revenue, an increase from 5.0% in 2007. In addition, for the first nine months of 2009 bad debt expense represented 9.2% of our total operating revenue, an increase from 6.5% in the first nine months of 2008. Small- and medium-sized businesses tend to have fewer financial resources and higher rates of failure than larger businesses, in particular during periods of economic downturn, such as we are currently experiencing. These factors increase our exposure to delinquent accounts by our clients.

***Since we have renegotiated higher interest rates in exchange for the reduction of our total outstanding debt, our interest expense will increase relative to the amount of outstanding debt.***

On September 8, 2009, the Company filed the first amended joint plan of reorganization (the Amended Plan ) and disclosure statement with revised financial forecasts and the capital structure anticipated at emergence from bankruptcy. The Bankruptcy Court approved our disclosure statement, as it related to the Amended Plan, on September 10, 2009. Under the Amended Plan, if ultimately confirmed by the Bankruptcy Court, our total debt is expected to be reduced from approximately \$9 billion to \$2.75 billion of term loan debt, bearing an annual interest rate of LIBOR plus 800 basis points with a LIBOR floor of 3.0% and a six-year term. As a result of the expected increased interest rates for our secured bank debt, our interest expense will increase relative to the amount of outstanding debt.

As the bankruptcy process continues, the terms of the Amended Plan may be subject to further negotiation and modification. At this time, there is no assurance the Company will be able to restructure as a going concern or successfully implement the Amended Plan.



**Risks Related to Our Common Stock**

*Our restructuring will most likely result in the holders of our common stock receiving no recovery.*

Under the priority scheme established by the Bankruptcy Code, unless creditors agree otherwise in accordance with the Bankruptcy Code, pre-petition liabilities and post-petition liabilities must be satisfied in full before shareholders are entitled to receive any distribution or retain any property under a plan of reorganization. The ultimate recovery to creditors and/or stockholders, if any, will not be determined until confirmation of a plan of reorganization. No assurance can be given as to what values, if any, will be ascribed in the Chapter 11 bankruptcy proceedings to each of these constituencies or what types or amounts of distributions, if any, they would receive. If certain requirements of the Bankruptcy Code are met, a plan of reorganization can be confirmed notwithstanding its rejection by equity holders and notwithstanding the fact that equity holders do not receive or retain any property on

Table of Contents

account of their equity interests under the plan of reorganization. We do not presently believe that there will be any recovery for holders of our common stock.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**



Edgar Filing: IDEARC INC. - Form 10-Q

The following table provides information about shares acquired from employees during the third quarter of 2009 as payment of withholding taxes in connection with the vesting of restricted stock awarded to employees pursuant to the Idearc Inc. 2008 Incentive Compensation Plan and the Idearc Inc. Long Term Incentive Plan:

Period	Total Number of Shares Purchased	Average Price Paid Per Share		Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet Be Purchased Under the Plans or Programs
July 1 - July 31	389	\$	0.03		
August 1 - August 31					
September 1 - September 30	14,522	\$	0.03		
Total	14,911	\$	0.03		

**Item 3. Defaults Upon Senior Securities.**



## Edgar Filing: IDEARC INC. - Form 10-Q

Our consolidated audited financial statements for the fiscal year ending December 31, 2008 contained an explanatory paragraph regarding our ability to continue as a going concern which constituted a default under our senior secured credit facility (the Senior Credit Facility). On March 31, 2009, we failed to make scheduled payments under the Senior Credit Facility of approximately \$42 million in interest and approximately \$31 million in principal, resulting in an additional default under the Senior Credit Facility. Our voluntary filing of the bankruptcy case on March 31, 2009 constituted a default under the Senior Credit Facility, which default resulted in the commitments under the Senior Credit Facility being immediately terminated and all borrowings, with accrued interest thereon, and all other amounts owed by us, including all amounts under outstanding letters of credit, becoming immediately due and payable. In addition, the bankruptcy filing constituted an event of default under the indenture governing the Company's 8% senior unsecured notes due 2016 (the Unsecured Notes). As a result of such default, the principal amount plus accrued and unpaid interest on the Unsecured Notes became immediately due and payable. The Chapter 11 bankruptcy filings also constituted a default under our outstanding swap agreements, allowing the counterparties thereto to accelerate the payment of the termination value of the swap agreements. As of September 30, 2009, the aggregate principal amounts outstanding under the Senior Credit Facility and the termination value of the interest rate swap agreements were approximately \$6,725 million and the aggregate principal amounts outstanding under the Unsecured Notes were approximately \$2,850 million. There are multiple defaults that are continuing and uncured under the Senior Credit Facility and indenture governing the Senior Unsecured Notes.

An immediate effect of the bankruptcy filing was the imposition of the automatic stay under the Bankruptcy Code, which, with limited exceptions, enjoins the ability of creditors to (i) seek remedies to enforce their rights to commence or continue of all their collection efforts, including our lenders and note holders; (ii) the enforcement of liens against our property; and (iii) the continuation of litigation against us.

### **Item 4. Submission of Matters to a Vote of Security Holders.**



None.

**Item 5. Other Information.**





None.

Table of Contents

**Item 6. Exhibits.**

Edgar Filing: IDEARC INC. - Form 10-Q

**Exhibits:**

- 3.1 Amended and Restated Certificate of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Registration Statement on Form 10, Amendment No. 5 (File No. 001-32939), filed October 30, 2006).
- 3.2 Amended and Restated Bylaws of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K, filed April 18, 2008).
- 31.1 Certification of Scott W. Klein filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 31.2 Certification of Samuel D. Jones filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 32.1 Certification of Scott W. Klein and Samuel D. Jones filed pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).

Table of Contents

**SIGNATURES**



Edgar Filing: IDEARC INC. - Form 10-Q

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

IDEARC INC.

November 6, 2009

/s/ Scott W. Klein  
Scott W. Klein  
Chief Executive Officer  
(Principal Executive Officer)

November 6, 2009

/s/ Samuel D. Jones  
Samuel D. Jones  
Chief Financial Officer and Treasurer  
(Principal Financial and Accounting Officer)

43

---

Table of Contents

**EXHIBIT INDEX**





## Edgar Filing: IDEARC INC. - Form 10-Q

### Exhibits:

- 3.1 Amended and Restated Certificate of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Registration Statement on Form 10, Amendment No. 5 (File No. 001-32939), filed October 30, 2006).
- 3.2 Amended and Restated Bylaws of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K, filed April 18, 2008).
- 31.1 Certification of Scott W. Klein filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 31.2 Certification of Samuel D. Jones filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 32.1 Certification of Scott W. Klein and Samuel D. Jones filed pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).