PENN NATIONAL GAMING INC
Form 10-Q
May 07, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2010

OR

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

For the transition period from to

Commission file number: 0-24206

PENN NATIONAL GAMING, INC.

(Exact name of registrant as specified in its charter)

Pennsylvania	**23-2234473**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

825 Berkshire Blvd., Suite 200
Wyomissing, PA 19610
(Address of principal executive offices) (Zip Code)

610-373-2400

(Registrant s telephone number, including area code)

Not Applicable

(Former name, former address, and former fiscal year, if changed since last report)

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 x No o

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

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 x	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Title	**Outstanding as of May 3, 2010**
Common Stock, par value $.01 per share	79,361,906 (includes 592,800 shares of restricted stock)

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This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Actual results may vary materially from expectations. Although Penn National Gaming, Inc. and its subsidiaries (collectively, the Company) believe that our expectations are based on reasonable assumptions within the bounds of our knowledge of our business and operations, there can be no assurance that actual results will not differ materially from our expectations. Meaningful factors that could cause actual results to differ from expectations include, but are not limited to, risks related to the following: our ability to maintain regulatory approvals for our existing businesses and to receive regulatory approvals for our new businesses; the passage of state, federal or local legislation (including referenda) that would expand, restrict, further tax, prevent or negatively impact operations in the jurisdictions in which we do business (such as a smoking ban at any of our facilities) or in jurisdictions where we seek to do business; the activities of our competitors and the emergence of new competitors; increases in the effective rate of taxation at any of our properties or at the corporate level; delays or changes to, or cancellations of, planned capital projects at our gaming and pari-mutuel facilities or an inability to achieve the expected returns from such projects; construction factors, including delays, unexpected remediation costs, local opposition and increased cost of labor and materials; the ability to recover proceeds on significant insurance claims; our ability to identify attractive acquisition and development opportunities and to agree to terms with partners for such transactions; the costs and risks involved in the pursuit of such opportunities, and our ability to complete the acquisition or development of, and achieve the expected returns from, such opportunities; the availability and cost of financing; the maintenance of agreements with our horsemen, pari-mutuel clerks and other organized labor groups; the outcome of pending legal proceedings; the effects of local and national economic, credit, capital market, housing, and energy conditions on the economy in general and on the gaming and lodging industries in particular; changes in accounting standards; third-party relations and approvals; our dependence on key personnel; the impact of terrorism and other international hostilities; the impact of weather; and other factors as discussed in the Company s Annual Report on Form 10-K for the year ended December 31, 2009, subsequent Quarterly Reports on Form 10-Q and Current Reports on Form 8-K as filed with the SEC. The Company does not intend to update publicly any forward-looking statements except as required by law.

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PENN NATIONAL GAMING, INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Penn National Gaming, Inc. and Subsidiaries

Consolidated Balance Sheets

(in thousands, except share and per share data)

	March 31, 2010 (unaudited)	December 31, 2009
Assets		
Current assets		
Cash and cash equivalents	$ 642,507	$ 713,118
Receivables, net of allowance for doubtful accounts of $3,594 and $3,548 at March 31, 2010 and December 31, 2009, respectively	37,846	46,672
Insurance receivable	13,654	33,494
Prepaid expenses and other current assets	105,586	121,545
Deferred income taxes	20,375	23,619
Total current assets	819,968	938,448
Property and equipment, net	1,909,192	1,837,504
Other assets		
Investment in and advances to unconsolidated affiliates	38,503	26,305
Goodwill	1,378,623	1,379,961
Other intangible assets	375,294	376,954
Deferred financing fees, net of accumulated amortization of $43,125 and $39,703 at March 31, 2010 and December 31, 2009, respectively	37,507	40,889
Other assets	96,661	112,555
Total other assets	1,926,588	1,936,664
Total assets	$ 4,655,748	$ 4,712,616
Liabilities		
Current liabilities		
Current maturities of long-term debt	$ 74,640	$ 86,071
Accounts payable	23,230	19,850
Accrued expenses	83,533	110,108
Accrued interest	47,080	61,786
Accrued salaries and wages	51,188	65,608
Gaming, pari-mutuel, property, and other taxes	39,734	38,943
Insurance financing	2,537	6,752
Other current liabilities	42,184	41,138
Total current liabilities	364,126	430,256
Long-term liabilities		
Long-term debt, net of current maturities	2,228,188	2,248,706
Deferred income taxes	132,141	127,107
Noncurrent tax liabilities	36,695	46,702

Other noncurrent liabilities		8,369		7,769
Total long-term liabilities		2,405,393		2,430,284
Shareholders equity				
Penn National Gaming, Inc. and subsidiaries shareholders equity:				
Preferred stock ($.01 par value, 1,000,000 shares authorized, 12,275 and 12,500 shares issued and outstanding at March 31, 2010 and December 31, 2009, respectively)				
Common stock ($.01 par value, 200,000,000 shares authorized, 79,202,810 and 78,972,256 shares issued at March 31, 2010 and December 31, 2009, respectively)		787		786
Additional paid-in capital		1,476,153		1,480,476
Retained earnings		433,571		397,407
Accumulated other comprehensive loss		(23,708)		(26,028)
Total Penn National Gaming, Inc. and subsidiaries shareholders equity		1,886,803		1,852,641
Noncontrolling interests		(574)		(565)
Total shareholders equity		1,886,229		1,852,076
Total liabilities and shareholders equity	$	4,655,748	$	4,712,616

See accompanying notes to the consolidated financial statements.

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Penn National Gaming, Inc. and Subsidiaries

Consolidated Statements of Income

(in thousands, except per share data)

(unaudited)

	Three Months Ended March 31, 2010	Three Months Ended March 31, 2009
Revenues		
Gaming	$ 543,373	$ 559,903
Management service fee	3,194	3,033
Food, beverage and other	80,432	84,622
Gross revenues	626,999	647,558
Less promotional allowances	(34,676)	(35,332)
Net revenues	592,323	612,226
Operating expenses		
Gaming	290,861	297,562
Food, beverage and other	63,220	64,529
General and administrative	94,516	99,470
Impairment loss for replaced Lawrenceburg vessel	136	
Empress Casino Hotel fire	59	5,400
Depreciation and amortization	51,180	44,430
Total operating expenses	499,972	511,391
Income from operations	92,351	100,835
Other income (expenses)		
Interest expense	(34,292)	(31,238)
Interest income	730	3,091
Loss from unconsolidated affiliates	(1,412)	(303)
Other	(1,321)	2,092
Total other expenses	(36,295)	(26,358)
Income from operations before income taxes	56,056	74,477
Taxes on income	19,901	33,816
Net income including noncontrolling interests	36,155	40,661
Less: Net loss attributable to noncontrolling interests	(9)	
Net income attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries	$ 36,164	$ 40,661
Earnings per common share attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries:		
Basic earnings per common share	$ 0.37	$ 0.42
Diluted earnings per common share	$ 0.34	$ 0.38

See accompanying notes to the consolidated financial statements.

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Penn National Gaming, Inc. and Subsidiaries

Consolidated Statements of Changes in Shareholders Equity

(in thousands, except share data) (unaudited)

	Penn National Gaming, Inc. shareholders									
	Preferred Stock		Common Stock		Additional Paid-In	Retained	Accumulated Other Comprehensive (Loss)	Noncontrolling	Total Shareholders	Comprehensive Income
	Shares	Amount	Shares	Amount	Capital	Earnings	Income	Interests	Equity	(Loss)
Balance, December 31, 2008	12,500	$	78,148,488	$ 782	$ 1,442,829	$ 662,355	$ (48,693)	$	$ 2,057,273	
Stock option activity, including tax benefit of $327			82,892		9,496				9,496	$
Restricted stock			93,500		496				496	
Change in fair value of interest rate swap contracts, net of income taxes of $1,339							2,380		2,380	2,380
Change in fair value of corporate debt securities							1,564		1,564	1,564
Foreign currency translation adjustment							(223)		(223)	(223)
Net income						40,661			40,661	40,661
Balance, March 31, 2009	12,500	$	78,324,880	$ 782	$ 1,452,821	$ 703,016	$ (44,972)	$	$ 2,111,647	$ 44,382
Balance, December 31, 2009	12,500	$	78,972,256	$ 786	$ 1,480,476	$ 397,407	$ (26,028)	$ (565)	$ 1,852,076	
Repurchase of preferred stock	(225)				(11,200)				(11,200)	$
Stock option activity, including tax expense of $660			65,444	1	4,881				4,882	
Restricted stock			165,110		1,996				1,996	
Change in fair value of interest rate swap contracts, net of income taxes of $1,369							1,987		1,987	1,987
Change in fair value of corporate debt securities							(8)		(8)	(8)
Foreign currency translation adjustment							341		341	341
Net income (loss)						36,164		(9)	36,155	36,155
Balance, March 31, 2010	12,275	$	79,202,810	$ 787	$ 1,476,153	$ 433,571	$ (23,708)	$ (574)	$ 1,886,229	$ 38,475

See accompanying notes to the consolidated financial statements.

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Penn National Gaming, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(in thousands) (unaudited)

Three Months Ended March 31,	**2010**	**2009**
Operating activities		
Net income including noncontrolling interests	$ 36,155	$ 40,661
Adjustments to reconcile net income including noncontrolling interests to net cash provided by operating activities:		
Depreciation and amortization	51,180	44,430
Amortization of items charged to interest expense	3,422	2,975
Amortization of items charged to interest income	(113)	(874)
Loss on sale of fixed assets	64	12
Loss from unconsolidated affiliates	1,412	303
Empress Casino Hotel fire	59	4,318
Gain on accelerated payment of other long-term obligations		(1,305)
Deferred income taxes	4,782	982
Charge for stock compensation	6,384	8,485
Impairment loss for replaced Lawrenceburg vessel	136	
Decrease, net of businesses acquired		
Accounts receivable	6,654	3,828
Insurance receivable	15,019	
Prepaid expenses and other current assets	16,636	13,714
Other assets	9,590	4,275
Increase (decrease), net of businesses acquired		
Accounts payable	1,476	(3,409)
Accrued expenses	(26,167)	(26,711)
Accrued interest	(11,350)	(1,818)
Accrued salaries and wages	(14,420)	(1,454)
Gaming, pari-mutuel, property and other taxes	791	(24)
Income taxes		14,718
Other current and noncurrent liabilities	1,646	(611)
Other noncurrent tax liabilities	(9,620)	1,618
Net cash provided by operating activities	93,736	104,113
Investing activities		
Expenditures for property and equipment	(120,385)	(63,575)
Proceeds from sale of property and equipment	1,103	1,212
Proceeds from Empress Casino Hotel fire	4,821	
Investment in Kansas Entertainment	(13,550)	
Decrease in cash in escrow	10,982	
Net cash used in investing activities	(117,029)	(62,363)
Financing activities		
Proceeds from exercise of options	746	776
Repurchase of preferred stock	(11,200)	
Proceeds from issuance of long-term debt	33,925	25,919
Principal payments on long-term debt	(65,874)	(70,744)
Payments on insurance financing	(4,215)	(6,070)
Increase in deferred financing fees	(40)	
Tax impact from stock options exercised	(660)	327
Net cash used in financing activities	(47,318)	(49,792)
Net decrease in cash and cash equivalents	(70,611)	(8,042)

Cash and cash equivalents at beginning of year		713,118		746,278
Cash and cash equivalents at end of period	$	642,507	$	738,236
Supplemental disclosure				
Interest expense paid	$	43,234	$	32,943
Income taxes paid	$	7,271	$	445

See accompanying notes to the consolidated financial statements.

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Penn National Gaming, Inc. and Subsidiaries

Notes to the Consolidated Financial Statements

1. Basis of Presentation

The accompanying unaudited consolidated financial statements of Penn National Gaming, Inc. (Penn) and its subsidiaries (collectively, the Company) have been prepared in accordance with United States (U.S.) generally accepted accounting principles (GAAP) for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete consolidated financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The notes to the consolidated financial statements contained in the Annual Report on Form 10-K for the year ended December 31, 2009 should be read in conjunction with these consolidated financial statements. For purposes of comparability, certain prior year amounts have been reclassified to conform to the current year presentation. Operating results for the three months ended March 31, 2010 are not necessarily indicative of the results that may be expected for the year ending December 31, 2010.

2. Summary of Significant Accounting Policies

Revenue Recognition and Promotional Allowances

Gaming revenue is the aggregate net difference between gaming wins and losses, with liabilities recognized for funds deposited by customers before gaming play occurs, for chips and ticket-in, ticket-out coupons in the customers possession, and for accruals related to the anticipated payout of progressive jackpots. Progressive slot machines, which contain base jackpots that increase at a progressive rate based on the number of coins played, are charged to revenue as the amount of the jackpots increase.

Revenue from the management service contract for Casino Rama is based upon contracted terms and is recognized when services are performed.

Food, beverage and other revenue, including racing revenue, is recognized as services are performed. Racing revenue includes the Company s share of pari-mutuel wagering on live races after payment of amounts returned as winning wagers, its share of wagering from import and export simulcasting, and its share of wagering from its off-track wagering facilities.

Revenues are recognized net of certain sales incentives in accordance with Financial Accounting Standards Board Accounting Standards Codification (ASC) 605-50, Revenue Recognition Customer Payments and Incentives (ASC 605-50). The consensus in ASC 605-50 requires that sales incentives and points earned in point-loyalty programs be recorded as a reduction of revenue. The Company recognizes incentives related to gaming play and points earned in point-loyalty programs as a direct reduction of gaming revenue.

The retail value of accommodations, food and beverage, and other services furnished to guests without charge is included in gross revenues and then deducted as promotional allowances. The estimated cost of providing such promotional allowances is primarily included in food, beverage and other expense. The amounts included in promotional allowances for the three months ended March 31, 2010 and 2009 are as follows:

	Three Months Ended March 31, 2010	2009
	(in thousands)	
Rooms	$ 5,970	$ 5,324
Food and beverage	26,104	27,285
Other	2,602	2,723
Total promotional allowances	$ 34,676	$ 35,332

The estimated cost of providing such complimentary services for the three months ended March 31, 2010 and 2009 are as follows:

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	Three Months Ended March 31, 2010		2009
	(in thousands)		
Rooms	$ 2,284	$	2,207
Food and beverage	19,194		18,573
Other	1,729		1,504
Total cost of complimentary services	$ 23,207	$	22,284

Earnings Per Share

The Company calculates earnings per share (EPS) in accordance with ASC 260, Earnings Per Share (ASC 260). Basic EPS is computed by dividing net income applicable to common stock, excluding net income attributable to noncontrolling interests, by the weighted-average number of common shares outstanding during the period. Diluted EPS reflects the additional dilution for all potentially-dilutive securities such as stock options.

In the fourth quarter of 2008, the Company issued 12,500 shares of Series B Redeemable Preferred Stock (the Preferred Stock), which the Company determined qualified as a participating security as defined in ASC 260. Under ASC 260, a security is considered a participating security if the security may participate in undistributed earnings with common stock, whether that participation is conditioned upon the occurrence of a specified event or not. In accordance with ASC 260, a company is required to use the two-class method when computing EPS when a company has a security that qualifies as a participating security. The two-class method is an earnings allocation formula that determines EPS for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. A participating security is included in the computation of basic EPS using the two-class method. Under the two-class method, basic EPS for the Company s Common Stock is computed by dividing net income attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries applicable to common stock by the weighted-average common shares outstanding during the period. Diluted EPS for the Company s Common Stock is computed using the more dilutive of the two-class method or the if-converted method. During the three months ended March 31, 2010, the Company repurchased 225 shares of Preferred Stock for $11.2 million.

The following table sets forth the allocation of net income attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries for the three months ended March 31, 2010 and 2009 under the two-class method:

	Three Months Ended March 31, 2010		2009
	(in thousands)		
Net income attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries	$ 36,164	$	40,661
Net income attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries applicable to preferred stock	6,931		7,864
Net income attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries applicable to common stock	$ 29,233	$	32,797

The following table reconciles the weighted-average common shares outstanding used in the calculation of basic EPS to the weighted-average common shares outstanding used in the calculation of diluted EPS for the three months ended March 31, 2010 and 2009:

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	Three Months Ended March 31, 2010	2009
	(in thousands)	
Determination of shares:		
Weighted-average common shares outstanding	78,563	77,813
Assumed conversion of dilutive stock options	741	943
Assumed conversion of preferred stock	27,733	27,778
Diluted weighted-average common shares outstanding	107,037	106,534

Reflecting the issuance of the Preferred Stock and the repurchase of 225 shares of Preferred Stock during the three months ended March 31, 2010, the Company is required to adjust its diluted weighted-average common shares outstanding for the purpose of calculating diluted EPS as follows: 1) when the price of the Company s Common Stock is less than $45, the diluted weighted-average common shares outstanding is increased by 27,277,778 shares (regardless of how much the stock price is below $45); 2) when the price of the Company s Common Stock is between $45 and $67, the diluted weighted-average common shares outstanding is increased by an amount which can be calculated by dividing $1.23 billion (face value) by the current price per share of the Company s Common Stock, which will result in an increase in the diluted weighted-average common shares outstanding of between 18,320,896 shares and 27,277,778 shares; and 3) when the price of the Company s Common Stock is above $67, the diluted weighted-average common shares outstanding is increased by 18,320,896 shares (regardless of how much the stock price exceeds $67).

Options to purchase 10,167,592 shares and 8,759,082 shares were outstanding during the three months ended March 31, 2010 and 2009, respectively, but were not included in the computation of diluted EPS because they are antidilutive.

The following table presents the calculation of basic and diluted EPS for the Company s Common Stock:

	Three Months Ended March 31, 2010	2009
	(in thousands, except per share data)	
Calculation of basic EPS attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries:		
Net income attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries applicable to common stock	$ 29,233	$ 32,797
Weighted-average common shares outstanding	78,563	77,813
Basic EPS	$ 0.37	$ 0.42
Calculation of diluted EPS attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries:		
Net income attributable to the shareholders of Penn National Gaming, Inc. and subsidiaries	$ 36,164	$ 40,661
Diluted weighted-average common shares outstanding	107,037	106,534
Diluted EPS	$ 0.34	$ 0.38

Stock-Based Compensation

The Company accounts for stock compensation under ASC 718, Compensation-Stock Compensation, which requires the Company to expense the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. This expense must be recognized ratably over the requisite service period following the date of grant.

The fair value for stock options was estimated at the date of grant using the Black-Scholes option-pricing model, which requires management to make certain assumptions. The risk-free interest rate was based on the U.S. Treasury spot rate with a remaining term equal to the expected life assumed at the date of grant. Expected volatility was estimated based on the historical volatility of the Company s stock price over a period of 5.32 years, in order to match the expected life of the options at the grant date. There is no expected dividend yield since the Company has not paid any cash dividends on its Common Stock since its initial public offering in May 1994 and since the Company intends to retain all of its earnings to finance the development of its business for the foreseeable future. The weighted-average expected life was based on the

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contractual term of the stock option and expected employee exercise dates, which was based on the historical and expected exercise behavior of the Company s employees. Forfeitures are estimated at the date of grant based on historical experience. The following are the weighted-average assumptions used in the Black-Scholes option-pricing model at March 31, 2010 and 2009:

Three Months Ended March 31,	2010	2009
Risk-free interest rate	2.80%	1.61%
Expected volatility	49.68%	45.56%
Dividend yield		
Weighted-average expected life (years)	5.32	5.36
Forfeiture rate	5.00%	4.00%

Accounting for Derivatives and Hedging Activities

The Company uses fixed and variable-rate debt to finance its operations. Both funding sources have associated risks and opportunities, such as interest rate exposure, and the Company s risk management policy permits the use of derivatives to manage this exposure. The Company does not hold or issue derivative financial instruments for trading or speculative purposes. Thus, uses of derivatives are strictly limited to hedging and risk management purposes in connection with managing interest rate exposure. Acceptable derivatives for this purpose include interest rate swap contracts, futures, options, caps, and similar instruments.

When using derivatives, the Company s intent is to apply special hedge accounting, which is conditional upon satisfying specific documentation and performance criteria. In particular, the underlying hedged item must expose the Company to risks associated with market fluctuations and the instrument used as the hedging derivative must generate offsetting effects in prescribed magnitudes. If these criteria are not met, a change in the market value of the financial instrument and all associated settlements would be recognized as gains or losses in the period of change.

Currently, the Company has a number of interest rate swap contracts in place. These contracts serve to mitigate income volatility for a portion of its variable-rate funding. Swap contract coverage extends out through 2011. In effect, these swap contracts synthetically convert the portion of variable-rate debt being hedged to the equivalent of fixed-rate funding. Under the terms of the swap contracts, the Company receives cash flows from the swap contract counterparties to offset the benchmark interest rate component of variable interest payments on the hedged financings, in exchange for paying cash flows based on the swap contracts fixed rates. These two respective obligations are net-settled, periodically. The Company accounts for these swap contracts as cash flow hedges, which requires determining a division of hedge results deemed effective and deemed ineffective. However, most of the Company s hedges were designed in such a way so as to perfectly offset specifically-defined interest payments, such that no ineffectiveness has occurred nor would any ineffectiveness occur, as long as the forecasted cash flows of the designated hedged items and the associated swap contracts remain unchanged.

The fair value of the Company s interest rate swap contracts is measured as the present value of all expected future cash flows based on the LIBOR-based swap yield curve as of the date of the valuation, subject to a credit adjustment to the LIBOR-based yield curve s implied discount rates. The credit adjustment reflects the Company s best estimate as to the Company s credit quality at March 31, 2010.

Under cash flow hedge accounting, effective derivative results are initially recorded in other comprehensive income (OCI) and later reclassified to earnings, coinciding with the income recognition relating to the variable interest payments being hedged (i.e., when the interest expense on the variable-rate liability is recorded in earnings). Any hedge ineffectiveness (which represents the amount by which hedge results exceed the variability in the cash flows of the forecasted transaction due to the risk being hedged) is recorded in current period earnings.

Under cash flow hedge accounting, derivatives are included in the consolidated balance sheets as assets or liabilities at fair value. The interest rate swap contract liabilities are included in accrued interest within the consolidated balance sheets at March 31, 2010 and December 31, 2009.

During the three months ended March 31, 2010, the Company had certain derivative instruments that were not designated to qualify for hedge accounting. The periodic change in the mark-to-market of these derivative instruments is recorded in current period earnings.

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Credit risk relating to derivative counterparties is mitigated by using multiple, highly-rated counterparties, and the credit quality of each is monitored on an ongoing basis.

3. New Accounting Pronouncements

In April 2010, the Financial Accounting Standards Board (the FASB) issued guidance on accruing for jackpot liabilities. The guidance clarifies that an entity should not accrue jackpot liabilities (or portions thereof) before a jackpot is won if the entity can avoid paying that jackpot. Jackpots should be accrued and charged to revenue when an entity has the obligation to pay the jackpot. This guidance applies to both base jackpots and the incremental portion of progressive jackpots. However, the guidance is expected to only affect the accounting for base jackpots, as the guidance uses the same principle that is currently applied by the Company to the incremental portion of progressive jackpots. The guidance is effective for fiscal years, and interim periods within those fiscal years, beginning on or after December 15, 2010. This guidance should be applied by recording a cumulative-effect adjustment to opening retained earnings in the period of adoption. The Company is currently determining the impact of this guidance on its consolidated financial statements.

In February 2010, the FASB issued amended guidance on subsequent events. The amended guidance removes the requirement for U.S. Securities and Exchange Commission filers to disclose the date through which subsequent events have been evaluated. The amended guidance is effective upon issuance, except for the use of the issued date for conduit debt obligors. The Company adopted the amended guidance upon issuance, as required. The adoption of the amended guidance did not have a material impact on the Company s consolidated financial statements.

In January 2010, the FASB issued guidance to improve disclosures about fair value measurements. The guidance provides amendments to require new disclosures regarding transfers in and out of Levels 1 and 2 of the fair value measurement hierarchy, and activity in Level 3, and to clarify existing disclosures regarding the level of disaggregation, inputs and valuation techniques. The guidance is effective for interim and annual reporting periods beginning after December 15, 2009, except for the new disclosures regarding purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements, which are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years. The Company adopted the guidance, except for the new disclosures regarding purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements, as of January 1, 2010, as required. The January 1, 2010 adoption did not have a material impact on the Company s consolidated financial statements. The Company is currently determining the impact of the new disclosures regarding purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements on its consolidated financial statements.

In June 2009, the FASB issued amended guidance for variable interest entities. The objective of the amended guidance is to improve financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. The amended guidance is effective as of the beginning of each reporting entity s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited. The Company adopted the amended guidance as of January 1, 2010, as required. The amended guidance did not have a material impact on the Company s consolidated financial statements. In February 2010, the FASB deferred the effective date of the amendments in this guidance for a reporting entity s interest in certain entities. The deferral did not have an impact on the Company s consolidated financial statements.

4. Investment In and Advances to Unconsolidated Affiliates

Investment in and advances to unconsolidated affiliates that are 50% owned, which primarily include the Company s investments in Kansas Entertainment, LLC (Kansas Entertainment) and Freehold Raceway, are accounted for under the equity method.

In December 2009, Kansas Entertainment was selected by the Kansas Lottery Gaming Facility Review Board to develop and operate a facility in the North East Gaming Zone in Wyandotte County, Kansas, and in February 2010, Kansas Entertainment received the final approval under the Kansas Expanded Lottery Act, along with its gaming license from the Kansas Racing and Gaming Commission, to proceed with the development of a Hollywood-themed destination facility overlooking Turn 2 at Kansas Speedway.

The Company s investment in Kansas Entertainment consists of the Company s portion of the privilege fee paid to the Kansas Lottery Commission in conjunction with its application, its portion of capital expenditures spent to develop the proposed facility, and its share of Kansas Entertainment s losses. The Company s share of losses in Kansas Entertainment was $1.1 million for the three months ended March 31, 2010, which is also included in loss from unconsolidated affiliates within the consolidated statement of income.

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The Company determined that Kansas Entertainment qualified as a variable interest entity at March 31, 2010. The Company did not consolidate its investment in Kansas Entertainment at, and for the three months ended March 31, 2010, as the Company determined that it did not qualify as the primary beneficiary of Kansas Entertainment at, and for the three months ended March 31, 2010, primarily as it did not have the ability to direct the activities of Kansas Entertainment that most significantly impacted Kansas Entertainment s economic performance without the input of its partner in Kansas Entertainment, International Speedway Corporation (International Speedway). In addition, the Company determined that International Speedway had substantive participating rights in Kansas Entertainment at, and for the three months ended March 31, 2010.

The $410 million facility, inclusive of licensing fees, is expected to feature a 100,000 square foot casino with capacity for 2,300 slot machines, 61 table games and 25 poker tables, a 1,500 parking structure, as well as a variety of dining and entertainment amenities. The Company, along with International Speedway, will share equally the cost of developing and constructing the proposed facility, and intend to jointly seek third party financing for the project. The Company estimates that its share of the project will be approximately $155 million.

5. Property and Equipment

Property and equipment, net, consists of the following:

	March 31, 2010	December 31, 2009
	(in thousands)	
Land and improvements	$ 306,965	$ 239,933
Building and improvements	1,435,540	1,433,611
Furniture, fixtures, and equipment	868,251	849,071
Leasehold improvements	17,215	17,204
Construction in progress	78,139	47,299
Total property and equipment	2,706,110	2,587,118
Less accumulated depreciation	(796,918)	(749,614)
Property and equipment, net	$ 1,909,192	$ 1,837,504

Depreciation expense, for property and equipment, totaled $49.5 million and $42.7 million for the three months ended March 31, 2010 and 2009, respectively. Interest capitalized in connection with major construction projects was $1.1 million and $2.9 million for the three months ended March 31, 2010 and 2009, respectively.

6. Goodwill and Other Intangible Assets

A reconciliation of goodwill and accumulated goodwill impairment losses is as follows (in thousands):

Balance at December 31, 2009:

Goodwill	$	2,024,963
Accumulated goodwill impairment losses		(645,002)
Goodwill, net	$	1,379,961
Goodwill acquired during the year		
Goodwill impairment losses		
Other		(1,338)
Balance at March 31, 2010:		
Goodwill	$	2,023,625
Accumulated goodwill impairment losses		(645,002)
Goodwill, net	$	1,378,623

The table below presents the gross carrying value, accumulated amortization, and net book value of each major class of intangible asset at March 31, 2010 and December 31, 2009:

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	March 31, 2010			December 31, 2009		
	(in thousands)					
	Gross Carrying Value	Accumulated Amortization	Net Book Value	Gross Carrying Value	Accumulated Amortization	Net Book Value
Indefinite-life intangible assets	$ 368,886	$	$ 368,886	$ 368,886	$	$ 368,886
Other intangible assets	49,396	42,988	6,408	49,396	41,328	8,068
Total	$ 418,282	$ 42,988	$ 375,294	$ 418,282	$ 41,328	$ 376,954

The Company s intangible asset amortization expense was $1.7 million for each of the three months ended March 31, 2010 and 2009.

The following table presents expected intangible asset amortization expense based on existing intangible assets at March 31, 2010 (in thousands):

2010 (9 months)	$ 4,113
2011	2,096
2012	199
Total	$ 6,408

7. Investment in Corporate Securities

During the year ended December 31, 2008, the Company made a $47.3 million investment in the corporate debt securities of other gaming companies. During the year ended December 31, 2009, the Company sold $42.2 million of this investment. The remaining investment, which the Company is treating as available-for-sale securities, is included in other assets within the consolidated balance sheets at March 31, 2010 and December 31, 2009.

During the three months ended March 31, 2010 and 2009, the Company recorded an $8,000 unrealized loss and an $1.6 million unrealized gain, respectively, in OCI for this investment. The change in the fair value also reflects the original issue discount amortization, which was $0.1 million and $0.8 million for the three months ended March 31, 2010 and 2009, respectively.

The following is a schedule of the contractual maturities of the Company s investment in corporate securities at March 31, 2010 (in thousands):

Within one year	$
1-3 years	4,655
Total	$ 4,655

8. Long-term Debt

Long-term debt, net of current maturities, is as follows:

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	March 31, 2010	December 31, 2009
	(in thousands)	
Senior secured credit facility	$ 1,723,673	$ 1,755,602
$250 million 6 ¾% senior subordinated notes	250,000	250,000
$325 million 8 ¾% senior subordinated notes	325,000	325,000
Capital leases	4,155	4,175
	2,302,828	2,334,777
Less current maturities of long-term debt	(74,640)	(86,071)
	$ 2,228,188	$ 2,248,706

The following is a schedule of future minimum repayments of long-term debt as of March 31, 2010 (in thousands):

Within one year	$ 74,640
1-3 years	1,651,288
3-5 years	250,175
Over 5 years	326,725
Total minimum payments	$ 2,302,828

At March 31, 2010, the Company was contingently obligated under letters of credit issued pursuant to the senior secured credit facility with face amounts aggregating $26.5 million.

Senior Secured Credit Facility

The senior secured credit facility historically consisted of three credit facilities comprised of a $750 million revolving credit facility with a maturity date of October 3, 2010, a $325 million Term Loan A Facility with a maturity date of October 3, 2011 and a $1.65 billion Term Loan B Facility with a maturity date of October 3, 2012. In September 2009, the Company amended its senior secured credit facility, in order to increase the borrowing capacity and to extend the term under the revolving credit facility portion of the senior secured credit facility. Under the new revolving credit facility, two tranches were created, one for those participants who agreed to extend and one for those that did not extend. Tranche A Revolving Loans consist of available borrowings of $359.4 million, which are due on the original maturity date of October 3, 2010, and Tranche B Revolving Loans consist of available borrowings of $640.6 million, which are due on July 3, 2012, for a total borrowing capacity of $1 billion.

As of March 31, 2010, $205.6 million was drawn under the revolving credit facility and $1,518.1 million was outstanding under the Term Loan B Facility, for a total of $1,723.7 million. During the year ended December 31, 2009, all of the outstanding borrowings under the Term Loan A Facility were repaid.

Interest Rate Swap Contracts

In accordance with the terms of its senior secured credit facility, the Company was required to enter into fixed-rate debt or interest rate swap agreements in an amount equal to 50% of the Company s consolidated indebtedness, excluding the revolving credit facility, within 100 days of the closing date of the senior secured credit facility.

The effect of derivative instruments on the consolidated statement of income for the three months ended March 31, 2010 was as follows (in thousands):

Derivatives in a Cash Flow Hedging Relationship	**Gain (Loss) Recognized in OCI on Derivative (Effective Portion)**		**Location of Gain (Loss) Reclassified from AOCI into Income (Effective Portion)**	**Gain (Loss) Reclassified from AOCI into Income (Effective Portion)**		**Location of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)**	**Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)**	
Interest rate swap contracts	$	(7,386)	Interest expense	$	(6,496)	None	$	
Total	$	(7,386)		$	(6,496)		$	

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Derivatives Not Designated as Hedging Instruments	Location of Gain (Loss) Recognized in Income on Derivative	Gain (Loss) Recognized in Income on Derivative	
Interest rate swap contracts	Interest expense	$	(34)
Total		$	(34)

The effect of derivative instruments on the consolidated statement of income for the three months ended March 31, 2009 was as follows (in thousands):

Derivatives in a Cash Flow Hedging Relationship	Gain (Loss) Recognized in OCI on Derivative (Effective Portion)	Location of Gain (Loss) Reclassified from AOCI into Income	Gain (Loss) Reclassified from AOCI into Income	Location of Gain (Loss) Recognized in Income on	Gain (Loss) Recognized in Income on