

COSTAR GROUP INC
Form 10-K
February 26, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K

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

For the fiscal year ended December 31, 2014

Commission file number 0-24531

CoStar Group, Inc.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or
organization)

52-2091509
(I.R.S. Employer Identification No.)

1331 L Street, NW, Washington, DC 20005
(Address of principal executive offices) (zip code)

(202) 346-6500
(Registrant's telephone number, including area code)

(877) 739-0486
(Registrant's facsimile number, including area code)

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, \$.01 par value	NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act:
None

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

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

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was

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required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Securities Exchange Act of 1934.

Large accelerated filer
Non-accelerated filer

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

Based on the closing price of the common stock on June 30, 2014 on the Nasdaq Stock Market, Nasdaq Global Select Market, the aggregate market value of registrant's common stock held by non-affiliates of the registrant was approximately \$4.9 billion.

As of February 20, 2015, there were 32,311,866 shares of the registrant's common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement, which is expected to be filed with the Securities and Exchange Commission within 120 days after the end of the registrant's fiscal year ended December 31, 2014, are incorporated by reference into Part III of this Report.

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PART I

Item 1. Business

In this report, the words “we,” “our,” “us,” “CoStar” or the “Company” refer to CoStar Group, Inc. and its direct and indirect wholly owned subsidiaries. This report also refers to our websites, but information contained on those sites is not part of this report.

CoStar Group, Inc., a Delaware corporation, founded in 1987, is the number one provider of information, analytics and online marketplaces to the commercial real estate industry in the United States (“U.S.”) and United Kingdom (“U.K.”) based on the fact that we offer the most comprehensive commercial real estate database available; have the largest research department in the industry; own and operate the leading online marketplaces for commercial real estate in the U.S. based on the number of unique visitors per month; provide more information, analytics and marketing services than any of our competitors and believe that we generate more revenues than any of our competitors. We created and compiled our standardized platform of information, analytics and online marketplace services where members of the commercial real estate and related business community can continuously interact and facilitate transactions by efficiently exchanging accurate and standardized commercial real estate information. Our service offerings span all commercial property types, including office, retail, industrial, multifamily, commercial land, mixed-use properties and hospitality. We manage our business geographically in two operating segments, with our primary areas of measurement and decision-making being North America, which includes the U.S. and Canada, and International, which includes the U.K. and France.

Strategy

Since our founding, our strategy has been to provide commercial real estate professionals with critical knowledge to explore and complete transactions by offering the most comprehensive, timely and standardized information on U.S. commercial real estate. As we have grown and further developed our plans, we have expanded our services for commercial real estate information, analytics and online marketplaces in an effort to continue to meet the needs of this industry as it grows and evolves. We have also extended our offering of comprehensive commercial real estate information to include London and other parts of the U.K., Toronto, Canada, and parts of France, through acquisitions and internal growth and development. Information about CoStar’s revenues from, and long-lived assets and total assets located in, foreign countries is included in Notes 2 and 12 of the Notes to Consolidated Financial Statements included in this Annual Report on Form 10-K. The revenues; net income before interest, income taxes, depreciation and amortization (“EBITDA”); and total assets and liabilities for each of our segments are set forth in Note 12 to our consolidated financial statements. Information about risks associated with our foreign operations is included in “Item 1A. Risk Factors” and “Item 7A. Quantitative and Qualitative Disclosures about Market Risk.”

We deliver our commercial real estate content to our U.S. customers primarily via an integrated suite of online service offerings that includes information about space available for lease, comparable sales information, information about properties for sale, tenant information, internet marketing services, analytical capabilities, information for clients’ websites, information about industry professionals and their business relationships, data integration and industry news. We also operate complementary online marketplaces for commercial real estate listings and apartment rentals.

LoopNet, our subsidiary, operates an online marketplace that enables commercial property owners, landlords, and real estate agents working on their behalf to list properties for sale or for lease and to submit detailed information about property listings. Commercial real estate agents, buyers and tenants also use LoopNet's online marketplace to search for available property listings that meet their criteria.

Apartments, LLC (doing business as Apartments.com), our subsidiary, operates an online apartment marketplace for renters that matches apartment seekers with apartment homes and provides property managers and owners a platform for marketing their properties. Apartments.com draws on CoStar's multifamily database, which contains detailed information on apartment properties, and a research effort to document the apartment industry in the U.S. CoStar designed the new Apartments.com site, which was launched in February 2015, around the needs of the renter in order to drive traffic to the site and attract advertisers who prefer to advertise on heavily trafficked apartment websites. The newly launched site provides a comprehensive selection of rentals, information on actual rental availabilities and rents, and in-depth data on neighborhoods, including restaurants, nightlife, history, schools and other important facts. To help renters find the information that meets their needs, the new site also offers innovative search tools.

We provide market research and analysis for commercial real estate investors and lenders via our CoStar Portfolio Strategy and CoStar Market Analytics service offerings, portfolio and debt analysis, management and reporting capabilities through our CoStar Investment Analysis and CoStar Risk Analytics service offerings; and real estate and lease management solutions, including lease administration and abstraction services, through our CoStar Real Estate Manager service offerings. We have created and are continually improving our standardized platform of information, analytics and online marketplaces where members of the commercial real estate and related business community can continuously interact and facilitate transactions by efficiently exchanging accurate and standardized commercial real estate information.

Our standardized platform includes the most comprehensive proprietary database in the industry; the largest research department in the industry; proprietary data collection, information management and quality control systems; a large in-house product development team; a broad suite of web-based information, analytics and online marketplaces; a large team of analysts and economists; and a large base of clients. Our database has been developed and enhanced for more than 27 years by a research department that makes thousands of daily database updates. In addition to our internal efforts to grow the database, we have obtained and assimilated over 90 proprietary databases.

We have five flagship brands - CoStar, LoopNet, Apartments.com, BizBuySell and LandsofAmerica. Our subscription-based information services consist primarily of CoStar Suite™ services. CoStar Suite is sold as a platform of service offerings consisting of CoStar Property Professional®, CoStar COMPS Professional® and CoStar Tenant® and through our mobile application, CoStarGo®. CoStar Suite is our primary service offering in our North America and International operating segments. Prior to the third quarter of 2014, FOCUS™ was our primary service offering in our International operating segment. We introduced CoStar Suite in the U.K. in the fourth quarter of 2012 and no longer offered FOCUS to new clients beginning in 2013.

Our subscription-based services consist primarily of similar services offered over the Internet to commercial real estate industry and related professionals. Our services are typically distributed to our clients under subscription-based license agreements that renew automatically, a majority of which have a term of one year. Upon renewal, many of the subscription contract rates may change in accordance with contract provisions or as a result of contract renegotiations. To encourage clients to use our services regularly, we generally charge a fixed monthly amount for our subscription-based information services rather than charging fees based on actual system usage. Contract rates are generally based on the number of sites, number of users, organization size, the client's business focus, geography and the number and types of services to which a client subscribes. Our subscription clients generally pay contract fees on a monthly basis, but in some cases may pay us on a quarterly or annual basis.

Expansion and Growth

Acquisitions

We have continually expanded the geographical coverage of our existing information services and developed new information, analytics and online marketplace services. In addition to internal growth, we have grown our business through strategic acquisitions.

Historically, our expansion includes the acquisitions of Chicago ReSource in Chicago in 1996 and New Market Systems in San Francisco in 1997. In August 1998, we expanded into the Houston region through the acquisition of Houston-based real estate information provider C Data Services. In January 1999, we expanded further into the Midwest and Florida by acquiring LeaseTrend and into Atlanta and Dallas/Fort Worth by acquiring Jamison Research. In February 2000, we acquired COMPS.COM, a San Diego-based provider of commercial real estate information. In November 2000, we acquired First Image Technologies, a California-based provider of commercial real estate software. In September 2002, we expanded further into Portland, Oregon through the acquisition of certain assets of

Napier Realty Advisors (doing business as REAL-NET). In January 2003, we established a base in the U.K. with our acquisition of London-based FOCUS Information Limited. In May 2004, we expanded into Tennessee through the acquisition of Peer Market Research, and in June 2004, we extended our coverage of the U.K. through the acquisition of Scottish Property Network. In September 2004, we strengthened our position in Denver, Colorado through the acquisition of substantially all of the assets of RealComp, a local comparable sales information provider.

In January 2005, we acquired National Research Bureau, a Connecticut-based provider of U.S. shopping center information. In December 2006, our U.K. subsidiary, CoStar Limited, acquired Grecam S.A.S. (“Grecam”), a provider of commercial property information and market-level surveys, studies and consulting services located in Paris, France. In February 2007, CoStar Limited also acquired Property Investment Exchange Limited (“Propex”), a provider of commercial property information and operator of an electronic platform that facilitates the exchange of investment property located in London, England. In April 2008, we acquired the assets of First CLS (doing business as the Dorey Companies and DoreyPRO), an Atlanta-based provider of local commercial real estate information. In July 2009, we acquired Massachusetts-based CoStar Portfolio Strategy (formerly known as Property and Portfolio Research), a provider of real estate analysis, market forecasts and credit risk analytics to the commercial real estate industry, and its wholly owned U.K. subsidiary Property and Portfolio Research Ltd., and in October 2009, we acquired Massachusetts-based CoStar Investment Analysis (formerly known as Resolve Technology), a provider of business intelligence and portfolio management software serving the institutional real estate investment industry. In October 2011, we acquired CoStar Real Estate Manager (formerly known as Virtual Premise), a Software as a Service, or on-demand software provider of real estate and lease management solutions located in Atlanta, Georgia. In April 2012, we completed the acquisition of LoopNet, an online marketplace that enables property owners, landlords, and commercial real estate agents working on their behalf to list properties for sale or for lease and to submit detailed information about property listings. More recently, on April 1, 2014, we purchased certain assets and assumed certain liabilities related to the Apartments.com business (collectively, the “Apartments.com Business”), a national online apartment rentals resource for renters, property managers and owners, from Classified Ventures, LLC (“CV”).

Expansion and Development

We expect to continue our software development efforts to improve existing services, introduce new services, integrate products and services, cross-sell existing services, and expand and develop supporting technologies for our research, sales and marketing organizations. We are committed to supporting and improving our information, analytics and online marketplace solutions.

In October 2013, we introduced technology enhancements to CoStar Suite, our platform of service offerings consisting of CoStar Property Professional, CoStar COMPS Professional and CoStar Tenant. The enhancements improve CoStar Suite's user interface, search functionality and analytic capabilities. For example, the CoStar Multifamily® information search feature allows users to access our extensive multifamily property database. In addition, CoStar Lease Analysis™, an integrated workflow tool, provides users a simple way to produce understandable cash flows for any proposed or existing lease. We plan to continue our software development efforts to enhance our new Lease Analysis workflow tool and to develop other potential lease comparable services in 2015.

In October 2013, we also released CoStarGo® 2.0, the next generation of our mobile application, which was launched in the U.S. on August 15, 2011 and introduced in the U.K. on November 5, 2012. CoStarGo is our iPad application that integrates and provides CoStar Suite subscribers mobile access to our comprehensive property, tenant and comparable sales information. CoStarGo 2.0 adds powerful analytic capabilities to our comprehensive mobile solution.

In 2014, we introduced enhancements to our flagship marketing platform, LoopNet.com. For example, we added a targeted advertising service that allows brokers or firms to purchase advertisements based on geographic and property type criteria. Additionally, we introduced ProVideo, a service that enables owners and brokers to enhance their LoopNet listings with high quality videos of interior spaces, amenities and exterior features.

In February 2015, as a result of our product development efforts, we launched a new Apartments.com website with a cleaner look, information about actual rental availabilities, rents and other fees, and better search functionality. In conjunction with the launch, we plan to embark on a wide-scale marketing campaign commencing during the first

quarter of 2015 and running throughout the remainder of 2015 to generate brand awareness and site traffic for Apartments.com, including an incremental investment of \$75.0 million above Apartments.com's 2014 annualized marketing spend since the close of the acquisition of the Apartments.com Business. The marketing campaign is expected to feature television and radio advertising, online/digital advertising, social media and out-of-home ads and will be reinforced by Search Engine Marketing.

We continue to integrate, develop and cross-sell the services offered by the businesses we have acquired, including Apartments.com and LoopNet. We evaluate potential changes to our service offerings from time to time in order to better align the services we offer with customers' needs. Further, in some cases, when integrating and coordinating our services and assessing industry and client needs, we may decide to combine, shift focus from, de-emphasize, phase out, or eliminate a service that, among other things, overlaps or is redundant with other services we offer. For example, we are currently assessing whether to transition the LoopNet marketplace to a pure marketing site for commercial real estate where, eventually, all listings would be paid and users could search the site for free.

To more fully integrate and connect our services and, ultimately, to provide improved access to our resources, we launched a new brand identity in May 2014. The new branding is designed to unite our flagship brands - CoStar, LoopNet, Apartments.com, BizBuySell and LandsofAmerica - with a modern, cohesive look that will enhance customers' access to the full breadth of our information, analytics and marketplace solutions. The resulting streamlined network of platforms is expected to improve the customer experience and make it easier for customers to find the most useful tools for their commercial real estate information, analytic and marketplace needs. The new brand identity was unveiled in connection with the launch of our new corporate website and newly designed website interfaces for CoStar, LoopNet and Apartments.com. Our new website interfaces provide streamlined navigation and search functions for visitors and enable customers to quickly access our market-leading services.

Internationally, we continue to integrate our operations more fully with those in the U.S. Similar to our North America operating segment, we intend to continue to upgrade our international platform of services and expand the coverage of our service offerings within our International segment. To further those initiatives, we introduced CoStar Suite in the U.K. during the fourth quarter of 2012 and no longer offered FOCUS to new clients beginning in 2013. CoStar Suite is sold as a consistent international platform of service offerings consisting of CoStar Property Professional, CoStar COMPS Professional and CoStar Tenant and through the Company's mobile application, CoStarGo. CoStarGo 2.0 was released in the U.K. in October 2013 simultaneous with its release in the U.S. Additionally, we upgraded our back-end research operations, fulfillment and Customer Relationship Management systems to support these new U.K. services. The financial performance of our International operating segment continues to improve. During the twelve months ended December 31, 2014, International EBITDA increased to a positive amount as a result of increased revenue and decreased operating expenses as compared to the twelve months ended December 31, 2013. See the "Non-GAAP Financial Measures" section included in this Annual Report on Form 10-K for further details on the non-GAAP financial measures.

We recently expanded the geographic reach of our North America services. In 2014, we began offering our services in Toronto, Canada. Building on our experience in Toronto, we plan to expand our research into additional Canadian cities. We believe that our integration efforts and continued investments in our services, including expansion of our existing service offerings, have created a platform for long-term revenue growth. We expect these investments to result in further penetration of our subscription-based information services and the successful cross-selling of our services to customers in existing markets.

We have invested in the expansion and development of our field sales force to support the growth and expansion of our company in North America and internationally. We plan to continue to invest in, evaluate and strategically position our sales force as the Company continues to develop and grow. We are also investing in our research capacity to support continued growth of our information and analytics offerings, to support the Apartments.com Business and to expand into additional Canadian markets.

In support of our continued expansion and development, during June 2014, we completed a public equity offering of 3,450,000 shares of common stock for \$160.00 per share, resulting in net proceeds to the Company of approximately \$529.4 million. We intend to use the net proceeds from the public equity offering to fund all or a portion of the costs of any strategic acquisitions we decide to pursue in the future, to finance the growth of our business and for working capital and other general corporate purposes.

Industry Overview

The market for commercial real estate information and analysis is vast based on the variety, volume and value of transactions related to commercial real estate. Each transaction has multiple participants and multiple information requirements, and in order to facilitate transactions, industry participants must have extensive, accurate and current information and analysis. Members of the commercial real estate and related business community require daily access

to current data such as space availability, properties for sale, rental units available, rental rates, vacancy rates, tenant movements, sales comparables, supply, new construction, absorption rates and other important market developments to carry out their businesses effectively. Market research (including historical and forecast conditions) and applied analytics have also become instrumental to the success of commercial real estate industry participants operating in the current economic environment. There is a strong need for an efficient marketplace, where commercial real estate professionals can exchange information, evaluate opportunities using standardized data and interpretive analyses, and interact with each other on a continuous basis.

A large number of parties involved in the commercial real estate and related business community make use of the services we provide in order to obtain information they need to conduct their businesses, including:

- Sales and leasing brokers
- Property owners
- Property managers
- Design and construction professionals
- Real estate developers
- Real estate investment trust managers
- Investment bankers
- Commercial bankers
- Mortgage bankers
- Mortgage brokers
- Retailers
- Government agencies
- Mortgage-backed security issuers
- Appraisers
- Pension fund managers
- Reporters
- Tenant vendors
- Building services vendors
- Communications providers
- Insurance companies' managers
- Institutional advisors
- Investors and asset managers

The commercial real estate and related business community generally has operated in an inefficient marketplace because of the fragmented approach to gathering and exchanging information within the marketplace. Various organizations, including hundreds of brokerage firms, directory publishers and local research companies, collect data on specific markets and develop software to analyze the information they have independently gathered. This highly fragmented methodology has resulted in duplication of effort in the collection and analysis of information, excessive internal cost and the creation of non-standardized data containing varying degrees of accuracy and comprehensiveness, resulting in a formidable information gap.

The creation of a standardized information platform for commercial real estate requires an infrastructure including a standardized database, accurate and comprehensive research capabilities, experienced analysts, easy to use technology and intensive participant interaction. By combining our extensive database, approximately 1,481 researchers and outside contractors, our experienced team of analysts and economists, technological expertise and broad customer base, we believe that we have created such a platform.

Within the apartment rental community, most apartment websites primarily supply only the listings that property owners pay to advertise and often return results that are inconsistent with the renter's search criteria. These limited results generally do not provide information about the actual rental availabilities. We believe that consumers expect accurate, actionable and comprehensive apartment rental information. To create the new Apartments.com website, we have drawn on our multifamily database and undertaken a research effort collecting and verifying information and visiting and photographing properties. With the launch of the new Apartments.com website, we believe that we have created an easily searchable site with a comprehensive selection of rentals, information on actual rental availabilities and rents, and in-depth data on neighborhoods, including restaurants, nightlife, history, schools and other important facts.

CoStar's Comprehensive Database

CoStar has spent more than 27 years building and acquiring a database of commercial real estate information, which includes information on leasing, sales, comparable sales, tenants, and demand statistics, as well as digital images.

As of January 30, 2015, our database of real estate information covered the U.S., London, England and other parts of the U.K., and contained information about:

- Approximately 1.3 million sale and lease listings;
- Approximately 4.5 million total properties;
- Approximately 8.2 billion square feet of sale and lease listings;
- Approximately 5.8 million tenants;
- Approximately 2.3 million sales transactions valued in the aggregate at approximately \$5.7 trillion; and
- Approximately 16.5 million digital attachments, including building photographs, aerial photographs, plat maps and floor plans.

This highly complex database is comprised of hundreds of data fields, tracking such categories as:

- Location
- Site and zoning information
- Building characteristics
- Space availability
- Tax assessments
- Ownership
- Sales and lease comparables
- Space requirements
- Number of retail stores
- Mortgage and deed information
- For-sale information
- Income and expense histories
- Tenant names
- Lease expirations
- Contact information
- Historical trends
- Demographic information
- Retail sales per square foot

CoStar Research

We have developed a sophisticated data collection organization utilizing a multi-faceted research process. In 2014, our full time researchers and contractors drove millions of miles, conducted hundreds of thousands of on-site building inspections, and conducted millions of interviews of brokers, owners, tenants, apartment community owners and property managers.

Research Department. As of January 30, 2015, we had approximately 1,481 commercial real estate research professionals and outside contractors performing research. Our research professionals undergo an extensive training program so that we can maintain consistent research methods and processes throughout our research department. Our researchers collect and analyze commercial real estate information through millions of phone calls, e-mails and internet updates each year, in addition to field inspections, public records review, news monitoring and direct mail. Each researcher is responsible for maintaining the accuracy and reliability of database information. As part of their update process, researchers develop cooperative relationships with industry professionals that allow them to gather useful information. Because of the importance commercial real estate professionals place on our data and our prominent position in the industry, many of these professionals routinely take the initiative and proactively report available space and transactions to our researchers.

CoStar has an extensive field research effort that includes physical inspection of properties in order to research new markets, find additional property inventory, photograph properties and verify existing information. CoStar's field research effort also includes creating high quality videos of interior spaces (including walk-through videos of apartment communities), amenities and exterior features of properties. CoStar utilizes 146 high-tech, field research vehicles across the U.S., Canada and the U.K. A significant majority of these vehicles are customized energy efficient hybrid cars that are equipped with computers, proprietary Global Positioning System tracking software, high resolution digital cameras and handheld laser instruments to help precisely measure buildings, geo-code them and position them on digital maps. Some of our researchers also use custom-designed trucks with the same equipment as well as pneumatic masts that extend up to an elevation of twenty-five feet to allow for unobstructed building photographs from "birds-eye" views. Each CoStar vehicle uses wireless technology to track and transmit field data. A typical site inspection consists of photographing the building, measuring the building, geo-coding the building, capturing "For Sale" or "For Lease" sign information, counting parking spaces, assessing property condition and construction, and gathering tenant information. Certain researchers canvass properties, collecting tenant data suite by suite. Our subsidiary, CoStar Field Research, LLC, recently entered into an agreement to purchase a low-flying airplane capable of conducting aerial research of commercial real estate. In 2015, we plan to place researchers on the low-flying aircraft to scout additional commercial developments and take aerial photographs.

Data and Image Providers. We license a small portion of our data and images from public record providers and third party data sources. Licensing agreements with these entities provide for our use of a variety of commercial real estate information, including property ownership, tenant information, demographic information, maps and aerial

photographs, all of which enhance various CoStar services. These license agreements generally grant us a non-exclusive license to use the data and images in the creation and supplementation of our information, analytics and online marketplaces and include what we believe are standard terms, such as a contract term ranging from one to five years, automatic renewal of the contract and fixed periodic license fees or a combination of fixed periodic license fees plus additional fees based upon our usage.

Management and Quality Control Systems. Our research processes include automated and non-automated controls to ensure the integrity of the data collection process. A large number of automated data quality tests check for potential errors, including occupancy date conflicts, available square footage greater than building area, typical floor space greater than land area and expired leases. We also monitor changes to critical fields of information to ensure all information is kept in compliance with our standard definitions and methodology. Our non-automated quality control procedures include:

- calling our information sources on recently updated properties to re-verify information;
- performing periodic research audits and field checks to determine if we correctly canvassed buildings;
- providing training and retraining to our research professionals to ensure accurate data compilation; and
- compiling measurable performance metrics for research teams and managers for feedback on data quality.

Finally, one of the most important and effective quality control measures we rely on is feedback provided by the commercial real estate professionals using our data every day.

Proprietary Technology

As of January 30, 2015, CoStar had a staff of 417 product development, database and network professionals. CoStar's information technology professionals focus on developing new services for our customers, integrating our current services, and delivering research automation tools that improve the quality of our data and increase the efficiency of our research analysts.

Our subscription-based information services consist primarily of CoStar Suite™ services. CoStar Suite is sold as a platform of service offerings consisting of CoStar Property Professional®, CoStar COMPS Professional® and CoStar Tenant® and through our mobile application, CoStarGo®.

Our information technology team is responsible for developing, improving and maintaining CoStar services, including but not limited to CoStar Property Professional®, CoStar COMPS Professional®, CoStar Tenant®, CoStar Showcase®, CoStarGo®, CoStar Connect®, CoStar Lease Analysis™, CoStar Multifamily®, LoopNet Premium Lister™, LoopNet Premium Searcher™, LoopLink®, CoStar Portfolio Strategy™ products and services, CoStar Market Analytics™ products and services, CoStar Investment Analysis™ Portfolio Maximizer and CoStar Investment Analysis™ Request, CoStar Real Estate Manager™ products and services, and Apartments.com products and services.

Our information technology team is responsible for developing the infrastructure necessary to support CoStar's business processes, our comprehensive database of commercial real estate information, analytics and online marketplaces and our extensive image library. The team implements technologies and systems that introduce efficient workflows and controls that increase the production capacity of our research teams and improve the quality of our data. Over the years, the team has developed data collection and quality control mechanisms that we believe are unique to the commercial real estate industry. The team continues to develop and modify our enterprise information management system that integrates CoStar sales, research, field research, customer support and accounting information. We use this system to maintain our commercial real estate research information, manage contacts with the commercial real estate community, provide research workflow automation and conduct daily automated quality assurance checks. In addition, our information technology team has also developed fraud-detection technology to detect and prevent unauthorized access to our services.

Our information technology professionals also maintain the servers and network components necessary to support CoStar services and research systems. CoStar's core services are served from multiple data centers to support uninterrupted service for our customers. CoStar's services are continually monitored in an effort to ensure our

customers fast and reliable access.

CoStar's comprehensive data protection policy provides for use of secure networks, strong passwords, encrypted data fields, off-site storage and other protective measures in an effort to ensure the availability and security of all core systems.

Services

Our suite of information, analytics and online marketplaces is branded and marketed to our customers. Our services are primarily derived from a database of building-specific information and offer customers specialized tools for accessing, analyzing and using our information. Over time, we expect to continue to enhance our existing information, analytics and online marketplaces and develop additional services that make use of our comprehensive database to meet the needs of our existing customers as well as potential new categories of customers.

Our principal information, analytics and online marketplaces as of January 30, 2015, are described in the following paragraphs:

CoStar

CoStar Property Professional® CoStar Property Professional, or “CoStar Property,” is the Company’s flagship service. It provides subscribers a comprehensive inventory of office, industrial, retail and multifamily properties and land in markets throughout the U.S., U.K. and Toronto, Canada, including for-lease and for-sale listings, historical data, building photographs, maps and floor plans. Commercial real estate professionals use CoStar Property to identify available space for lease, evaluate leasing and sale opportunities, value assets and position properties in the marketplace. Our clients also use CoStar Property to analyze market conditions by calculating current vacancy rates, absorption rates or average rental rates, and forecasting future trends based on user selected variables. CoStar Property provides subscribers with powerful map-based search capabilities as well as a user controlled, password protected extranet (or electronic “file cabinet”) where brokers may share space surveys and transaction-related documents online, in real time, with team members. When used together with CoStar Connect, CoStar Property enables subscribers to share space surveys and transaction-related documents with their clients, accessed through their corporate website. CoStar Property, along with all of CoStar’s other core information, analytics and online marketplaces, is delivered solely via the Internet.

•**CoStar Multifamily®** CoStar Multifamily information, included as part of CoStar Property Professional, provides subscribers a comprehensive multifamily property database combined with analytic and forecasting tools that enable them to make investment decisions about multifamily properties. CoStar Multifamily provides information about buildings with 20 or more units including rents and occupancy rates, comparable sales transactions, construction locations, floor plans, high-resolution property images and detailed information on amenities and concessions.

•**CoStar Lease Analysis™** CoStar Lease Analysis is an integrated workflow tool that allows subscribers to incorporate CoStar data with their own data to perform in depth lease analyses. CoStar Lease Analysis can be used to produce an understandable cash flow analysis as well as key metrics about any proposed or existing lease. It combines financial modeling with CoStar’s comprehensive property information, enabling the subscriber to compare lease alternatives.

CoStar COMPS Professional® CoStar COMPS Professional, or “COMPS Professional,” provides comprehensive coverage of comparable commercial real estate sales information in the U.S., U.K. and Toronto, Canada. It is the industry’s most comprehensive database of comparable sales transactions and is designed for professionals who need to research property comparables, identify market trends, expedite the appraisal process and support property valuations. COMPS Professional offers subscribers numerous fields of property information, access to support documents (e.g., deeds of trust) for new comparables, demographics and the ability to view for-sale properties alongside sold properties in three formats – plotted on a map, aerial image or in a table.

CoStar Tenant® CoStar Tenant is a detailed online business-to-business prospecting and analytical tool providing commercial real estate professionals with the most comprehensive commercial real estate-related U.S., U.K. and Toronto, Canada tenant information available. CoStar Tenant profiles tenants occupying space in commercial buildings and provides updates on lease expirations - one of the service’s key features - as well as occupancy levels, growth rates and numerous other facts. Delivering this information via the Internet allows users to target prospective clients quickly through a searchable database that identifies only those tenants meeting certain criteria.

CoStarGo® CoStarGo is an iPad application that integrates and provides subscribers of Costar Suite mobile access to our comprehensive property, comparable sales and tenant information in our suite of online service offerings – consisting of CoStar Property Professional, CoStar COMPS Professional and CoStar Tenant. CoStarGo provides a single, location-centric mobile interface that allows users to access and display comprehensive information on

millions of properties and gain instant access to analytic data and demographic information from the field.

CoStar Advertising® CoStar Advertising offers property owners and brokers a highly targeted and cost effective way to market a space for lease or a property for sale directly to CoStar subscribers looking for that type of space through interactive advertising. Our advertising model is based on varying levels of exposure, enabling the advertiser to target as narrowly or broadly as its budget permits. With the CoStar Advertising program, when the advertiser's listings appear in a results set, they receive priority positioning and are enhanced to stand out. The advertiser can also purchase exposure in additional submarkets, or the entire market area so that this ad will appear even when this listing would not be returned in a results set.

CoStar Portfolio Strategy™ and CoStar Market Analytics™ Our subsidiary, CoStar Portfolio Strategy, offers products and services designed to meet the research needs of commercial real estate owners, investors and lenders. CoStar Portfolio Strategy and CoStar Market Analytics cover metropolitan areas throughout the U.S., the U.K., Toronto, Canada and Europe, with offerings including historical and forecast market data and analysis by market and property type, and services including access to CoStar Portfolio Strategy’s analysts, economists, and strategists to develop and deliver custom research solutions. Key tools include analysis of underlying property data, assessment of current market fundamentals, forecasts of future market performance, and credit default models.

•CoStar Risk Analytic™ COMPASS is CoStar Portfolio Strategy’s premier commercial real estate risk management tool. It allows users to calculate Probability of Default, Loss Given Default, Expected Loss, and Confidence Interval (of Expected Loss) results for a loan or a portfolio. It provides direct comparisons of credit risk and refinance risk across Time, Market, Property Type, and Loan Structure for all macroeconomic forecast scenarios. COMPASS^{CRE} is used by lenders, issuers, ratings agencies, and regulators to estimate required loss reserves and economic capital, target lending opportunities, set pricing strategy, objectively compare/price loans, more effectively allocate capital, and manage refinance risk.

CoStar Investment Analysis™ Portfolio Maximizer CoStar Investment Analysis Portfolio Maximizer is an industry leading real estate portfolio management software solution. CoStar Investment Analysis Portfolio Maximizer allows users to model partnership structures, calculate waterfall distributions and fees, model and analyze debt obligations, and create multiple “what if” scenarios for alternative investment decisions.

CoStar Investment Analysis™ Request CoStar Investment Analysis Request is the first business intelligence software solution built specifically for managing commercial real estate investments. CoStar Investment Analysis Request helps users eliminate some of the difficulties of consolidating real estate investment data from disparate sources and facilitates standardization of information presentation and reporting across an organization. CoStar Investment Analysis Request also provides a platform for users to develop business intelligence and reporting capabilities.

CoStar Real Estate Manager™ Corporate Edition CoStar Real Estate Manager Corporate Edition is a real estate management software solution designed for corporate real estate managers, company executives, business unit directors, brokers and project managers. CoStar Real Estate Manager Corporate Edition helps users connect real estate initiatives with company strategic goals, streamline portfolio operations, automate the process for collecting and managing space requests, reduce occupancy costs with analytics that track location performance against targets, and maximize location performance through proactive portfolio management. CoStar Real Estate Manager also provides lease abstraction and data review services in order to facilitate the effective implementation of this software solution.

CoStar Real Estate Manager™ Retail Edition CoStar Real Estate Manager Retail Edition is a real estate management software solution designed for company executives, real estate dealmakers and store planning and construction managers. CoStar Real Estate Manager Retail Edition helps users to utilize comprehensive and real-time data to establish goals and store strategies, manage the execution of real estate strategies, summarize critical portfolio data to drive cost-saving decisions, and benchmark prerequisite store-level information and metrics for maximizing location performance through proactive portfolio management. CoStar Real Estate Manager also provides lease abstraction and data review services in order to facilitate the effective implementation of this software solution.

CoStar Private Sale Network™ CoStar Private Sale Network provides clients with custom-designed and branded websites to market their listings directly to investors. CoStar Private Sale Network allows investors to customize a commercial real estate website and build and send email communications to announce listings, calls for offers, and bid deadlines.

CoStar Brokerage Applications™ CoStar Brokerage Applications provides users with access to the latest tools to effectively manage and optimize business operations. These structured and consistent project management tools allow users to track critical dates, employee or organization-wide results, and current and prospective projects.

LoopNet

LoopNet® Basic and Premium Membership Our subsidiary, LoopNet, offers two types of memberships on the LoopNet marketplace, basic and premium. Basic membership is available free-of-charge to anyone who registers at our LoopNet website and enables members to experience some of the benefits of the LoopNet offering, with limited functionality. As of January 30, 2015, LoopNet had approximately 9.4 million registered members, of which 81,856 were premium members.

•LoopNet Premium Lister™ LoopNet Premium Lister is designed for commercial real estate professionals and other customers who seek the broadest possible exposure for their listings, access to leads lists, and advanced marketing and searching tools. LoopNet Premium Lister provides subscribers with the ability to market their listings to all LoopNet.com visitors, as well as numerous other features. LoopNet Premium Lister is available for a quarterly or annual subscription.

•LoopNet Premium Searcher™ LoopNet Premium Searcher is designed for members searching for commercial real estate who need commercial real estate marketplace searching access, reports and other marketing and searching tools. LoopNet Premium Searcher provides subscribers with full access to all LoopNet property listings, including Premium and Basic Listings, as well as numerous other features. LoopNet Premium Searcher is available for a monthly, quarterly or annual subscription.

LoopLink® LoopLink is an online real estate marketing and database services suite that enables commercial real estate firms to showcase their available properties both on the LoopNet marketplace and on the brokerage firm's own website using hosted search software. Within LoopNet, each LoopLink listing is branded with the client's logo and is hyperlinked to the client's website. Additionally, the LoopLink service provides customizable, branded property search and results screens that can be integrated into the client's website. The LoopNet import service offers the opportunity to simplify the process of submitting listings to LoopNet from the client's internal databases, and features advanced data matching and data integrity rules and file conversion capabilities. LoopNet charges a monthly subscription fee to commercial real estate firms for the LoopLink service. Key features of LoopLink include comprehensive reporting and listing administration tools, a searchable and seamlessly integrated professional directory, property mapping for geographic and feasibility analysis, thumbnail photos and expanded property descriptions in search results.

Apartments.com

Apartments.com™ Our subsidiary, Apartments, LLC (doing business as Apartments.com), operates an online apartment marketplace for renters that matches apartment seekers with apartment homes and provides property managers and owners a platform for marketing their properties. Apartments.com provides a variety of ad packages and enhancements that allow property managers and owners to fully showcase their apartment community through increased exposure and interactions that allow renters to view, engage and connect with the community, including featured community listings, customized flyers and brochures, and special offer coupons.

ApartmentHomeLiving.com™ ApartmentHomeLiving.com provides renters with another national online apartment rentals resource that showcases apartments for rent with official prices, pictures, floor plans and detailed information on each apartment.

LandsOfAmerica

LandsOfAmerica™ and LandAndFarm™ LandsOfAmerica.com and LandAndFarm.com are leading online marketplaces for rural land for sale. Sellers pay a fee to list their land for sale, and interested buyers can search the respective sites' listings for free.

BizBuySell

BizBuySell® and BizQuest® BizBuySell.com and BizQuest.com are leading online marketplaces for operating businesses for sale. Business sellers pay a fee to list their operating businesses for sale, and interested buyers can search the respective sites' listings for free. The BizBuySell and BizQuest Franchise Directories allow interested business buyers to search hundreds of franchise opportunities, and franchisors can list their availabilities in the directory on a cost per lead basis.

Clients

We draw clients from across the commercial real estate and related business community. Commercial real estate brokers have traditionally formed the largest portion of CoStar clients, however, we also provide services to owners, developers, landlords, property managers, financial institutions, retailers, vendors, appraisers, investment banks, government agencies and other parties involved in commercial real estate. The following chart lists U.S. and U.K. clients that are well known or have the highest annual subscription fees in each of the various categories, each as of January 30, 2015:

Brokers	Lenders, Investment Bankers	Institutional Advisors, Asset Managers
Avison Young	AEGON USA Realty Advisors	Bravo Strategies — U.K.
Binswanger	Bank of America, N.A.	AEW Capital Management LP
BNP Paribas — U.K.	Capital One Bank	BlackRock
CB Richard Ellis	Citibank	Hartford Investment Management Company
CB Richard Ellis — U.K.	Citigroup Global Markets — U.K.	ING Investment Management
Charles Dunn Company	Deutsche Bank	Lasalle Investment Management — U.K.
Coldwell Banker Commercial NRT	JP Morgan Chase Bank	Manulife Financial
Colliers	Key Bank	MetLife Real Estate Investment
Colliers International UK — U.K.	Q10 Capital LLC	NorthMarq Capital
CRESA	Suntrust	Progressive Casualty Insurance Co.
Cushman & Wakefield	TD Bank	Prudential
Cushman & Wakefield — U.K.	Wells Fargo	Standard Life Investments — U.K.
DAUM Commercial Real Estate Services	Wells Fargo — U.K.	USAA Real Estate Company
Drivers Jonas Deloitte — U.K.		
DTZ, a UGL company		
Gerald Eve — U.K.		
GVA Grimley — U.K.	Owners, Developers	Appraisers, Accountants
HFF	Europa Capital Partners — U.K.	Deloitte
Jones Lang LaSalle	Hines	Integra
Jones Lang LaSalle — U.K.	Industrial Developments	KPMG
Kidder Mathews	LNR Property Corp	Marvin F. Poer
Knight Frank LLP — U.K.	Shorenstein Properties, LLC	Price Waterhouse Coopers
Lambert Smith Hampton — U.K.	Tishman Speyer	Ryan LLC
Lee & Associates		
Marcus & Millichap		
Mohr Partners		
Montagu Evans — U.K.	Retailers	Government Agencies
NAI Global	7-Eleven	City of Chicago
Newmark Grubb Knight Frank	Carter's	Cook County Assessor's Office
Re/Max	Dollar General Corporation	County of Los Angeles
Savills Commercial — U.K.	Jos. A Bank	Federal Deposit Insurance Corporation
Savills Studley	Massage Envy	Federal Reserve Bank of New York
Sperry Van Ness	Petco	Internal Revenue Service
Transwestern	Rent-A-Center	Transportation Security Administration
USI Real Estate Brokerage Services	Sony	U.S. Department of Housing and Urban Development
Voit Real Estate Services	Spencer Gifts LLC	U.S. General Services Administration
Weichert Commercial Brokerage	Walgreens	Valuation Office Agency — U.K.

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REITs	Property Managers	Vendors
Boston Properties	AP Commercial	Comcast Corporation
Brandywine Realty Trust	Elliott Associates	Cox Communications
Duke Realty Corporation	Leggat McCall Properties	Kastle Systems
KBS Realty Advisors	Lincoln Property Company	Regus
Kimco Realty Corporation	Navisys Group	Time Warner Cable
Simon Property Group	Osprey Management Company	Turner Construction Company
Vornado/Charles E. Smith	PM Realty Group	Verizon Communications

For the years ended December 31, 2012, 2013 and 2014, no single client accounted for more than 5% of our revenues.

Sales and Marketing

As of January 30, 2015, CoStar had a staff of 751 sales, marketing and customer support professionals, with the majority of our direct sales force located in field sales offices. Our sales teams are primarily located in 31 field sales offices throughout the U.S. and in offices located in London, England; Manchester, England; Glasgow, Scotland; Paris, France and Toronto, Canada. Our inside sales teams are located in our Washington, DC; San Francisco, California; and Chicago, Illinois offices. These teams prospect for new clients and perform service demonstrations exclusively by telephone and over the Internet to support the direct sales force. A portion of the inside sales teams are also responsible for selling some of our services.

Our local offices typically serve as the platform for our in-market sales, customer support and field research operations for their respective regions. The sales force is responsible for selling to new prospects, training new and existing clients, providing ongoing customer support, renewing existing client contracts and identifying cross-selling opportunities. In addition, the sales force has primary front line responsibility for customer care. Our customer service and support staff is charged with ensuring high client satisfaction by providing ongoing customer support.

Our sales strategy is to aggressively attract new clients, while providing ongoing incentives for existing clients to subscribe to additional services. We actively manage client accounts in order to retain clients by providing frequent service demonstrations as well as company-client contact and communication. We place a premium on training new and existing client personnel on the use of our services so as to promote maximum client utilization and satisfaction with our services. Our strategy also involves entering into multi-year, multi-market license agreements with our larger clients.

We seek to make our services essential to our clients' businesses. To encourage clients to use our services regularly, we generally charge a fixed monthly amount for our subscription-based information services rather than fees based on actual system usage. Contract rates for subscription-based services are generally based on the number of sites, number of users, organization size, the client's business focus, geography and the number and types of services to which a client subscribes. Our subscription clients generally pay contract fees on a monthly basis, but in some cases may pay us on a quarterly or annual basis.

Our primary marketing methods include: service demonstrations; face to face networking; web-based marketing; direct marketing; communication via our corporate website and news services; participation in trade show and industry events; Company-sponsored events; print advertising in trade magazines and other business publications; client referrals; CoStar Advisor™, LoopNews™ and other company newsletters distributed via email to our clients and prospects. In addition, we recently launched an improved Apartments.com website with a cleaner look, information about actual rental availabilities, rents and other fees, and better search functionality. In conjunction with the launch, we plan to embark on a wide-scale marketing campaign commencing during the first quarter of 2015 and running throughout the remainder of 2015 to generate brand awareness and site traffic for Apartments.com, including an incremental investment of \$75.0 million above Apartments.com's 2014 annualized marketing spend since the close of the acquisition of the Apartments.com Business. The marketing campaign is expected to feature television and radio advertising, online/digital advertising, social media and out-of-home ads and will be reinforced by Search Engine Marketing.

Web-based marketing and direct marketing are effective means for us to find prospective clients. Our web-based marketing efforts include search engine optimization, paid advertising with major search engines and display advertising on commercial real estate news and business websites and mobile applications, and our direct marketing efforts include direct mail, email and telemarketing, and make extensive use of our unique, proprietary database. Once we have identified a prospective client, our most effective sales method is a service demonstration. We use various forms of advertising to build brand identity and reinforce the value and benefits of our services. We also sponsor and

attend local association activities and events, including industry-leading events for commercial real estate brokers, owner/investors and retail and financial services institutions, and attend and/or exhibit at industry trade shows and conferences to reinforce our relationships with our core user groups.

We currently offer dozens of webinars each year aimed at helping customers learn more about the commercial real estate industry and how to use our services. The webinars are available both as live presentations and as on-demand programs hosted on our website. On a monthly basis, we issue the CoStar Commercial Repeat Sales Index ("CCRSI"), a comprehensive set of benchmarks that investors and other market participants can use to better understand commercial real estate price movements. The Index is produced using our underlying data and is publicly distributed by CoStar through the news media and made available online at <http://www.costargroup.com/costar-news/ccrsi>.

Our sales and marketing efforts have focused and will continue to focus on cross-selling and marketing our services. We continue to cross-sell the services offered by the businesses we have acquired, including Apartments.com and LoopNet. Our goal is to upsell clients to the services that best meet their needs and to create further cross-selling revenue synergies.

Competition

The market for information, analytics and online marketplaces generally is competitive and rapidly changing. In the commercial real estate and apartment rentals industries, we believe the principal competitive factors affecting these services and providers are:

- quality and depth of the underlying databases;
- ease of use, flexibility, and functionality of the software;
- intuitiveness and appeal of the user interface;
- timeliness of the data, including listings;
- breadth of geographic coverage and services offered;
- completeness and accuracy of content;
- client service and support;
- perception that the service offered is the industry standard;
- price;
- effectiveness of marketing and sales efforts;
- proprietary nature of methodologies, databases and technical resources;
- vendor reputation;
- brand loyalty among customers; and
- capital resources.

We compete directly and indirectly for customers with the following categories of companies:

online marketing services or websites targeted to commercial real estate brokers, buyers and sellers of commercial real estate properties, insurance companies, mortgage brokers and lenders, such as [commercialssearch.com](#), [PropertyLine.com](#), Reed Business Information Limited, [officespace.com](#), [MrOfficeSpace.com](#), [TenantWise](#), [www.propertyshark.com](#), [Rofo](#), [BuildingSearch.com](#), [CIMLS](#), [CompStak](#), [Rightmove](#), [WorkplaceIQ](#), [RealPoint LLC](#) and [estatesgazette.com](#);

publishers and distributors of information, analytics and marketing services, including regional providers and national print publications, such as [Xceligent](#), [eProperty Data](#), [CBRE Economic Advisors](#), [Marshall & Swift](#), [Yale Robbins](#), [Reis](#), [Real Capital Analytics](#), [The Smith Guide](#), [Pierce Eislen](#) and [Axiometrics, Inc.](#);

internet listing services featuring apartments for rent, such as [ApartmentGuide.com](#), [ApartmentFinder.com](#), [ForRent.com](#), [Zillow Rentals](#), [Trulia Rent](#), [Craigslist](#), [ApartmentList.com](#), [Rent.com](#), and [Move.com](#);

locally controlled real estate boards, exchanges or associations sponsoring property listing services and the companies with whom they partner, such as [Xceligent](#), [eProperty Data](#), [Catalyst](#), the National Association of Realtors, [CCIM Institute](#), [Society of Industrial and Office Realtors](#), the [Commercial Association of Realtors Data Services](#) and the [Association of Industrial Realtors](#);

real estate portfolio management software solutions, such as [Cougar Software](#), [MRI Software](#), [Altus](#) and [Intuit](#);

real estate lease management and administration software solutions, such as [Accruent](#), [Tririga](#), [Manhattan Software](#) and [AMT](#);

in-house research departments operated by commercial real estate brokers; and

public record providers.

As the market for information, analytics and online marketplaces develops, additional competitors (including companies which could have greater access to data, financial, product development, technical, analytic or marketing resources than we do) may enter the market and competition may intensify. For example, a company like Bloomberg L.P. has the resources, and has previously announced an intention, to move into the commercial real estate information business. Further, a company like Google, which has a far-reaching web presence and substantial data aggregation capabilities, could enter the commercial real estate marketing arena. A company like Zillow, which already has a presence in residential real estate and the apartment rentals industry, could use its resources to further expand in the online apartment rentals industry creating greater competition among internet listing services for the marketing budgets of property managers and property owners. While we believe that we have successfully differentiated ourselves from existing competitors, current or future competitors could materially harm our business.

Proprietary Rights

To protect our proprietary rights in our methodologies, database, software, trademarks and other intellectual property, we depend upon a combination of:

- trade secret, misappropriation, copyright, trademark, computer fraud, database protection and other laws;
- registration of copyrights and trademarks;
- nondisclosure, noncompetition and other contractual provisions with employees and consultants;
- license agreements with customers;
- patent protection; and
- technical measures.

We seek to protect our software's source code, our database and our photography as trade secrets and under copyright law. Although copyright registration is not a prerequisite for copyright protection, we have filed for copyright registration for many of our databases, photographs, software and other materials. Under current U.S. copyright law, the arrangement and selection of data may be protected, but the actual data itself may not be. Certain U.K. database protection laws provide additional protections for our U.K. databases. We license our services under license agreements that grant our clients non-exclusive, non-transferable rights. These agreements restrict the disclosure and use of our information and prohibit the unauthorized reproduction or transfer of any of our proprietary information, methodologies or analytics.

We also attempt to protect our proprietary databases, our trade secrets and our proprietary information through confidentiality and noncompetition agreements with our employees and consultants. Our services also include technical measures designed to detect, discourage and prevent unauthorized copying of our intellectual property. We have established an internal antipiracy team that uses fraud-detection technology to continually monitor use of our services to detect and prevent unauthorized access, and we actively prosecute individuals and firms that engage in this unlawful activity.

We maintain U.S. and international trademark registrations for CoStar's core service names and proactively file U.S. and international trademark applications covering our new and planned service names. Our federally registered trademarks include CoStar®, CoStar Property®, CoStar COMPS Professional®, CoStar Tenant®, CoStarGo®, CoStar Showcase®, and LoopNet®, among many others. In the U.S., trademarks are generally valid as long as they are in use and have not been found to be generic. We consider our trademarks in the aggregate to constitute a valuable asset. In addition, we maintain a patent portfolio that protects certain of our systems and methodologies. We currently have one granted patent in the U.K., which expires in 2021, covering, among other things, certain of our field research methodologies and six patents in the U.S. which expire in 2020, 2021 (2 patents), 2022 (2 patents) and 2025, respectively, covering, among other things, critical elements of CoStar's proprietary field research technology and mapping tools. We regard the rights protected by our patents as valuable to our business, but do not believe that our business is materially dependent on any single patent or on our portfolio of patents as a whole.

Employees

As of January 30, 2015, we employed 2,444 employees. None of our employees are represented by a labor union. We have experienced no work stoppages. We believe that our employee relations are excellent.

Available Information

Our investor relations internet website is <http://www.costargroup.com/investors>. The reports we file with or furnish to the Securities and Exchange Commission, including our annual report, quarterly reports and current reports, as well as

amendments to those reports, are available free of charge on our internet website as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission. You may review and copy any of the information we file with the Securities and Exchange Commission at the Commission's Public Reference Room at 100 F Street, NE, Washington, DC 20549. You may obtain information regarding the operation of the Public Reference Room by calling the Securities and Exchange Commission at 1-800-SEC-0330. The Securities and Exchange Commission maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the Commission at <http://www.sec.gov>.

Item 1A. Risk Factors

Cautionary Statement Concerning Forward-Looking Statements

We have made forward-looking statements in this Report and make forward-looking statements in our press releases and conference calls that are subject to risks and uncertainties. Forward-looking statements include information that is not purely historic fact and include, without limitation, statements concerning our financial outlook for 2015 and beyond, our possible or assumed future results of operations generally, and other statements and information regarding assumptions about our revenues, EBITDA, adjusted EBITDA, non-generally accepted accounting principles (“GAAP”) net income, non-GAAP net income per share, net income, net income per share, fully diluted net income per share, weighted-average outstanding shares, taxable income, cash flow from operating activities, available cash, operating costs, amortization expense, intangible asset recovery, capital and other expenditures, effective tax rate, equity compensation charges, future taxable income, purchase amortization, the anticipated benefits of completed acquisitions, the anticipated benefits of cross-selling efforts, product development and release, sales and marketing campaigns, product integrations, elimination and de-emphasizing of services, contract renewal rate, the timing of future payments of principal under our \$400.0 million term loan facility available to us under a credit agreement dated April 1, 2014 (the “2014 Credit Agreement”), expectations regarding our compliance with financial and restrictive covenants in the 2014 Credit Agreement, acquisitions, financing plans, geographic expansion, capital structure, contractual obligations, legal proceedings and claims, our database, database growth, services and facilities, employee relations, future economic performance, our ability to liquidate or realize our long-term investments, management’s plans, goals and objectives for future operations, and growth and markets for our stock. Sections of this Report which contain forward-looking statements include “Business,” “Risk Factors,” “Properties,” “Legal Proceedings,” “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” “Quantitative and Qualitative Disclosures About Market Risk,” “Controls and Procedures” and the Financial Statements and related Notes.

Our forward-looking statements are also identified by words such as “hope,” “anticipate,” “may,” “believe,” “expect,” “intend,” “will,” “should,” “plan,” “estimate,” “predict,” “continue” and “potential” or the negative of these terms or other comparable terminology. You should understand that these forward-looking statements are estimates reflecting our judgment, beliefs and expectations, not guarantees of future performance. They are subject to a number of assumptions, risks and uncertainties that could cause actual results to differ materially from those expressed or implied in the forward-looking statements. The following important factors, in addition to those discussed or referred to under the heading “Risk Factors,” and other unforeseen events or circumstances, could affect our future results and could cause those results or other outcomes to differ materially from those expressed or implied in our forward-looking statements: commercial real estate market conditions; the pace of recovery in the commercial real estate market; general economic conditions; our ability to identify, acquire and integrate acquisition candidates; our ability to realize the expected benefits, cost savings or other synergies from acquisitions, including the Apartments.com acquisition, on a timely basis or at all; our ability to combine acquired businesses successfully or in a timely and cost-efficient manner; business disruption relating to integration of acquired businesses or other business initiatives; the amount of investment for sales and marketing and our ability to realize a return on investments in sales and marketing; our ability to effectively and strategically combine, eliminate or de-emphasize service offerings; reductions in revenues as a result of service changes; the time and resources required to develop upgraded services and expand service offerings; changes or consolidations within the commercial real estate industry; customer retention; our ability to attract new clients; our ability to sell additional services to existing clients; our ability to integrate our North America and International product offerings; our ability to successfully introduce new products or upgraded services in U.S. and foreign markets; our ability to attract consumers to our online marketplaces; competition; foreign currency fluctuations; global credit market conditions affecting investments; our ability to continue to expand successfully, timely and in a cost-efficient manner, including internationally; our ability to effectively penetrate and gain acceptance in new sectors; our ability to control costs; litigation; changes in accounting policies or practices; release of new and upgraded services or entry into new markets by us or our competitors; data quality; expansion, growth,

development and reorganization of our sales force; employee retention; technical problems with our services; managerial execution; changes in relationships with real estate brokers and other strategic partners; legal and regulatory issues; and successful adoption of and training on our services.

Accordingly, you should not place undue reliance on forward-looking statements, which speak only as of, and are based on information available to us on, the date of this Report. All subsequent written and oral forward-looking statements attributable to us or any person acting on our behalf are expressly qualified in their entirety by the cautionary statements contained or referred to in this section. We do not undertake any obligation to update any such statements or release publicly any revisions to these forward-looking statements to reflect new information or events or circumstances after the date of this Report or to reflect the occurrence of unanticipated events.

Risk Factors

Risks Related to our Business

Our revenues and financial position will be adversely affected if we are not able to attract and retain clients. Our success and revenues depend on attracting and retaining subscribers to our information, analytics and online marketplaces. Our subscription-based information, analytics and online marketplaces generate the largest portion of our revenues. However, we may be unable to attract new clients, and our existing clients may decide not to add, not to renew or to cancel subscription services. In addition, in order to increase our revenue, we must continue to attract new customers, continue to keep our cancellation rate low and continue to sell new services to our existing customers. We may not be able to continue to grow our customer base, keep the cancellation rate for customers and services low or sell new services to existing customers as a result of several factors, including without limitation: economic pressures; the business failure of a current client or clients; a decision that customers have no need for our services; a decision to use alternative services; customers' and potential customers' pricing and budgetary constraints; consolidation in the real estate and/or financial services industries; data quality; technical problems; or competitive pressures. We compete against many other commercial real estate information, analytics, and marketing service providers for business, including competitors that offer their services through rapidly changing methods of delivering real estate information. If clients cancel services or decide not to renew their subscription agreements, and we do not sell new services to our existing clients or attract new clients, then our renewal rate and revenues may decline.

A downturn or consolidation in the commercial real estate industry may decrease customer demand for our services. The commercial real estate market may be adversely impacted by many different factors, including lower than expected job growth or job losses resulting in reduced real estate demand; rising interest rates and slowing transaction volumes that negatively impact investment returns; excessive speculative new construction in localized markets resulting in increased vacancy rates and diminished rent growth; and unanticipated disasters and other adverse events such as slowing of the growth in the working age population resulting in reduced demand for all types of real estate. A reversal of improvements in the commercial real estate industry's leasing activity and absorption rates or a renewed downturn in the commercial real estate market may affect our ability to generate revenues and may lead to more cancellations by our current or future customers, either of which could cause our revenues or our revenue growth rate to decline and reduce our profitability. A depressed commercial real estate market has a negative impact on our core customer base, which could decrease demand for our information, analytics and online marketplaces. Also, companies in this industry are consolidating, often in order to reduce expenses. Consolidation, or other cost-cutting measures by our customers, may lead to cancellations of our information, analytics and online marketplace services by our customers, reduce the number of our existing clients, reduce the size of our target market or increase our clients' bargaining power, all of which could cause our revenues to decline and reduce our profitability. If cancellations, reductions of services, and failures to pay increase, and we are unable to offset the resulting decrease in revenue by increasing sales to new or existing customers, our revenues may decline or grow at lower rates.

If we are unable to hire qualified persons for, or retain and continue to develop, our sales force, or if our sales force is unproductive, our revenues could be adversely affected. In order to support revenues and future revenue growth, we need to continue to develop, train and retain our sales force. Our ability to build and develop a strong sales force may be affected by a number of factors, including: our ability to attract, integrate and motivate sales personnel; our ability to effectively train our sales force; the ability of our sales force to sell an increased number and different types of services; our ability to manage effectively an outbound telesales group; the length of time it takes new sales personnel to become productive; the competition we face from other companies in hiring and retaining sales personnel; our ability to effectively structure our sales force; and our ability to effectively manage a multi-location sales organization. If we are unable to hire qualified sales personnel and develop and retain the members of our sales force, including sales force management, or if our sales force is unproductive, our revenues or growth rate could decline and our expenses could increase.

Negative general economic conditions could increase our expenses and reduce our revenues. Our business and the commercial real estate industry are particularly affected by negative trends in the general economy. The success of our business depends on a number of factors relating to general global, national, regional and local economic conditions, including perceived and actual economic conditions, recessions, inflation, deflation, exchange rates, interest rates, taxation policies, availability of credit, employment levels, and wage and salary levels. Negative general economic conditions could adversely affect our business by reducing our revenues and profitability. If we experience greater cancellations or reductions of services and failures to timely pay, and we do not acquire new clients or sell new services to our existing clients, our revenues may decline and our financial position would be adversely affected. Adverse national and global economic events, as well as any significant terrorist attack, are likely to have a dampening effect on the economy in general, which could negatively affect our financial performance and our stock price. Market disruptions may also contribute to extreme price and volume fluctuations in the stock market that may affect our stock price for reasons unrelated to our operating performance. In addition, a significant increase in inflation could increase our expenses more rapidly than expected, the effect of which may not be offset by corresponding increases in revenue. Conversely, deflation resulting in a decline of prices could reduce our revenues. In the current economic environment, it is difficult to predict whether we will experience significant inflation or deflation in the near future. A significant increase in either could have an adverse effect on our results of operations.

We may not be able to compete successfully against existing or future competitors in attracting advertisers, which could harm our business, results of operations and financial condition. We compete to attract advertisers. Large companies with significant brand recognition have large numbers of direct sales personnel and web traffic, which may provide a competitive advantage. To compete successfully for advertisers against future and existing competitors, we must continue to invest resources in developing our advertising platform and proving the effectiveness and relevance of our advertising services. Pressure from competitors seeking to acquire a greater share of our advertisers' overall marketing budget could adversely affect our pricing and margins, lower our revenue, and increase our research and development and marketing expenses. If we are unable to compete successfully against our existing or future competitors, our business, results of operations or financial condition could be adversely affected.

We may be unable to increase awareness of our brands, including CoStar, LoopNet or Apartments.com, which could adversely affect our business. We rely heavily on our brands, which we believe are key assets of our Company. Awareness and differentiation of our brands are important for attracting and expanding the number of users of, and subscribers to, our online marketplaces, such as Apartments.com and LoopNet.com. In 2015, we expect to increase our investment in sales and marketing activities by approximately \$75.0 million to increase brand awareness and grow traffic in conjunction a wide-scale marketing campaign commencing during the first quarter of 2015 and running throughout the remainder of 2015 to generate brand awareness and site traffic for the improved Apartments.com website. Further, we expect that sales and marketing expenses for our other brands will continue to increase as we seek to grow the number of subscribers or advertisers to our marketplaces. Increased advertising may not be successful in increasing brand awareness or, ultimately, be cost-effective. If we are unable to maintain or enhance user and advertiser awareness of our brands, or if we are unable to recover our additional marketing and advertising costs through increased usage of our services, our business, results of operations and financial condition could be adversely affected.

We rely on Internet search engines to drive traffic to our websites. If search results do not feature our websites prominently, traffic to our websites would decrease and our business could be adversely affected. Google, Bing, Yahoo! and other Internet search websites drive traffic to our websites, including Apartments.com and LoopNet.com. For example, when a user types an apartment building address into an Internet search engine, organic search ranking of our Apartments.com webpages will determine how prominently such webpages are displayed in the search results. However, our ability to maintain high organic search result rankings is not entirely within our control. Our competitors' search engine optimization, or SEO, efforts may result in their websites receiving a higher search result page ranking than the rankings our websites receive, or Internet search engines could revise their methodologies in a

way that would adversely affect our search result rankings, each of which could slow the growth of our user base. Further, search engine providers could align with our competitors, which could adversely affect traffic to our websites. Our websites have experienced fluctuations in search result rankings in the past, and we anticipate similar fluctuations in the future. If we experience a material reduction in the number of users directed to our websites through Internet search engines, our business, results of operations and financial condition could be adversely affected.

If we are unable to maintain or increase traffic to our marketplaces, our business and operating results could be adversely affected. Our ability to generate revenue from our marketplace businesses depends, in part, on our ability to attract users to our websites. If we fail to maintain or increase traffic to our marketplaces, our ability to acquire additional subscribers or advertisers and deliver leads to existing subscribers and advertisers could be adversely affected. We expect that our marketing expenses may increase in connection with our efforts to maintain or increase traffic to our websites. Our efforts to maintain or generate additional traffic to our marketplaces may not be successful. Even if we are able to attract additional users, increases in our operating expenses could negatively impact our operating results if we are unable to generate more revenue through increased sales of subscriptions to our marketplace products. We also face competition to attract users to our marketplace websites. Our existing and potential competitors include companies that could devote greater technical and other resources than we have available to provide services that users might view as superior to our offerings. Any of our future or existing competitors may introduce different solutions that attract users away from our services or provide solutions similar to our own that have the advantage of better branding or marketing resources. If we are unable to increase traffic to our marketplaces, or if we are unable to generate enough additional revenue to offset increases in expenses related to increasing traffic to our marketplaces, our business and operating results could be adversely affected.

If real estate professionals or other advertisers reduce or cancel their advertising spending with us and we are unable to attract new advertisers, our operating results would be harmed. Our marketplace businesses, including the Apartments.com Business and LoopNet.com, depend on advertising revenue generated primarily through sales to persons in the real estate industry, including property managers and owners, and other advertisers. Our ability to attract and retain advertisers, and ultimately to generate advertising revenue, depends on a number of factors, including:

- increasing the number of unique visitors to, and users of, our websites and mobile applications;
- the quantity and quality of the leads that we provide to our advertisers;
- the success of any increased marketing and product development efforts directed at attracting additional users and advertisers to our marketplaces;
- keeping pace with changes in technology and with our competitors; and
- offering an attractive return on investment to our advertisers for their advertising spending with us.

Further, with respect to the Apartments.com marketplace, our ability to attract and retain advertisers also depends on the current apartment rental market and apartment vacancy rates. If vacancy rates are too high or too low, advertisers may not need to utilize our marketplace services.

We do not have long-term contracts with most of the advertisers who advertise on our marketplaces. These advertisers could choose to modify or discontinue their relationships with us with little or no advance notice. In addition, as existing subscriptions for advertising expire, we may not be successful in renewing these subscriptions or securing new subscriptions. We may not succeed in retaining existing advertisers' spending or capturing a greater share of such spending if we are unable to convince advertisers of the effectiveness of our services as compared to alternatives. In addition, future changes to our pricing methodology for advertising services may cause advertisers to reduce or discontinue their advertising with us. If current advertisers reduce or end their advertising spending with us and we are unable to attract new advertisers, our advertising revenue and business, results of operations and financial condition could be adversely affected.

If we do not invest in product development and provide services that are attractive to our users and to our advertisers, our business could be adversely affected. Our success depends on our continued improvements to provide services that make our marketplaces useful for users, and attractive to our advertisers. As a result, we must continually invest resources in research and development to improve the appeal and comprehensiveness of our services and effectively incorporate new technologies. If we are unable to provide services that users want to use, then users may become

dissatisfied and use competitors' websites. If we are unable to continue offering innovative services, we may be unable to attract additional users and advertisers or retain our current users and advertisers, which could harm our business, results of operations and financial condition.

If we are not able to successfully finance and/or integrate acquisitions, our business operations and financial position could be adversely affected. We have expanded our markets and services in part through acquisitions of complementary businesses, services, databases and technologies, and expect to continue to do so in the future. Our strategy to acquire complementary companies or assets depends on our ability to identify, and the availability of, suitable acquisition candidates. We may incur costs in the preliminary stages of an acquisition, but may ultimately be unable or unwilling to consummate the proposed transaction for various reasons. In addition, acquisitions involve numerous risks, including the ability to realize or capitalize on synergy created through combinations; managing the integration of personnel and products; potential increases in operating costs; managing geographically remote operations; the diversion of management's attention from other business concerns and potential disruptions in ongoing operations during integration; the inherent risks in entering markets and sectors in which we have either limited or no direct experience; and the potential loss of key employees, clients or vendors and other business partners of the acquired companies. We may not successfully integrate acquired businesses or assets and may not achieve anticipated benefits of an acquisition, including expected synergies. Acquisitions could result in dilutive issuances of equity securities, the incurrence of debt, one-time write-offs of goodwill and substantial amortization expenses of other intangible assets. We may be unable to obtain financing on favorable terms, or at all, if necessary to finance future acquisitions making it impossible or more costly to acquire complementary businesses. If we are able to obtain financing, the terms may be onerous and restrict our operations. Further, certain acquisitions may be subject to regulatory approval, which can be time consuming and costly to obtain, and the terms of such regulatory approvals may impose limitations on our ongoing operations or require us to divest assets or lines of business.

The failure to successfully integrate the Apartments.com Business and/or fully realize expected synergies from the acquisition in the expected time frame or at all may adversely affect our future results and our business. The success of the Apartments.com acquisition will depend, in part, on our ability to successfully integrate the Apartments.com Business and realize the benefits and synergies we anticipate to result from the combination of our business and the Apartments.com Business, including anticipated growth opportunities and cost savings. We may not be able to achieve these objectives in whole or in part. Any failure to timely realize these anticipated benefits could have a material adverse effect on our revenues, expenses and operating results.

The success of the acquisition will also depend in part on our ability to minimize or eliminate any difficulties that may occur in connection with the integration of our business and the Apartments.com Business. The integration process could result in the loss of key employees, loss of key clients, loss of key vendors and other business partners, increases in operating costs, increases in taxes, or the disruption of each company's ongoing businesses, any or all of which could adversely affect our ability to achieve the anticipated benefits and synergies of the acquisition. Our efforts to integrate the two businesses will divert management's attention and other resources from uses that could otherwise have been beneficial to the Company. In addition, management may decide to combine or eliminate products or services currently offered by Apartments.com, which could also result in the loss of revenues, key employees, key clients, key vendors or other business partners.

During the integration process, we will depend on CV to provide certain services to us during a transitional period, including, among others, billing and collection services. If these services are not provided to us, we may incur additional expense to replicate or procure these services from other third parties.

Our current or future geographic expansion plans may not result in increased revenues, which may negatively impact our business, results of operations and financial position. Expanding into new markets and investing resources towards increasing the depth of our coverage within existing markets imposes additional burdens on our research, systems development, sales, marketing and general managerial resources. During 2015, we plan to continue to increase the depth of our coverage in the U.S., Canada and the U.K. If we are unable to manage our expansion efforts effectively, if our expansion efforts take longer than planned or if our costs for these efforts exceed our expectations, our financial position could be adversely affected. In addition, if we incur significant costs to improve data quality within existing

markets, or are not successful in marketing and selling our services in these markets or in new markets, our expansion may have a material adverse effect on our financial position by increasing our expenses without increasing our revenues, adversely affecting our profitability.

If we are not able to obtain and maintain accurate, comprehensive or reliable data, we could experience reduced demand for our information, analytics and online marketplace services. Our success depends on our clients' confidence in the comprehensiveness, accuracy and reliability of the data and analysis we provide. The task of establishing and maintaining accurate and reliable data and analysis is challenging. If our data, including the data we obtain from third parties, or analysis is not current, accurate, comprehensive or reliable, we could experience reduced demand for our services or legal claims by our customers, which could result in lower revenues and higher expenses. Our U.S. researchers use integrated internal research processes to update our database. Any inefficiencies, errors, or technical problems with this application could reduce the quality of our data, which could result in reduced demand for our services, lower revenues and higher costs.

We may not be able to successfully introduce new or upgraded information, analytics and online marketplace services or combine or shift focus from services with less demand, which could decrease our revenues and our profitability. Our future business and financial success will depend on our ability to continue to anticipate the needs of, and to introduce new and upgraded services into the marketplace. To be successful, we must adapt to changes in the industry, as well as rapid technological changes by continually enhancing our information, analytics and online marketplace services. Developing new services and upgrades to services, as well as integrating and coordinating current services, imposes heavy burdens on our systems department, management and researchers. The processes are costly, and our efforts to develop, integrate and enhance our services may not be successful. As we continue to combine our operations with those that we have acquired, we must continue to assess the purposes for which various services may be used alone or together, and how we can best address those uses through stand-alone services or combinations or coordinating applications thereof. In addition, successfully launching and selling a new or upgraded service puts pressure on our sales and marketing resources. We recently launched the new Apartments.com website after undergoing extensive product development. We also plan to launch a wide-scale marketing campaign in an effort to increase brand awareness and site traffic. The launch of the new site and/or the new marketing campaign may not result in increased brand awareness, site traffic and/or revenues. If we are unsuccessful in obtaining greater market share, we may not be able to offset the expense associated with the new launch and marketing campaign, which could have a material adverse effect on our financial results.

If we are unable to develop new or upgraded services or decide to combine, shift focus from, or phase out a service that overlaps or is redundant with other services we offer, then our customers may choose a competitive service over ours and our revenues may decline and our profitability may be reduced. For example, we are currently assessing whether to transition the LoopNet marketplace to a pure marketing site for commercial real estate where, eventually, all listings would be paid and users could search the site for free. We would expect to see a short-term reduction in revenues and earnings if we implement this transition. Although we are assessing the best strategy to implement this shift and will seek to convert customers to higher value, more profitable annual subscription information services to increase revenues and earnings over time, we cannot predict with certainty whether we will be successful in shifting customers to higher value, more profitable subscriptions and, consequently, in offsetting any reduction in revenue and earnings; therefore, if we make this transition, our revenues and earnings may ultimately decline. In addition, if we incur significant costs in developing new or upgraded services or combining and coordinating existing services, are not successful in marketing and selling these new services or upgrades, or our customers fail to accept these new or combined and coordinating services, it could have a material adverse effect on our results of operations by decreasing our revenues and reducing our profitability.

Competition could render our services uncompetitive. The market for information systems and services in general is highly competitive and rapidly changing. Competition in this market may increase further if economic conditions or other circumstances cause customer bases and customer spending to decrease and service providers to compete for fewer customer resources. Our existing competitors, or future competitors, may have greater name recognition, larger customer bases, better technology or data, lower prices, easier access to data, greater user traffic or greater financial, technical or marketing resources than we have. Our competitors may be able to undertake more effective marketing campaigns, obtain more data, adopt more aggressive pricing policies, make more attractive offers to potential employees, subscribers, distribution partners and content providers or may be able to respond more quickly to new or emerging technologies or changes in user requirements. If we are unable to retain customers or obtain new customers, our revenues could decline. Increased competition could result in lower revenues and higher expenses, which would reduce our profitability.

Our focus on internal and external investments may place downward pressure on our operating margins. Over the past few years, we have increased the rate of investments in our business, including internal investments in product development and sales and marketing, to expand the breadth and depth of services we provide to our customers. Our investment strategy is intended to increase our revenue growth in the future. Our operating margins may experience

downward pressure in the short term as a result of investments. Furthermore, our investments may not have their intended effect. For instance, our external investments may lose value and we may incur impairment charges with respect to such investments. Such impairment charges may negatively impact our profitability. If we are unable to successfully execute our investment strategy or if we fail to adequately anticipate and address potential problems, we may experience decreases in our revenues and operating margins.

If we are unable to enforce or defend our ownership and use of intellectual property, our business, brands, competitive position and operating results could be harmed. The success of our business depends in large part on our intellectual property, including intellectual property involved in our methodologies, database, services and software. We rely on a combination of trademark, trade secret, patent, copyright and other laws, nondisclosure and noncompetition provisions, license agreements and other contractual provisions and technical measures to protect our intellectual property rights. However, current law may not provide for adequate protection of our databases and the actual data. In addition, legal standards relating to the validity, enforceability and scope of protection of proprietary rights in internet related businesses are uncertain and evolving, and changes in these standards may adversely impact the viability or value of our proprietary rights. If we are not successful in protecting our intellectual property, including our content, our brands and our business, results of operations and financial condition could be harmed. The same would be true if a court found that our services infringe other persons' intellectual property rights. Any intellectual property lawsuits or threatened lawsuits in which we are involved, either as a plaintiff or as a defendant, could cost us a significant amount of time and money and distract management's attention from operating our business. In addition, if we do not prevail on any intellectual property claims, this could result in a change to our methodology or information, analytics and online marketplace services and could reduce our profitability.

Effective trademark, trade secret, patent, and copyright protection may not be available in every country in which our services may be provided. The laws of certain countries do not protect proprietary rights to the same extent as the laws of the United States and, therefore, in certain jurisdictions, we may be unable to protect our intellectual property and our proprietary technology adequately against unauthorized third-party copying or use, which could harm our competitive position.

In addition, we seek to enforce our rights against people and entities that infringe our intellectual property, including through legal action. Taking such action may be costly, and we cannot ensure that such actions will be successful. Any increase in the unauthorized use of our intellectual property could make it more expensive for us to do business and harm our results of operations or financial condition.

We are subject to a number of risks related to acceptance of credit cards and debit cards for customer payments. We accept payments for our services through credit and debit card transactions. For credit and debit card payments, we pay interchange and other fees, which may increase over time. An increase in those fees may require us to increase the prices we charge and would increase our cost of revenues, either of which could harm our business, financial condition or results of operations.

We depend on processing vendors to complete credit and debit card transactions. If we or our processing vendors fail to maintain adequate systems for the authorization and processing of credit card transactions, it could cause one or more of the major credit card companies to disallow our continued use of their payment products. We could lose customers if we are not able to continue to use payment products of the major credit card companies. In addition, if the systems for the authorization and processing of credit card transactions fail to work properly and, as a result, we do not charge our customers' credit cards on a timely basis or at all, our business, revenue, results of operations and financial condition could be harmed.

We are also subject to payment card association operating rules, certification requirements and rules governing electronic funds transfers, which could change or be reinterpreted in ways that make it more difficult for us to comply. We are required to comply with payment card industry security standards. Failing to comply with those standards may violate payment card association operating rules, federal and state laws and regulations, and the terms of our contracts with payment processors. Any failure to comply also may subject us to fines, penalties, damages and civil liability, and may result in the loss of our ability to accept credit and debit card payments. Further, there is no guarantee that such compliance will prevent illegal or improper use of our payment systems or the theft, loss, or misuse of data pertaining to credit and debit cards, card holders and transactions. If we fail to adequately control fraudulent credit

card transactions, we may face civil liability, diminished public perception of our security measures, and significantly higher credit card-related costs, each of which could harm our business, results of operations and financial condition.

If we are unable to maintain our chargeback rate or refund rates at acceptable levels, our processing vendors may increase our transaction fees or terminate their relationships with us. Any increases in our credit and debit card fees could harm our results of operations, particularly if we elect not to raise our rates for our services to offset the increase. The termination of our ability to process payments on any major credit or debit card would significantly impair our ability to operate our business.

We may not be able to successfully halt the operation of websites that aggregate our data, as well as data from other companies, such as copycat websites that may misappropriate our data. Third parties may misappropriate our data through website scraping, robots or other means and aggregate this data on their websites with data from other companies. In addition, “copycat” websites may misappropriate data on our website and attempt to imitate our brands or the functionality of our website. We may not be able to detect all such websites in a timely manner and, even if we could, technological and legal measures may be insufficient to stop their operations. In some cases, particularly in the case of websites operating outside of the U.S., our available remedies may not be adequate to protect us against the misappropriation of our data. Regardless of whether we can successfully enforce our rights against the operators of these websites, any measures that we may take could require us to expend significant financial or other resources.

Litigation or government investigations in which we become involved may significantly increase our expenses and adversely affect our stock price. Currently and from time to time, we are a party to various lawsuits. Any lawsuits, threatened lawsuits or government investigations in which we are involved could cost us a significant amount of time and money to defend, could distract management’s attention away from operating our business, could result in negative publicity and could adversely affect our stock price. In addition, if any claims are determined against us or if a settlement requires us to pay a large monetary amount or take other action that materially restricts or impedes our operations, our profitability could be significantly reduced and our financial position could be adversely affected. Our insurance may not be sufficient to cover any losses we incur in connection with litigation claims.

If we fail to protect confidential information against security breaches, or if customers or potential customers are reluctant to use our services because of privacy concerns, we might face additional costs and could lose customers or potential customers. We collect, use and disclose personally identifiable information, including among other things names, addresses, phone numbers, and email addresses. We also collect, store and use sensitive or confidential transaction information and, in certain circumstances, credit card information. Our policies concerning the collection, use and disclosure of these types of information are described on our websites. While we believe that our policies are appropriate and that we are in compliance with our policies, we could be subject to legal claims, government action, harm to our reputation or experience significant remediation costs if we experience a security breach or our practices fail, or are seen as failing, to comply with our policies or with applicable laws concerning personally identifiable information.

We may be subject to legal liability for collecting, displaying or distributing information. Because the content in our database is collected from various sources and distributed to others, we may be subject to claims for breach of contract, defamation, negligence, unfair competition or copyright or trademark infringement or claims based on other theories. We could also be subject to claims based upon the content that is accessible from our website through links to other websites or information on our website supplied by third parties. We could also be subject to claims that the collection or provision of certain information breached laws and regulations relating to privacy and data protection. Even if these claims do not result in liability to us, we could incur significant costs in investigating and defending against any claims. Our potential liability for information distributed by us to others could require us to implement measures to reduce our exposure to such liability, which may require us to expend substantial resources and limit the attractiveness of our information, analytics and online marketplaces to users.

Concern of prospective customers regarding our use of the personal information collected on our websites could keep prospective customers from subscribing to our services. Industry-wide incidents or incidents with respect to our websites, including misappropriation of third-party information, security breaches, or changes in industry standards, regulations or laws, could deter people from using the Internet or our websites to conduct transactions that involve the transmission of confidential information, which could harm our business. Under various state laws, if there is a breach of our computer systems and we know or suspect that unencrypted personal customer data has been stolen, we are required to inform any customers whose data was stolen, which could result in significant costs and harm our reputation and business.

In addition, certain state laws require businesses that maintain personal information in electronic databases to implement reasonable measures to keep that information secure. Various states have enacted different and sometimes contradictory requirements for protecting personal information collected and maintained electronically. Compliance with numerous and contradictory requirements of the different states is particularly difficult for an online business such as ours which collects personal information from customers in multiple jurisdictions.

We may face adverse publicity and loss of consumer confidence if we are not able to comply with laws requiring us to take adequate measures to assure the confidentiality of the personally identifiable information that our customers have given to us. This could result in a loss of customers and revenue that could jeopardize our success. Even if we are in full compliance with all relevant laws and regulations, we may face liability or disruption of business if we do not comply in every instance or if the security of the customer data that we collect is compromised, regardless of whether our practices comply or not. If we were required to pay any significant amount of money in satisfaction of claims under these laws, or if we were forced to suspend operations for any length of time due to our inability to comply fully with any such laws, our business, operating results and financial condition could be adversely affected.

Our business depends on retaining and attracting highly capable management and operating personnel. Our success depends in large part on our ability to retain and attract management and operating personnel, including our President and Chief Executive Officer, Andrew Florance, and our other officers and key employees. Our business requires highly skilled technical, sales, management, web development, marketing and research personnel, who are in high demand and are often subject to competing offers. To retain and attract key personnel, we use various measures, including employment agreements, awards under a stock incentive plan and incentive bonuses for key employees. These measures may not be enough to retain and attract the personnel we need or to offset the impact on our business of the loss of the services of Mr. Florance or other key officers or employees.

We may have difficulty attracting, motivating and retaining executives and other key employees in light of the acquisition of the Apartments.com Business. Uncertainty about the effect of the acquisition on our employees, including employees who joined the Company as a result of the acquisition of the Apartments.com Business, may have an adverse effect on the combined business. This uncertainty may impair our ability to attract, retain and motivate key personnel. If our key employees or Apartments.com key employees depart, we may incur costs in identifying, hiring, training and retaining replacements for departing employees, which could reduce our ability to realize the anticipated benefits of the acquisition of the Apartments.com Business.

An impairment in the carrying value of goodwill could negatively impact our consolidated results of operations and net worth. Goodwill and identifiable intangible assets not subject to amortization are tested annually by each reporting unit on October 1 of each year for impairment and are tested for impairment more frequently based upon the existence of one or more indicators. We consider our operating segments, North America and International, as our reporting units under Financial Accounting Standards Board (“FASB”) authoritative guidance for consideration of potential impairment of goodwill. We assess the impairment of long-lived assets, identifiable intangibles and goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Judgments made by management relate to the expected useful lives of long-lived assets and our ability to realize undiscounted cash flows of the carrying amounts of such assets. The accuracy of these judgments may be adversely affected by several factors, including the factors listed below:

- § Significant underperformance relative to historical or projected future operating results;
- § Significant changes in the manner of our use of acquired assets or the strategy for our overall business;
- § Significant negative industry or economic trends; or
- § Significant decline in our market capitalization relative to net book value for a sustained period.

These types of events or indicators and the resulting impairment analysis could result in goodwill impairment charges in the future, which would reduce our profitability. Impairment charges could negatively affect our financial results in the periods of such charges, which may reduce our profitability. As of December 31, 2014, we had approximately \$1.1 billion of goodwill, including \$1.1 billion in our North America segment and \$24.4 million in our International segment.

As a result of the consolidation of certain of our facilities, we may incur additional costs. We have taken, and may continue to take, actions that may increase our cost structure in the short-term but are intended to reduce certain portions of our long-term cost structure, such as consolidation of office space. As a result of consolidation of office space, we may reduce our long-term occupancy costs, but incur restructuring charges. If our long-term cost reduction efforts are ineffective or our estimates of cost savings are inaccurate, our profitability could be negatively impacted. Expected savings from relocating facilities can be highly variable and uncertain. Further, we may not be successful in achieving the operating efficiencies or operating cost reductions expected from these efforts in the amounts or at the times we anticipate.

If we are unable to obtain or retain listings from commercial real estate brokers, agents, property owners, and apartment property managers, our commercial real estate ("CRE") marketplace services, including but not limited to LoopNet, Apartments.com, CoStar Showcase, LandandFarm.com and Lands of America, could be less attractive to current or potential customers, which could reduce our revenues. The value of our CRE marketplace services to our customers depends on our ability to increase the number of property listings provided and searches conducted. The success of our CRE marketplace services depends substantially on the number of property listings submitted by brokers, agents, property owners and, in the case of apartment rentals, property managers. This is because an increase in the number of listings increases the utility of the online service and of its associated search, listing and marketing services. If agents marketing large numbers of property listings, such as large brokers in key real estate markets, choose not to continue their listings with us, or choose to list them with a competitor, our CRE marketplace services could be less attractive to other real estate industry transaction participants, resulting in reduced revenue. Similarly, the value and utility of our other marketplaces, including BizBuySell and BizQuest, are also dependent on attracting and retaining listings.

If we are unable to convince commercial real estate professionals that our CRE marketplace services are superior to traditional methods of listing, searching, and marketing commercial real estate, they could choose not to use those services, which could reduce our revenues or increase our expenses. The primary source of new customers for our CRE marketplace services is participants in the commercial real estate community. Many commercial real estate professionals are used to listing, searching and marketing real estate in traditional and off-line ways, such as by distributing print brochures, sharing written lists, placing signs on properties, word-of-mouth, and newspaper advertisements. Commercial real estate and investment professionals may prefer to continue to use traditional methods or may be slow to adopt and accept our online products and services. If we are not able to persuade commercial real estate participants of the efficacy of our online products and services, they may choose not to use our CRE marketplace services, which could negatively impact our business. Similarly, if we are unable to convince the business and investment community to utilize our online business for sale marketplaces rather than traditional methods of listing and marketing businesses for sale, our revenues could be negatively affected.

The number of LoopNet's registered members is higher than the number of actual members. The number of registered members in LoopNet's network is higher than the number of actual members because some members have multiple registrations or others may have registered under fictitious names. Given the challenges inherent in identifying these accounts, we do not have a reliable system to accurately identify the number of actual members, and thus we rely on the number of registered members as a measure of the size of the LoopNet marketplace. If the number of LoopNet's actual members does not continue to grow and those members do not convert to premium members, then the LoopNet marketplace business may not grow as fast as we expect, which could harm our operating and financial results.

If we are unable to increase our revenues or our operating costs are higher than expected, our profitability may decline and our operating results may fluctuate significantly. We may not be able to accurately forecast our revenues or future revenue growth rate. Many of our expenses, particularly personnel costs and occupancy costs, are relatively fixed. As a result, we may not be able to adjust spending quickly enough to offset any unexpected increase in expenses or revenue shortfall. We may experience higher than expected operating costs, including increased personnel costs, occupancy costs, selling and marketing costs, investments in geographic expansion, acquisition costs, communications costs, travel costs, software development costs, professional fees and other costs. If operating costs exceed our expectations and cannot be adjusted accordingly, our profitability may be reduced and our results of operations and financial position will be adversely affected. Additionally, we may not be able to sustain our historic revenue growth rates, and our percentage revenue growth rates may decline. Our ability to increase our revenues and operating profit will depend on increased demand for our services. Our sales are affected by, among other things, general economic and commercial real estate conditions. Reduced demand, whether due to changes in customer preference, a weakening of the U.S. or global economy, competition or other reasons, may result in decreased revenue and growth, adversely affecting our operating results.

International operations expose us to additional business risks, which may reduce our profitability. Our international operations and expansion subject us to additional business risks, including: currency exchange rate fluctuations; adapting to the differing business practices and laws in foreign countries; difficulties in managing foreign operations; limited protection for intellectual property rights in some countries; difficulty in collecting accounts receivable and longer collection periods; costs of enforcing contractual obligations; impact of recessions in economies outside the U.S.; and potentially adverse tax consequences. In addition, international expansion imposes additional burdens on our executive and administrative personnel, systems development, research and sales departments, and general managerial resources. If we are not able to manage our international operations successfully, we may incur higher expenses and our profitability may be reduced. Finally, the investment required for additional international expansion could exceed the profit generated from such expansion, which would reduce our profitability and adversely affect our financial position.

Fluctuating foreign currencies may negatively impact our business, results of operations and financial position. Due to our acquisitions of CoStar U.K. Limited (formerly FOCUS Information Limited), Grecam S.A.S., and Property and Portfolio Research Ltd., as well as our expansion into Canada, a portion of our business is denominated in the British Pound, Euro and Canadian dollar. As a result, fluctuations in foreign currencies may have an impact on our business, results of operations and financial position. Foreign currency exchange rates have fluctuated and may continue to fluctuate. Significant foreign currency exchange rate fluctuations may negatively impact our international revenue, which in turn affects our consolidated revenue. Currencies may be affected by internal factors, general economic conditions and external developments in other countries, all of which can have an adverse impact on a country's currency. Currently, we are not party to any hedging transactions intended to reduce our exposure to exchange rate fluctuations. We may seek to enter into hedging transactions in the future, but we may be unable to enter into these transactions successfully, on acceptable terms or at all. We cannot predict whether we will incur foreign exchange losses in the future. Further, significant foreign exchange fluctuations resulting in a decline in the respective, local currency may decrease the value of our foreign assets, as well as decrease our revenues and earnings from our foreign subsidiaries, which would reduce our profitability and adversely affect our financial position.

Our indebtedness could adversely affect us, including by decreasing our business flexibility and increasing our costs. On April 1, 2014 (the "Closing Date"), we entered into the 2014 Credit Agreement by and among CoStar, as borrower, CoStar Realty Information, Inc., as co-borrower, the lenders from time to time party thereto and JPMorgan Chase Bank, N.A., as administrative agent. The 2014 Credit Agreement provides for a \$400.0 million term loan facility and a \$225.0 million revolving credit facility, each with a term of five years. The proceeds of the term loan facility and the initial borrowing under the revolving credit facility on the Closing Date in an amount of \$150.0 million were used to refinance the term loan facility and revolving credit facility established under a credit agreement dated February 16, 2012 (the "2012 Credit Agreement"), including related fees and expenses, and pay a portion of the consideration and transaction costs related to the acquisition. The 2014 Credit Agreement contains customary restrictive covenants imposing operating and financial restrictions on us, including restrictions that may limit our ability to engage in acts that we believe may be in our long-term best interests. These covenants restrict our ability and the ability of our subsidiaries to (i) incur additional indebtedness, (ii) create, incur, assume or permit to exist any liens, (iii) enter into mergers, consolidations or similar transactions, (iv) make investments and acquisitions, (v) make certain dispositions of assets, (vi) make dividends, distributions and prepayments of certain indebtedness, and (vii) enter into certain transactions with affiliates.

The operating restrictions and financial covenants in the 2014 Credit Agreement and any future financing agreements may limit our ability to finance future operations or capital needs, to engage in other business activities or to respond to changes in market conditions. Our ability to comply with any financial covenants could be affected materially by events beyond our control, and we may be unable to satisfy any such requirements. If we fail to comply with these covenants, we may need to seek waivers or amendments of such covenants, seek alternative or additional sources of financing or reduce our expenditures. We may be unable to obtain such waivers, amendments or alternative or additional financing on a timely basis or at all, or on favorable terms.

We are required to make periodic principal and interest payments pursuant to the terms of the 2014 Credit Agreement. If an event of default occurs, the interest rate on overdue amounts will increase and the lenders under the 2014 Credit Agreement may declare all outstanding borrowings, together with accrued interest and other fees, to be immediately due and payable and may exercise remedies in respect of the collateral. We may not be able to repay all amounts due under the 2014 Credit Agreement in the event these amounts are declared due upon an event of default.

Negative conditions in the global credit markets may affect the liquidity of a portion of our long-term investments. Currently, our long-term investments include mostly AAA-rated auction rate securities ("ARS"), which are primarily student loan securities supported by guarantees from the Federal Family Education Loan Program ("FFELP") of the U.S. Department of Education. Continuing negative conditions in the global credit markets have

prevented some investors from liquidating their holdings of auction rate securities because the amount of securities submitted for sale has exceeded the amount of purchase orders for such securities. As of December 31, 2014, we held \$18.7 million par value of ARS, all of which failed to settle at auctions. When an auction fails for ARS in which we have invested, we may be unable to liquidate some or all of these securities at par. In the event we need or desire to immediately access these funds, we will not be able to do so until a future auction on these investments is successful, a buyer is found outside the auction process or an alternative action is determined. If a buyer is found but is unwilling to purchase the investments at par, we may incur a loss, which would reduce our profitability and adversely affect our financial position.

Our ARS investments are not currently actively trading and therefore do not currently have a readily determinable market value. The estimated fair value of the ARS no longer approximates par value. We have used a discounted cash flow model to determine the estimated fair value of our investment in ARS as of December 31, 2014. The assumptions used in preparing the discounted cash flow model include estimates for interest rates, credit spreads, timing and amount of cash flows, liquidity risk premiums, expected holding periods and default risk of the ARS. We update the discounted cash flow model on a quarterly basis to reflect any changes in the assumptions used in the model and settlements of ARS investments that occurred during the period. Based on this assessment of fair value, as of December 31, 2014, we determined there was a decline in the fair value of our ARS investments of approximately \$691,000. The decline was deemed to be a temporary impairment and was recorded as an unrealized loss in accumulated other comprehensive loss in stockholders' equity. If the issuers of these ARS are unable to successfully close future auctions and/or their credit ratings deteriorate, we may be required to record additional unrealized losses in accumulated other comprehensive loss or an other-than-temporary impairment charge to earnings on these investments, which would reduce our profitability and adversely affect our financial position.

We have not made any material changes in the accounting methodology used to determine the fair value of the ARS. We do not expect any material changes in the near term to the underlying assumptions used to determine the unobservable inputs used to calculate the fair value of the ARS as of December 31, 2014. However, if changes in these assumptions occur, and, should those changes be significant, we may be required to record additional unrealized losses in accumulated other comprehensive loss or an other-than-temporary impairment charge to earnings on these investments.

U.S. political, credit and financial market conditions may negatively impact or impair the value of our current portfolio of cash, cash equivalents and investments, including U.S. Treasury securities and U.S.-backed investments, as well as our access to credit. Our cash, cash equivalents and investments are held in a variety of common financial instruments, including U.S. treasury securities. Deterioration in the U.S. credit and financial markets may result in losses or deterioration in the fair value of our cash, cash equivalents, or investments. On August 5, 2011, Standard & Poor's lowered its long term sovereign credit rating on the U.S. from AAA to AA+. This downgrade, and any future downgrades of the U.S. credit rating, could impact the stability of future U.S. treasury auctions, affect the trading market for U.S. government securities, result in increased interest rates and impair access to credit. These factors could negatively impact the liquidity or valuation of our current portfolio of cash, cash equivalents, and investments, which may affect our ability to fund future obligations. Further, these factors may result in an increase in interest rates and borrowing costs and make it more difficult to obtain credit on acceptable terms, which may affect our ability to fund future obligations and increase the costs of obtaining financing for future obligations.

Technical problems or disruptions that affect either our customers' ability to access our services, or the software, internal applications, database and network systems underlying our services, could damage our reputation and brands and lead to reduced demand for our information, analytics and online marketplace services, lower revenues and increased costs. Our business, brands and reputation depend upon the satisfactory performance, reliability and availability of our websites, the Internet and our service providers. Interruptions in these systems, whether due to system failures, computer viruses, software errors, physical or electronic break-ins, or malicious hacks or attacks on our systems (such as denial of service attacks), could affect the security and availability of our services on our mobile applications and our websites and prevent or inhibit the ability of users to access our services. Our operations also depend on our ability to protect our databases, computers and software, telecommunications equipment and facilities against damage from potential dangers such as fire, flood, power loss, security breaches, computer viruses, telecommunications failures, terrorist attacks, acts of war, electronic and physical break-ins, computer viruses, earthquakes and similar events. Our users rely on our services when conducting their own businesses. Disruptions in, or reductions in ability to access, our services for whatever reason could damage our users' businesses, harm our reputation, result in additional costs or result in reduced demand for our information, analytics and online marketplace services, any of which could harm our business, results of operations and financial condition.

In addition, the software, internal applications and systems underlying our services are complex and may not be error-free. Our careful development and testing may not be sufficient to ensure that we will not encounter technical problems when we attempt to enhance our software, internal applications and systems. Any inefficiencies, errors or technical problems with our software, internal applications and systems could reduce the quality of our services or interfere with our customers' access to our information, analytics and online marketplaces, which could reduce the demand for our services, lower our revenues and increase our costs.

The majority of the communications, network and computer hardware used to operate our mobile applications and websites are located at facilities in Virginia and California. We do not own or control the operation of certain of these facilities. Our systems and operations are vulnerable to damage or interruption from fire, flood, power loss, security breaches, computer viruses, telecommunications failure, terrorist attacks, acts of war, electronic and physical break-ins, earthquakes and similar events. These risks may be increased with respect to operations housed at facilities we do not own or control. The occurrence of any of the foregoing events could result in damage to our systems and hardware or could cause them to fail completely, and our insurance may not cover such events or may be insufficient to compensate us for losses that may occur.

A failure of our systems at any site could result in reduced functionality for our users, and a total failure of our systems could cause our mobile applications or websites to be inaccessible. Problems faced or caused by our information technology service providers, including content distribution service providers, private network providers, internet providers and third-party web-hosting providers, or with the systems by which they allocate capacity among their customers (as applicable), could adversely affect the experience of our users. Any financial difficulties, such as bankruptcy reorganization, faced by these third-party service providers or any of the service providers with whom they contract may have negative effects on our business, the nature and extent of which are difficult to predict. If our third-party service providers are unable to keep up with our growing needs for capacity, our business could be harmed. In addition, if distribution channels for our mobile applications experience disruptions, such disruptions could adversely affect the ability of users and potential users to access or update our mobile applications, which could harm our business.

Our business interruption insurance may not cover certain events or may be insufficient to compensate us for the potentially significant losses, including the potential harm to the future growth of our business, which may result from interruptions in our service as a result of system failures or malicious attacks. Any errors, defects, disruptions or other performance problems with our services could harm our reputation, business, results of operations and financial condition.

Our operating results and revenues are subject to fluctuations and our quarterly financial results may be subject to seasonality and market cyclicality, each of which could cause our stock price to be negatively affected. The commercial real estate market may be influenced by general economic conditions, economic cycles, annual seasonality factors and many other factors, which in turn may impact our financial results. The market is large and fragmented. The different sectors of the industry, such as office, industrial, retail, multifamily, and others, are influenced differently by different factors, and have historically moved through economic cycles with different timing. As such, it is difficult to estimate the potential impact of economic cycles and conditions or seasonality from year-to-year on our overall operating results. In addition, our results may be impacted by seasonality. The timing of widely observed holidays and vacation periods, particularly slow downs during the end-of-year holiday period, and availability of real estate agents and related service providers during these periods, could significantly affect our quarterly operating results during that period. If we are unable to adequately respond to economic, seasonal or cyclical conditions, our revenues, expenses and operating results may fluctuate from quarter to quarter. Our operating results, revenues and expenses may fluctuate for many reasons, including those described below and elsewhere in this Annual Report on Form 10-K:

- Rates of subscriber adoption and retention;
- Timing of our sales conference or significant marketing events;
- A slow-down during the end-of-year holiday period;
- Changes in our pricing strategy and timing of changes;
- The timing and success of new service introductions and enhancements;
- The shift of focus from, or phase out of services that overlap or are redundant with other services we offer;
- The amount and timing of our operating expenses and capital expenditures;

- Our ability to control expenses;
- The amount and timing of non-cash stock-based charges;
- Costs related to acquisitions of businesses or technologies or impairment charges associated with such investments and acquisitions;
- Competition;
- Changes or consolidation in the real estate industry;
- Our investments in geographic expansion and to increase coverage in existing markets;
- Interest rate fluctuations;
- Successful execution of our expansion and integration plans;
- The development of our sales force;
- Foreign currency and exchange rate fluctuations;
- Inflation; and
- Changes in client budgets.

These fluctuations or seasonality effects could negatively affect our results of operations during the period in question and/or future periods or cause our stock price to decline. In addition, changes in accounting policies or practices may affect our level of net income. Fluctuations in our financial results, revenues and expenses may cause the market price of our common stock to decline.

The consent order approved by the Federal Trade Commission in connection with the LoopNet merger imposes conditions that could have an adverse effect on us and our business, and failure to comply with the terms of the consent order may result in adverse consequences for the combined company. On April 26, 2012, the FTC accepted the consent order in connection with the LoopNet merger that was previously agreed to among the FTC staff, CoStar, and LoopNet on April 17, 2012. The consent order was subject to a 30-day public comment period, and on August 29, 2012, the FTC issued its final acceptance of the consent order.

The consent order, which is publicly available on the FTC's website at <http://www.ftc.gov/>, requires CoStar to maintain certain business practices that the FTC believes are pro-competitive. For example, the consent order requires CoStar to maintain its customary practice of selling its products separately and on a market-by-market basis. It also requires CoStar to license its products to customers who have bought its competitors' products on a non-discriminatory basis. In addition, CoStar is required to maintain its customary licensing practices with respect to the length of its contracts, to allow customers with multi-year contracts to cancel with one year's advance notice, and to agree to reduce the cost of any litigation with customers by offering to arbitrate certain disputes. In the event that CoStar fails or is unable to comply with the terms of the consent order, CoStar could be subject to an enforcement proceeding that could result in substantial fines and/or injunctive relief. Further, the provisions of the consent order may result in unanticipated adverse effects on the combined company and, therefore, reduce our ability to realize the anticipated benefits of the merger. For example, the terms of the consent order that require us to continue to sell our products separately may prohibit us from combining or eliminating certain business lines, products or services that we believe would result in a long-term positive impact on our revenue and earnings.

We have incurred and will continue to incur acquisition-related costs. We have incurred severance costs and expect to incur additional costs to integrate prior acquisitions, such as IT integration expenses and costs related to the renegotiation of redundant vendor agreements. Costs in connection with acquisitions and integrations may be higher than expected, and we may also incur unanticipated acquisition-related costs. These costs could adversely affect our financial condition, results of operation or prospects of the combined business.

Changes in accounting and reporting policies or practices may affect our financial results or presentation of results, which may affect our stock price. Changes in accounting and reporting policies or practices could reduce our net income, which reductions may be independent of changes in our operations. These reductions in reported net income could cause our stock price to decline. For example, in 2006, we adopted authoritative guidance for stock compensation, which required us to expense the value of granted stock options.

Market volatility may have an adverse effect on our stock price. The trading price of our common stock has fluctuated widely in the past, and we expect that it will continue to fluctuate in the future. The price could fluctuate widely based on numerous factors, including: economic factors; quarter-to-quarter variations in our operating results; changes in analysts' estimates of our earnings; announcements by us or our competitors of technological innovations, new services, or other significant or strategic information; general conditions in the commercial real estate industry; developments or disputes concerning copyrights or proprietary rights or other legal proceedings; and regulatory developments. In addition, the stock market in general, and the shares of internet-related and other technology companies in particular, have experienced extreme price fluctuations. This volatility has had a substantial effect on the market prices of securities issued by many companies for reasons unrelated to the operating performance of the specific companies and may have the same effect on the market price of our common stock.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

Our headquarters is located at 1331 L Street, NW, in downtown Washington, DC, where we occupy approximately 149,500 square feet of office space. Our lease for our headquarters expires May 31, 2025 (with two 5-year renewal options). Our headquarters is used primarily by our North America operating segment. Our principal facility in the U.K. is located in London, England, where we occupy approximately 7,000 square feet of office space. Our lease for this facility has a maximum term ending July 8, 2023, with early termination at our option on July 9, 2018, with advance notice. This facility is used primarily by our International operating segment.

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In addition to two downtown Washington, DC leased facilities (including our headquarters) and our London, England facility, our research operations are principally run out of leased spaces in San Diego, California; Columbia, Maryland; Atlanta, Georgia; Glasgow, Scotland; and Paris, France. Additionally, we lease office space in a variety of other metropolitan areas. These locations include, without limitation, the following: New York; Los Angeles; Chicago; San Francisco; Sacramento; Boston; Orange County, California; Philadelphia; Houston; Phoenix; Detroit; Pittsburgh; Miami; Orlando; Denver; Dallas; Kansas City; Cleveland; Cincinnati; Indianapolis; Austin; Salt Lake City; Las Vegas; Seattle; Portland; St. Louis; Louisville; Minneapolis; San Luis Obispo, California; Ontario, California; Charlotte; Durham, North Carolina; Manchester, England and Toronto, Canada.

We believe these facilities are suitable and appropriately support our business needs.

Item 3. Legal Proceedings

Currently, and from time to time, we are involved in litigation incidental to the conduct of our business. Certain pending legal proceedings are discussed in Note 11 of the Notes to Consolidated Financial Statements included in this Annual Report on Form 10-K. We are not a party to any lawsuit or proceeding that, in the opinion of our management based on consultations with legal counsel, is likely to have a material adverse effect on our financial position or results of operations.

Item 4. Mine Safety Disclosures

Not Applicable.

PART II

Item 5. Market for the Registrant's Common Stock, Related Stockholder Matters and Issuer Purchases of Equity Securities

Price Range of Common Stock. Our common stock is traded on the Nasdaq Global Select Market under the symbol "CSGP." The following table sets forth, for the periods indicated, the high and low daily closing prices per share of our common stock, as reported by the Nasdaq Global Select Market.

	High	Low
Year Ended December 31, 2013		
First Quarter	\$ 109.46	\$ 89.28
Second Quarter	\$ 129.51	\$ 105.73
Third Quarter	\$ 170.09	\$ 131.03
Fourth Quarter	\$ 186.62	\$ 161.29
Year Ended December 31, 2014		
First Quarter	\$ 214.00	\$ 166.78
Second Quarter	\$ 188.95	\$ 150.55
Third Quarter	\$ 160.10	\$ 138.76
Fourth Quarter	\$ 188.39	\$ 137.60

As of February 2, 2015, there were 900 holders of record of our common stock.

Dividend Policy. We have never declared or paid any dividends on our common stock. The 2014 Credit Agreement includes covenants that, subject to certain exceptions, restrict our ability and the ability of our subsidiaries to pay dividends or distributions. Any future determination to pay dividends will be at the discretion of our Board of Directors, subject to applicable limitations under Delaware law, and will be dependent upon our results of operations, financial position and other factors deemed relevant by our Board of Directors. We do not anticipate paying any dividends on our common stock during the foreseeable future, but intend to retain any earnings for future growth of our business.

Recent Issues of Unregistered Securities. We did not issue any unregistered securities during the year ended December 31, 2014.

Issuer Purchases of Equity Securities. The following table is a summary of our repurchases of common stock during each of the three months in the quarter ended December 31, 2014:

ISSUER PURCHASES OF EQUITY SECURITIES

Month, 2014	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
October 1 through 31	58	\$148.32	—	—
November 1 through 30	—	—	—	—
	3,273	167.10	—	—

December 1
through 31
Total

3,331

(1) \$166.78

—

—

(1) The number of shares purchased consists of shares of common stock tendered by employees to the Company to satisfy the employees' minimum tax withholding obligations arising as a result of vesting of restricted stock grants under the Company's 2007 Stock Incentive Plan, as amended, which shares were purchased by the Company based on their fair market value on the vesting date. None of these share purchases were part of a publicly announced program to purchase common stock of the Company.

Stock Price Performance Graph

The stock performance graph below shows how an initial investment of \$100 in our common stock would have compared to:

• An equal investment in the Standards & Poor's Stock 500 ("S&P 500") Index;

• An equal investment in the S&P 500 Internet Software & Services Index; and

The comparison covers the period beginning December 31, 2009, and ending on December 31, 2014, and assumes the reinvestment of any dividends. You should note that this performance is historical and is not necessarily indicative of future price performance.

Company / Index	12/31/09	12/31/10	12/31/11	12/31/12	12/31/13	12/31/14
CoStar Group, Inc.	100	137.80	159.76	213.96	441.90	439.62
S&P 500 Index	100	115.06	117.49	136.30	180.44	205.14
S&P 500 Internet Software & Services Index	100	102.56	107.95	129.36	192.46	205.16

Item 6. Selected Consolidated Financial and Operating Data

Selected Consolidated Financial and Operating Data
(in thousands, except per share data)

The following table provides selected consolidated financial and other operating data for the five years ended December 31, 2014. The consolidated statement of operations data shown below for each of the three years ended December 31, 2012, 2013, and 2014 and the consolidated balance sheet data as of December 31, 2013 and 2014 are derived from audited consolidated financial statements that are included in this report. The consolidated statement of operations data for each of the years ended December 31, 2010 and 2011 and the consolidated balance sheet data as of December 31, 2010, 2011, and 2012 shown below are derived from audited consolidated financial statements for those years that are not included in this report. Information about prior period acquisitions that may affect the comparability of the selected financial information presented below is included in "Item 1. Business."

Consolidated Statement of Operations Data:	Year Ended December 31,				
	2010	2011	2012	2013	2014
Revenues	\$226,260	\$251,738	\$349,936	\$440,943	\$575,936
Cost of revenues	83,599	88,167	114,866	129,185	156,979
Gross margin	142,661	163,571	235,070	311,758	418,957
Operating expenses	119,886	141,800	207,630	257,604	338,079
Income from operations	22,775	21,771	27,440	54,154	80,878
Interest and other income	735	798	526	326	516
Interest and other expense	—	—	(4,832)	(6,943)	(10,481)
Income before income taxes	23,510	22,569	23,134	47,537	70,913
Income tax expense, net	10,221	7,913	13,219	17,803	26,044
Net income	\$13,289	\$14,656	\$9,915	\$29,734	\$44,869
Net income per share — basic	\$0.65	\$0.63	\$0.37	\$1.07	\$1.48
Net income per share — diluted	\$0.64	\$0.62	\$0.37	\$1.05	\$1.46
Weighted average shares outstanding — basic	20,330	23,131	26,533	27,670	30,215
Weighted average shares outstanding — diluted	20,707	23,527	26,949	28,212	30,641

Consolidated Balance Sheet Data:	As of December 31,				
	2010	2011	2012	2013	2014
Cash, cash equivalents, short-term and long-term investments	\$239,316	\$573,379	\$177,726	\$277,943	\$544,163
Working capital	188,279	521,401	97,925	196,913	480,521

Total assets	439,648	771,035	1,165,139	1,256,982
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Exhibit 99.1
to
Form 8-K,
filed on
January 23,
2009

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Exhibit Numbers	Description	Incorporation By Reference To
4.29	Amendment No. 11 to Receivables Financing Agreement and Consent, dated as of February 18, 2009, by and among Rite Aid Funding II, CAFCO, LLC, CRC Funding, LLC, Falcon Asset Securitization Company LLC, Variable Funding Capital Company LLC, Citibank, N.A., JPMorgan Chase Bank, NA., Wachovia Bank, National Association, Citicorp North America, Inc., Rite Aid Hdqtrs. Funding, Inc., as collection agent, and certain other parties thereto as originators	Exhibit 10.3 to Form 8-K, filed on February 20, 2009
4.30	Definitions Annex to the Senior Loan Documents and the Second Priority Debt Documents	Filed herewith
4.31	Fourth Amendment, dated as of June 4, 2007, to the Amended and Restated Collateral Trust and Intercreditor Agreement, dated as of June 27, 2001, as amended and restated as of May 28, 2003, among Rite Aid Corporation and its subsidiaries that are a party thereto, the collateral trustees, the collateral processing co-agents and the trustees of various indentures covered by this agreement	Filed herewith
4.32	Amended and Restated Collateral Trust and Intercreditor Agreement dated as of May 28, 2003, among Rite Aid Corporation, each Subsidiary of Rite Aid named therein or which becomes a party hereto, Wilmington Trust Company, as collateral trustee for the holders from time to time of the Second Priority Debt Obligations, Citicorp North America, Inc., as senior collateral processing co-agent, JPMorgan Chase Bank, as senior collateral processing co-agent for the Senior Secured Parties under the Senior Loan Documents, U.S. Bank and Trust, as trustee under the 12.5% Note Indenture, BNY Midwest Trust Company, as trustee under the 9.5% Note Indenture and as trustee under the 8.125% Note Indenture, and each other Second Priority Representative which becomes a party thereto	Exhibit 10.2 to Form 8-K, filed on May 30, 2003
4.33	Senior Subsidiary Guarantee Agreement, dated as of June 27, 2001, as amended and restated as of May 28, 2003, and as supplemented as of September 27, 2004, among the Subsidiary Guarantors and Citicorp North America, Inc., as collateral processing agent	Filed herewith

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Exhibit Numbers	Description	Incorporation By Reference To
4.34	Senior Subsidiary Security Agreement, dated as of June 27, 2001, as amended and restated as of May 28, 2003, as supplemented by Supplement No. 1 dated as of June 27, 2004, and as amended and restated as of September 22, 2004 by the Subsidiary Guarantors in favor of the Citicorp North America, Inc. and JPMorgan Chase Bank, N.A., as collateral processing co-agents	Filed herewith
4.35	Senior Indemnity, Subrogation and Contribution Agreement, dated as of June 27, 2001, as amended and restated as of May 28, 2003, and supplemented as of September 27, 2004, among Rite Aid Corporation, the Subsidiary Guarantors, and Citicorp North America, Inc. and JPMorgan Chase Bank, N.A., as collateral processing co-agents	Exhibit 4.27 to Form 10-K, filed on April 29, 2008
4.36	Second Priority Subsidiary Guarantee Agreement, dated as of June 27, 2001, as amended and restated as of May 28, 2003, and as supplemented as of January 5, 2005, among the Subsidiary Guarantors and Wilmington Trust Company, as collateral agent	Filed herewith
4.37	Second Priority Subsidiary Security Agreement, dated as of June 27, 2001, as amended and restated as of May 28, 2003, as supplemented as of January 5, 2005, and as amended in the Reaffirmation Agreement and Amendment dates as of January 11, 2005, by the Subsidiary Guarantors in favor of Wilmington Trust Company, as collateral trustee.	Filed herewith
4.38	Second Priority Indemnity, Subrogation and Contribution Agreement, dated as of June 27, 2001, as amended and restated as of May 28, 2003, and as supplemented as of January 5, 2005, among the Subsidiary Guarantors and Wilmington Trust Company, as collateral agent	Exhibit 4.33 to Form 10-K, filed on April 29, 2008.

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Exhibit Numbers	Description	Incorporation By Reference To
4.39	The Receivables Financing Agreement, dated as of September 21, 2004, by and among Rite Aid Funding I, as borrower, Rite Aid Hdqtrs. Funding, Inc., as collection agent, Citicorp North America, Inc., as program agent and as an investor agent, Citibank, N.A., as a bank, Wachovia Bank, National Association, as an investor agent and as a bank, JPMorgan Chase Bank, N.A. (as successor to Bank One, NA), as an investor agent and as a bank, CAFCO, LLC, as an investor, Falcon Asset Securitization Company LLC (as successor to Jupiter Securitization Corporation), as an investor, Variable Funding Capital Company LLC (as successor to Blue Ridge Asset Funding Corporation), as an investor, and Rite Aid Corporation and the companies named therein, as originators	Exhibit 10.3 to Form 10-Q, filed on September 28, 2004
4.40	Credit Agreement, dated as of February 18, 2009, among Rite Aid Funding II as the Borrower and the Lenders party thereto and Citicorp North America, Inc. as the Administrative Agent and Rite Aid Hdqtrs. Funding, Inc. as Collection Agent and each of the parties named on Schedule III thereto as Originators and Citigroup Global Markets Inc. as the Sole Lead Arranger and Sole Bookrunning Manager	Exhibit 10.1 to Form 8-K, filed on February 20, 2009
4.41	Intercreditor Agreement, dated as of February 18, 2009, by and among Citicorp North America, Inc. and Citicorp North America, Inc., and acknowledged and agreed to by Rite Aid Funding II	Exhibit 10.2 to Form 8-K, filed on February 20, 2009
10.1	1999 Stock Option Plan*	Exhibit 10.1 to Form 10-K, filed on May 21, 2001
10.2	2000 Omnibus Equity Plan*	Included in Proxy Statement dated October 24, 2000
10.3	2001 Stock Option Plan*	Exhibit 10.3 to Form 10-K, filed on May 21, 2001
10.4	2004 Omnibus Equity Plan*	Exhibit 10.4 to Form 10-K, filed on April 28, 2005
10.5	2006 Omnibus Equity Plan*	Exhibit 10 to Form 8-K, filed on January 22, 2007
10.6	Employment Agreement by and between Rite Aid Corporation and John T. Standley, dated as of September 24, 2008*	Exhibit 10.2 to Form 10-Q, filed on October 8, 2008
10.7	Employment Agreement by and between Rite Aid Corporation and Frank G. Vitrano, dated as of September 24, 2008*	Exhibit 10.3 to Form 10-Q, filed on October 8, 2008

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Exhibit Numbers	Description	Incorporation By Reference To
10.8	Employment Agreement by and between Rite Aid Corporation and Marc A. Strassler, dated as of March 9, 2009*	Filed herewith
10.9	Employment Agreement by and between Rite Aid Corporation and Robert G. Miller, dated as of April 9, 2003*	Exhibit 10.7 to Form 10-K, filed on May 2, 2003
10.10	Amendment No. 1 to Employment Agreement by and between Rite Aid Corporation and Robert G. Miller, dated as of April 28, 2005*	Exhibit 10.8 to Form 10-K, filed on April 28, 2005
10.11	Amendment No. 2 to Employment Agreement by and between Rite Aid Corporation and Robert G. Miller, dated as of April 28, 2008*	Exhibit 10.8 to Form 10-K, filed on April 29, 2008
10.12	Amendment No. 3 to Employment Agreement by and between Rite Aid Corporation and Robert G. Miller, dated as of December 23, 2008*	Exhibit 10.5 to Form 10-Q, filed on January 7, 2009
10.13	Side Agreement to Employment Agreement between Rite Aid Corporation and Robert G. Miller, dated as of November 28, 2006*	Exhibit 10.9 to Form 10-K, filed on April 29, 2008
10.14	Rite Aid Corporation Restricted Stock and Stock Option Award Agreement, made as of December 5, 1999, by and between Rite Aid Corporation and Robert G. Miller*	Exhibit 4.31 to Form 8-K, filed on January 18, 2000
10.15	Employment Agreement by and between Rite Aid Corporation and Mary F. Sammons, dated as of December 5, 1999*	Exhibit 10.2 to Form 8-K, filed on January 18, 2000
10.16	Amendment No. 1 to Employment Agreement by and between Rite Aid Corporation and Mary F. Sammons, dated as of May 7, 2001*	Exhibit 10.12 to Form 10-Q, filed on May 21, 2001
10.17	Amendment No. 2 to Employment Agreement by and between Rite Aid Corporation and Mary F. Sammons, dated as of September 30, 2003*	Exhibit 10.3 to Form 10-Q, filed on October 7, 2003
10.18	Amendment No. 3 to Employment Agreement by and between Rite Aid Corporation and Mary F. Sammons, dated as of December 30, 2008*	Exhibit 10.6 to Form 10-Q, filed on January 7, 2009
10.19	Side Agreement to Employment Agreement by and between Rite Aid Corporation and Mary F. Sammons, dated as of October 11, 2006*	Exhibit 10.14 to Form 10-K, filed on April 29, 2008
10.20	Rite Aid Corporation Restricted Stock and Stock Option Award Agreement, made as of December 5, 1999, by and between Rite Aid Corporation and Mary F. Sammons*	Exhibit 4.32 to Form 8-K, filed on January 18, 2000

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Exhibit Numbers	Description	Incorporation By Reference To
10.21	Employment Agreement by and between Rite Aid Corporation and Douglas E. Donley, dated as of August 1, 2000*	Exhibit 10.1 to Form 10-Q, filed on December 22, 2005
10.22	Amendment No. 1 to Employment Agreement by and between Rite Aid Corporation and Douglas E. Donley, dated as of December 18, 2008*	Exhibit 10.4 to Form 10-Q, filed on January 7, 2009
10.23	Rite Aid Corporation Special Executive Retirement Plan*	Exhibit 10.15 to Form 10-K, filed on April 26, 2004
10.24	Employment Agreement by and between Rite Aid Corporation and Brian Fiala, dated as of June 26, 2007*	Exhibit 10.1 to Form 10-Q, filed on July 12, 2007
10.25	Amendment No. 1 to Employment Agreement by and between Rite Aid Corporation and Brian Fiala, dated as of December 18, 2008*	Exhibit 10.3 to Form 10-Q, filed on January 7, 2009
10.26	Employment Agreement by and between Rite Aid Corporation and Ken Martindale, dated as of December 3, 2008*	Exhibit 10.7 to Form 10-Q, filed on January 7, 2009
10.27	Supply Agreement by and between Rite Aid Corporation and McKesson Corporation, dated as of December 22, 2003**	Exhibit 10.25 to Form 10-K, filed on April 29, 2008
10.28	First Amendment to Supply Agreement by and between Rite Aid Corporation and McKesson Corporation, dated as of December 8, 2007**	Exhibit 10.26 to Form 10-K, filed on April 29, 2008
10.29	Second Amendment to Supply Agreement by and between Rite Aid Corporation and McKesson Corporation, dated as of November 7, 2008**	Exhibit 10.1 to Form 10-Q, filed on January 7, 2009
10.30	Third Amendment to Supply Agreement by and between Rite Aid Corporation and McKesson Corporation, dated as of February 1, 2009**	Filed herewith
10.31	Management Services Agreement by and between Rite Aid Corporation and Leonard Green & Partners, L.P., dated as of January 1, 2003	Exhibit 10.27 to Form 10-K, filed on April 29, 2008
10.32	Fourth Amendment to Management Services Agreement by and between Rite Aid Corporation and Leonard Green & Partners, L.P., dated as of February 12, 2007	Exhibit 10.28 to Form 10-K, filed on April 29, 2008
11	Statement regarding computation of earnings per share	Filed herewith (see note 3 to the consolidated financial statements)
12	Statement regarding computation of ratio of earnings to fixed charges	Filed herewith

21 Subsidiaries of the Registrant

Filed herewith

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Exhibit Numbers	Description	Incorporation By Reference To
23	Consent of Independent Registered Public Accounting Firm	Filed herewith
31.1	Certification of CEO pursuant to Rule 13a-14(a) /15d-14 (a) under the Securities Exchange Act of 1934	Filed herewith
31.2	Certification of CFO pursuant to Rule 13a-14 (a) /15d-14 (a) under Securities Exchange Act of 1934	Filed herewith
32	Certification of CEO and CFO pursuant to 18 U.S.C., Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith

*
Constitutes a compensatory plan or arrangement required to be filed with this Form 10-K.

**
Confidential portions of these Exhibits were redacted and filed separately with the Securities and Exchange Commission pursuant to requests for confidential treatment.

In reviewing the agreements included as exhibits to this Annual Report on Form 10-K please remember they are included to provide you with information regarding their terms and are not intended to provide any other factual or disclosure information about Rite Aid Corporation, its subsidiaries or the other parties to the agreements. The agreements contain representations and warranties by each of the parties to the applicable agreement. These representations and warranties have been made solely for the benefit of the other parties to the applicable agreement and:

should not in all instances be treated as categorical statements of fact, but rather as a way of allocating the risk to one of the parties if those statements prove to be inaccurate;

have been qualified by disclosures that were made to the other party in connection with the negotiation of the applicable agreement, which disclosures are not necessarily reflected in the agreement;

*may apply standards of materiality in a way that is different from what may be viewed as material to you or other investors;
and*

were made only as of the date of the applicable agreement or such other date or dates as may be specified in the agreement and are subject to more recent developments.

Accordingly, these representations and warranties may not describe the actual state of affairs as of the date they were made or at any other time. Additional information about Rite Aid Corporation may be found elsewhere in this report and the Company's other public filings, which are available without charge through the SEC's website at <http://www.sec.gov>.

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of
Rite Aid Corporation
Camp Hill, Pennsylvania

We have audited the accompanying consolidated balance sheets of Rite Aid Corporation and subsidiaries (the "Company") as of February 28, 2009 and March 1, 2008, and the related consolidated statements of operations, stockholders' (deficit) equity, and cash flows for each of the three years in the period ended February 28, 2009. Our audits also included the financial statement schedule listed in the Index at Item 15(a)(2). These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Rite Aid Corporation and subsidiaries as of February 28, 2009 and March 1, 2008, and the results of their operations and their cash flows for each of the three years in the period ended February 28, 2009, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of February 28, 2009, based on the criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 16, 2009 expressed an unqualified opinion on the Company's internal control over financial reporting.

Deloitte & Touche LLP
Philadelphia, Pennsylvania
April 16, 2009

RITE AID CORPORATION AND SUBSIDIARIES**CONSOLIDATED BALANCE SHEETS****(In thousands, except per share amounts)**

	February 28, 2009	March 1, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 152,035	\$ 155,762
Accounts receivable, net	526,742	665,971
Inventories, net	3,509,494	3,936,827
Prepaid expenses and other current assets	176,661	163,334
Total current assets	4,364,932	4,921,894
Property, plant and equipment, net	2,587,356	2,873,009
Goodwill		1,783,372
Other intangibles, net	1,017,011	1,187,327
Deferred tax assets		384,163
Other assets	357,241	338,258
Total assets	\$ 8,326,540	\$ 11,488,023
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY		
Current liabilities:		
Current maturities of long-term debt and lease financing obligations	\$ 40,683	\$ 185,609
Accounts payable	1,256,982	1,425,768
Accrued salaries, wages and other current liabilities	1,004,762	1,110,288
Deferred tax liabilities		76,374
Total current liabilities	2,302,427	2,798,039
Long-term debt, less current maturities	5,801,230	5,610,489
Lease financing obligations, less current maturities	169,796	189,426
Other noncurrent liabilities	1,252,739	1,178,884
Total liabilities	9,526,192	9,776,838
Commitments and contingencies		
Stockholders' (deficit) equity:		
Preferred stock series G, par value \$1 per share; liquidation value \$100 per share; 2,000 shares authorized; shares issued .006 and 1,393	1	139,253
Preferred stock series H, par value \$1 per share; liquidation value \$100 per share; 2,000 shares authorized; shares issued 1,435 and 1,352	143,498	135,202
Preferred stock series I, par value \$1 per share; liquidation value \$25 per share; 5,200 shares authorized; shares issued 0 and 4,820		116,415
Common stock, par value \$1 per share; 1,500,000 shares authorized; shares issued and outstanding 886,113 and 830,209	886,113	830,209
Additional paid-in capital	4,265,211	4,047,499
Accumulated deficit	(6,452,696)	(3,537,276)
Accumulated other comprehensive loss	(41,779)	(20,117)
Total stockholders' (deficit) equity	(1,199,652)	1,711,185
Total liabilities and stockholders' (deficit) equity	\$ 8,326,540	\$ 11,488,023

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

RITE AID CORPORATION AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except per share amounts)**

	February 28, 2009 (52 Weeks)	Year Ended March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Revenues	\$ 26,289,268	\$ 24,326,846	\$ 17,399,383
Costs and expenses:			
Cost of goods sold	19,253,616	17,689,272	12,710,609
Selling, general and administrative expenses	6,985,367	6,366,137	4,338,462
Goodwill impairment charge	1,810,223		
Lease termination and impairment charges	293,743	86,166	49,317
Interest expense	477,627	449,596	275,219
Loss on debt modifications and retirements, net	39,905	12,900	18,662
Loss (gain) on sale of assets, net	11,581	(3,726)	(11,139)
	28,872,062	24,600,345	17,381,130
(Loss) income before income taxes	(2,582,794)	(273,499)	18,253
Income tax expense (benefit)	329,257	802,701	(11,609)
Net (loss) income from continuing operations	\$ (2,912,051)	\$ (1,076,200)	\$ 29,862
Loss from discontinued operations, net of gain on disposal and income tax benefit	(3,369)	(2,790)	(3,036)
Net (loss) income	\$ (2,915,420)	\$ (1,078,990)	\$ 26,826
Computation of loss applicable to common stockholders:			
Net (loss) income	\$ (2,915,420)	\$ (1,078,990)	\$ 26,826
Accretion of redeemable preferred stock	(102)	(102)	(102)
Cumulative preferred stock dividends	(21,768)	(32,533)	(31,455)
Preferred stock beneficial conversion		(556)	
Loss applicable to common stockholders	\$ (2,937,290)	\$ (1,112,181)	\$ (4,731)
Basic and diluted loss per share:			
Basic loss per share	\$ (3.49)	\$ (1.54)	\$ (0.01)
Diluted loss per share	\$ (3.49)	\$ (1.54)	\$ (0.01)

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

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RITE AID CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' (DEFICIT) EQUITY
For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007
(In thousands)

	Preferred Stock Series E		Preferred Stock Series G		Preferred Stock Series H		Preferred Stock Series I		Common Stock		Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Amount			
BALANCE														
March 4, 2006	2,500	\$ 120,000	1,212	\$ 121,207	1,200	\$ 120,020	4,820	\$ 116,074	527,667	\$ 527,667	\$ 3,114,997	\$(2,489,023)	\$(24,021)	\$ 1,606,921
Net income												26,826		26,826
Other comprehensive income:														
Minimum pension liability													6,802	6,802
Tax provision from minimum pension liability adjustment													(2,813)	(2,813)
Comprehensive income														30,815
Adjustment to initially apply FAS No. 158, net of tax benefit of \$2,560 (see Note 15)													(3,627)	(3,627)
Exchange of restricted shares for taxes									(723)	(723)	(2,421)			(3,144)
Issuance of restricted stock									4,790	4,790	(4,790)			
Cancellation of restricted stock									(972)	(972)	972			
Amortization of restricted stock balance											10,702			10,702
Stock-based compensation expense											11,630			11,630
Stock options exercised									5,924	5,924	14,462			20,386
Tax benefit from exercise of stock options											4,202			4,202
Dividends on preferred stock			87	8,710	74	7,365					(16,075)			
Adjustment to issuance costs of Series I preferred stock								341						341
Cash dividends paid on preferred shares											(15,380)			(15,380)
BALANCE	2,500	\$ 120,000	1,299	\$ 129,917	1,274	\$ 127,385	4,820	\$ 116,415	536,686	\$ 536,686	\$ 3,118,299	\$(2,462,197)	\$(23,659)	\$ 1,662,846
MARCH 3,														

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2007

Net loss											(1,078,990)	(1,078,990)	
Other comprehensive income:													
Changes in Defined Benefit Plans											6,285	6,285	
Tax provision from minimum pension liability adjustment											(2,743)	(2,743)	
Comprehensive loss												(1,075,448)	
Adjustment to initially apply FIN 48											4,467	4,467	
Issuance of shares to Jean Coutu Group						250,000	250,000	840,000				1,090,000	
Exchange of restricted shares for taxes						(1,423)	(1,423)	(7,080)				(8,503)	
Issuance of restricted stock						7,179	7,179	(7,179)					
Cancellation of restricted stock						(1,382)	(1,382)	1,382					
Amortization of restricted stock balance								21,224				21,224	
Stock-based compensation expense								19,215				19,215	
Stock options exercised						4,135	4,135	8,629				12,764	
Dividends on preferred stock	94	9,336	78	7,817				(17,153)					
Preferred stock beneficial conversion								556			(556)		
Conversion of Series E preferred stock	(2,500)	(120,000)				35,014	35,014	84,986					
Cash dividends paid on preferred shares								(15,380)				(15,380)	
BALANCE MARCH 1, 2008	\$	1,393	\$ 139,253	1,352	\$ 135,202	4,820	\$ 116,415	830,209	\$ 830,209	\$ 4,047,499	\$ (3,537,276)	\$ (20,117)	\$ 1,711,185
Net loss											(2,915,420)	(2,915,420)	
Other comprehensive income:													
Changes in Defined Benefit Plans											(21,662)	(21,662)	
Comprehensive loss												(2,937,082)	
Exchange of restricted shares for taxes						(1,741)	(1,741)	(1,113)				(2,854)	
						2,646	2,646	(2,646)					

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Issuance of restricted stock																				
Cancellation of restricted stock						(967)	(967)	967												
Amortization of restricted stock balance								17,913												17,913
Stock-based compensation expense								13,535												13,535
Stock options exercised						516	516	601												1,117
Dividends on preferred stock	100	10,006	83	8,296				(18,302)												
Conversion of Series G and I preferred stock	(1,493)	(149,258)			(4,820)	(116,415)	55,450	55,450	210,223											
Cash dividends paid on preferred shares									(3,466)											(3,466)
BALANCE																				
FEBRUARY																				
28, 2009	\$	\$	1	1,435	\$ 143,498	\$	886,113	\$ 886,113	\$ 4,265,211	\$ (6,452,696)	\$ (41,779)	\$ (1,199,652)								

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

RITE AID CORPORATION AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF CASH FLOWS****(In thousands)**

	February 28, 2009 (52 Weeks)	Year Ended March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
OPERATING ACTIVITIES:			
Net (loss) income	\$(2,915,420)	\$(1,078,990)	\$ 26,826
Adjustments to reconcile to net cash provided by operating activities:			
Depreciation and amortization	586,208	472,473	270,307
Goodwill impairment charge	1,810,223		
Lease termination and impairment charges	293,743	86,166	49,317
LIFO charges	184,569	16,114	43,006
Loss (gain) on sale of assets, net	11,629	(11,826)	(11,139)
Stock-based compensation expense	31,448	40,439	22,331
Loss on debt modifications and retirements, net	39,905	12,900	18,662
Changes in deferred taxes	307,789	805,204	(13,362)
Proceeds from sale of inventory		16,811	
Proceeds from insured loss		8,550	593
Changes in operating assets and liabilities:			
Net proceeds from accounts receivable securitization	104,881	85,000	20,000
Accounts receivable	33,784	36,820	(39,543)
Inventories	196,517	(306,360)	(37,275)
Accounts payable	(140,258)	(115,624)	14,219
Other assets and liabilities, net	(185,108)	11,691	(54,797)
Net cash provided by operating activities	359,910	79,368	309,145
INVESTING ACTIVITIES:			
Payments for property, plant and equipment	(460,857)	(687,529)	(334,485)
Intangible assets acquired	(80,489)	(52,846)	(29,243)
Acquisition of Jean Coutu, USA, net of cash acquired	(112)	(2,306,774)	(18,369)
Proceeds from sale-leaseback transactions	161,553	48,985	55,563
Proceeds from dispositions of assets and investments	33,547	58,470	9,348
Proceeds from insured loss		5,950	4,406
Net cash used in investing activities	(346,358)	(2,933,744)	(312,780)
FINANCING ACTIVITIES:			
Proceeds from issuance of long-term debt	900,629	2,307,867	1,145,000
Net (payments to) proceeds from revolver	(11,000)	549,000	(234,000)
Proceeds from financing secured by owned property	31,266	44,267	26,527
Principal payments on long-term debt	(870,054)	(15,939)	(901,297)
Change in zero balance cash accounts	(16,298)	79,606	15,662
Net proceeds from the issuance of common stock	1,117	12,764	20,386
Payments for preferred stock dividends	(3,466)	(15,380)	(15,380)
Excess tax deduction on stock options			1,587
Deferred financing costs paid	(49,473)	(58,195)	(24,769)
Net cash (used in) provided by financing activities	(17,279)	2,903,990	33,716

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(Decrease) increase in cash and cash equivalents	(3,727)	49,614	30,081
Cash and cash equivalents, beginning of year	155,762	106,148	76,067
Cash and cash equivalents, end of year	\$ 152,035	\$ 155,762	\$ 106,148

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

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****1. Summary of Significant Accounting Policies***Description of Business*

The Company is a Delaware corporation and through its wholly-owned subsidiaries, operates retail drugstores in the United States of America. It is one of the largest retail drugstore chains in the United States, with 4,901 stores in operation as of February 28, 2009. The Company's drugstores' primary business is pharmacy services. The Company also sells a full selection of health and beauty aids and personal care products, seasonal merchandise and a large private brand product line.

The Company's operations consist solely of the retail drug segment. Revenues are as follows:

	February 28, 2009	Year Ended March 1, 2008	March 3, 2007
	(52 Weeks)	(52 Weeks)	(52 Weeks)
Pharmacy sales	\$ 17,604,284	\$ 16,179,170	\$ 11,042,183
Front-end sales	8,581,115	8,049,446	6,272,333
Other revenue	103,869	98,230	84,867
	\$ 26,289,268	\$ 24,326,846	\$ 17,399,383

Sales of prescription drugs represented approximately 67.2%, 66.7%, and 63.7% of the Company's total sales in fiscal years 2009, 2008 and 2007, respectively. The Company's principal classes of products in fiscal 2009 were the following:

Product Class	Percentage of Sales
Prescription drugs	67.2%
Over-the-counter medications and personal care	8.7%
Health and beauty aids	5.3%
General merchandise and other	18.8%

Fiscal Year

The Company's fiscal year ends on the Saturday closest to February 29 or March 1. The fiscal years ended February 28, 2009, March 1, 2008 and March 3, 2007 included 52 weeks.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and all of its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand and highly liquid investments, which are readily convertible to known amounts of cash and which have original maturities of three months or less when purchased.

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

1. Summary of Significant Accounting Policies (Continued)

Allowance for Uncollectible Receivables

Approximately 96% of prescription sales are made to customers that are covered by third-party payors, such as insurance companies, government agencies and employers. The Company recognizes receivables that represent the amount owed to the Company for sales made to customers or employees of those payors that have not yet been paid. The Company maintains a reserve for the amount of these receivables deemed to be uncollectible. This reserve is calculated based upon historical collection activity adjusted for current conditions.

Inventories

Inventories are stated at the lower of cost or market. Inventory balances include the capitalization of certain costs related to purchasing, freight and handling costs associated with placing inventory in its location and condition for sale. The Company uses the last-in, first-out ("LIFO") method of accounting for substantially all of its inventories. At February 28, 2009 and March 1, 2008, inventories were \$746,467 and \$562,728, respectively, lower than the amounts that would have been reported using the first-in, first-out ("FIFO") method. The Company calculates its FIFO inventory valuation using the retail method for store inventories and the cost method for distribution facility inventories. The LIFO charge was \$184,569, \$16,114 and \$43,006 for fiscal years 2009, 2008, and 2007, respectively.

Impairment of Long-Lived Assets

Asset impairments are recorded when the carrying value of assets are not recoverable. For purposes of recognizing and measuring impairment of long-lived assets, the Company categorizes assets of operating stores as "Assets to Be Held and Used" and assets of stores that have been closed as "Assets to Be Disposed Of". The Company evaluates assets at the store level because this is the lowest level of identifiable cash flows ascertainable to evaluate impairment. Assets being tested for recoverability at the store level include tangible long-lived assets and identifiable, finite-lived intangibles that arose in purchase business combinations. Corporate assets to be held and used are evaluated for impairment based on excess cash flows from the stores that support those assets.

The Company reviews long-lived assets to be held and used for impairment annually or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the sum of the undiscounted expected future cash flows is less than the carrying amount of the asset, the Company recognizes an impairment loss. Impairment losses are measured as the amount by which the carrying amount of the asset exceeds the fair value of the asset. When fair values are not available, the Company estimates fair value using the expected future cash flows discounted at a rate commensurate with the risks associated with the recovery of the asset.

Property, Plant and Equipment

Property, plant and equipment are stated at cost, net of accumulated depreciation and amortization. The Company provides for depreciation using the straight-line method over the following useful lives: buildings 30 to 45 years; equipment 3 to 15 years.

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

1. Summary of Significant Accounting Policies (Continued)

Leasehold improvements are amortized on a straight-line basis over the shorter of the estimated useful life of the asset or the term of the lease. When determining the amortization period of a leasehold improvement, the Company considers whether discretionary exercise of a lease renewal option is reasonably assured. If it is determined that the exercise of such option is reasonably assured, the Company will amortize the leasehold improvement asset over the minimum lease term, plus the option period. This determination depends on the remaining life of the minimum lease term and any economic penalties that would be incurred if the lease option is not exercised.

Capitalized lease assets are recorded at the lesser of the present value of minimum lease payments or fair market value and amortized over the estimated useful life of the related property or term of the lease.

The Company capitalizes direct internal and external development costs and direct external application development costs associated with internal-use software. Neither preliminary evaluation costs nor costs associated with the software after implementation are capitalized. For fiscal years 2009, 2008 and 2007, the Company capitalized costs of approximately \$4,990, \$3,399 and \$4,956, respectively.

Intangible Assets

The Company has certain finite-lived intangible assets that are amortized over their useful lives. The value of favorable and unfavorable leases on stores acquired in business combinations are amortized over the terms of the leases on a straight-line basis. Prescription files acquired in business combinations are amortized over an estimated useful life of ten years on an accelerated basis, which approximates the anticipated prescription file retention and related cash flows. Purchased prescription files acquired in other than business combinations are amortized over their estimated useful lives of five years on a straight line basis.

Revenue Recognition

For all sales other than third party pharmacy sales, the Company recognizes revenue from the sale of merchandise at the time the merchandise is sold. For third party pharmacy sales, revenue is recognized at the time the prescription is filled, which is or approximates when the customer picks up the prescription. The Company records revenue net of an allowance for estimated future returns. Return activity is immaterial to revenues and results of operations in all periods presented.

Cost of Goods Sold

Cost of goods sold includes the following: the cost of inventory sold during the period, including related vendor rebates and allowances, LIFO charges, costs incurred to return merchandise to vendors, inventory shrink costs, purchasing costs and warehousing costs which include inbound freight costs from the vendor, distribution payroll and benefit costs, distribution center occupancy costs and depreciation expense and delivery expenses to the stores.

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

1. Summary of Significant Accounting Policies (Continued)

Vendor Rebates and Allowances

Rebates and allowances received from vendors relate to either buying and merchandising or promoting the product. Buying and merchandising related rebates and allowances are recorded as a reduction of cost of goods sold as product is sold. Buying and merchandising rebates and allowances include all types of vendor programs such as cash discounts from timely payment of invoices, purchase discounts or rebates, volume purchase allowances, price reduction allowances and slotting allowances. Certain product promotion related rebates and allowances, primarily related to advertising, are recorded as a reduction in selling, general and administrative expenses when the advertising commitment has been satisfied.

Rent

The Company records rent expense on operating leases on a straight-line basis over the minimum lease term. The Company begins to record rent expense at the time that the Company has the right to use the property. From time to time, the Company receives incentive payments from landlords that subsidize lease improvement construction. These leasehold incentives are deferred and recognized on a straight-line basis over the minimum lease term.

Selling, General and Administrative Expenses

Selling, general and administrative expenses include store and corporate administrative payroll and benefit costs, occupancy costs which include retail store and corporate rent costs, facility and leasehold improvement depreciation and utility costs, advertising, repair and maintenance, insurance, equipment depreciation and professional fees.

Repairs and Maintenance

Routine repairs and maintenance are charged to operations as incurred. Improvements and major repairs, which extend the useful life of an asset, are capitalized and depreciated.

Advertising

Advertising costs, net of specific vendor advertising allowances, are expensed in the period the advertisement first takes place. Advertising expenses, net of vendor advertising allowances, for fiscal 2009, 2008 and 2007 were \$375,790, \$375,025 and \$295,232, respectively.

Insurance

The Company is self-insured for certain general liability and workers' compensation claims. For claims that are self-insured, stop-loss insurance coverage is maintained for workers' compensation occurrences exceeding \$750 and general liability occurrences exceeding \$2,000. The Company utilizes actuarial studies as the basis for developing reported claims and estimating claims incurred but not reported relating to the Company's self-insurance. Workers' compensation claims are discounted to present value using a risk-free interest rate.

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

1. Summary of Significant Accounting Policies (Continued)

A majority of the Company-sponsored associate medical plans are self-insured. The remaining Company-sponsored associate medical plans are covered through guaranteed cost contracts.

Benefit Plan Accruals

The Company has several defined benefit plans, under which participants earn a retirement benefit based upon a formula set forth in the plan. The Company records expense related to these plans using actuarially determined amounts that are calculated under the provisions of SFAS No. 87, "Employer's Accounting for Pensions". Key assumptions used in the actuarial valuations include the discount rate, the expected rate of return on plan assets and the rate of increase in future compensation levels.

Stock-Based Compensation

The Company has several stock option plans, which are described in detail in Note 15. The Company accounts for stock-based compensation under SFAS No. 123(R), "Share-Based Payment", which requires companies to account for share-based payments to associates using the fair value method of expense recognition. Fair value for stock options can be calculated using either a closed form or open form calculation method. SFAS No. 123(R) requires companies to recognize option expense over the requisite service period of the award, net of an estimate for the impact of award forfeitures.

The Company adopted SFAS No. 123(R) effective March 5, 2006 using the modified prospective transition method. The Company had previously adopted the provisions of SFAS No. 123, "Accounting for Stock-Based Compensation" effective March 2, 2003 and had been recognizing expense on a ratable basis related to share-based payments to associates using the fair value method. The adoption of SFAS No. 123(R) did not have a material impact on its financial position and results of operations.

SFAS No. 123(R) also requires the company to reclassify tax benefits realized upon the exercise of stock options in excess of that which is associated with the expense recognized for financial reporting purposes. These amounts are presented as a financing cash inflow rather than as a reduction of income taxes paid in the consolidated statement of cash flows.

Store Pre-opening Expenses

Costs incurred prior to the opening of a new or relocated store, associated with a remodeled store or related to the opening of a distribution facility are charged against earnings when incurred.

Litigation Reserves

The Company is involved in litigation on an ongoing basis. The Company accrues its best estimate of the probable loss related to legal claims. Such estimates are developed in consultation with in-house and outside counsel, and are based upon a combination of litigation and settlement strategies.

Store Closing Costs and Lease Exit Charges

When a store is closed, the Company records an expense for unrecoverable costs and accrues a liability equal to the present value at current credit adjusted risk-free interest rates of the remaining

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

1. Summary of Significant Accounting Policies (Continued)

lease obligations and anticipated ancillary occupancy costs, net of estimated sublease income. Other store closing and liquidation costs are expensed when incurred.

Income Taxes

Deferred income taxes are determined based on the difference between the financial reporting and tax bases of assets and liabilities. Deferred income tax expense (benefit) represents the change during the reporting period in the deferred tax assets and deferred tax liabilities, net of the effect of acquisitions and dispositions. Deferred tax assets include tax loss and credit carryforwards and are reduced by a valuation allowance if, based on available evidence, it is more likely than not that some portion of the deferred tax assets will not be realized. Changes in valuation allowances from period to period are included in the tax provision in the period of change.

The Company has net operating loss ("NOL") carryforwards that can be utilized to offset future income for federal and state tax purposes. These NOLs generate a significant deferred tax asset. The Company regularly reviews the deferred tax assets for recoverability considering historical profitability, projected taxable income, the expected timing of the reversals of existing temporary differences and tax planning strategies.

The Company recognizes tax liabilities in accordance with FIN 48 and management adjusts these liabilities with changes in judgement as a result of the evaluation of new information not previously available. Due to the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from the current estimate of the tax liabilities.

Sales Tax Collected

Sales taxes collected from customers and remitted to various governmental agencies are presented on a net basis (excluded from revenues) in the Company's statement of operations.

Use of Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Significant Concentrations

The Company's pharmacy sales were primarily to customers covered by health plan contracts, which typically contract with a third party payor that agrees to pay for all or a portion of a customer's eligible prescription purchases. During fiscal 2009, the top five third party payors accounted for approximately 37.3% of the Company's total sales. The largest third party payor represented 12.6%, 11.3%, and 9.4% of total sales during fiscal 2009, 2008, and 2007, respectively. Third party payors are entities such as an insurance company, governmental agency, health maintenance organization or other managed care provider, and typically represent several health care contracts and customers. During fiscal 2009, state sponsored Medicaid agencies accounted for approximately 6.6% of the Company's

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

1. Summary of Significant Accounting Policies (Continued)

total sales, the largest of which was less than 2.0% of the Company's total sales. Any significant loss of third-party payor business could have a material adverse effect on the Company's business and results of operations.

During fiscal 2009, the Company purchased brand pharmaceuticals and some generic pharmaceuticals which amounted to approximately 93.7% of the dollar volume of its prescription drugs from a single wholesaler, McKesson Corp. ("McKesson"), under a contract expiring April 2010. With limited exceptions, the Company is required to purchase all of its branded pharmaceutical products from McKesson. If the Company's relationship with McKesson was disrupted, the Company could have temporary difficulty filling prescriptions until a replacement wholesaler agreement was executed, which would negatively impact the business.

Certain Business Risks and Management's Plans

The U.S. economy is currently in a recession and a period of unprecedented volatility, and the future economic environment may continue to be less favorable than that of recent years. The Company is highly leveraged and its substantial indebtedness could limit cash flow available for operations and could adversely affect its ability to service debt or obtain additional financing. As a result of the current condition of the credit markets, the Company may not be able to obtain additional financing on favorable terms, or at all. If the Company's operating results, cash flow or capital resources prove inadequate, or if interest rates rise significantly, the Company could face substantial liquidity problems and might be required to dispose of material assets or operations to meet its debt and other obligations or otherwise be required to delay its planned activities.

Management believes that the Company has adequate sources of liquidity to meet its anticipated requirements for working capital, debt service and capital expenditures through fiscal 2010. The Company's \$1,750,000 revolving credit facility, of which \$838,000 was outstanding at February 28, 2009, and the Company's \$145,000 Tranche 1 term loan mature on September 30, 2010. The Company intends to refinance these facilities prior to their maturity dates and expects these efforts to be successful. However, there can be no assurance that the Company will be able to refinance these facilities on terms acceptable to it.

If the Company does not meet the New York Stock Exchange continued listing requirements, its common stock may be delisted. Upon such an event, the Company may be required to repurchase or refinance its 8.5% convertible note due 2015. The senior secured credit facility and accounts receivable securitization facilities provide that the triggering of this repurchase right constitutes a default under such facilities. To avoid such a scenario, the Company may seek to refinance the Convertible Notes or affect a reverse stock split. See Note 11 for more information on the continued listing requirement of the Company's common stock and management's plans with respect thereto.

Derivatives

The Company may enter into interest rate swap agreements to hedge the exposure to increasing rates with respect to its variable rate debt, when the Company deems it prudent to do so. Upon inception of interest rate swap agreements, or modifications thereto, the Company performs a comprehensive review of the interest rate swap agreements based on the criteria as provided by SFAS

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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(In thousands, except per share amounts)

1. Summary of Significant Accounting Policies (Continued)

No. 133, "Accounting for Derivative Instruments and Hedging Activities", as amended by SFAS No. 138. As of February 28, 2009 and March 1, 2008, the Company had no interest rate swap arrangements or other derivatives.

Discontinued Operations

For purposes of determining discontinued operations, the Company has determined that the store level is a component of the entity within the context of SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets". A component of an entity comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the Company. The Company routinely evaluates its store base and closes non-performing stores. The Company evaluates the results of operations of these closed stores both quantitatively and qualitatively to determine if appropriate for reporting as discontinued operations. Stores sold where the Company retains the prescription files are excluded from the analysis as the Company retains direct cash flows resulting from the migration of revenue to existing stores.

Recent Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements". This standard establishes a standard definition for fair value, establishes a framework under generally accepted accounting principles for measuring fair value and expands disclosure requirements for fair value measurements. This standard is effective for financial statements issued for fiscal years beginning after November 15, 2007. In December 2007, a FASB Staff Position (FSP) was proposed, and subsequently approved, to delay the effective dates of SFAS No. 157 as it relates to all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis, or at least annually. The Company has adopted SFAS No. 157 as of March 2, 2008 as it relates to financial assets and liabilities and there was no impact on the financial statements. The Company will adopt SFAS No. 157 as it relates to nonfinancial assets and liabilities in the quarter ending May 30, 2009 and does not expect the adoption to have a material impact on its financial position or results of operations.

In December 2007, the FASB issued SFAS No. 141 (Revised) "Business Combinations". SFAS 141 (Revised) establishes principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the assets acquired and liabilities assumed in a business combination, and makes several changes to the method of accounting for business combinations previously set forth in SFAS No. 141. SFAS No. 141 (Revised) will become effective for acquisitions consummated in fiscal years beginning after December 15, 2008.

2. Acquisition

On June 4, 2007, the Company acquired all of the membership interests of JCG (PJC) USA, LLC ("Jean Coutu USA"), the holding company for the Brooks Eckerd drugstore chain ("Brooks Eckerd"), from Jean Coutu Group (PJC) Inc. ("Jean Coutu Group"), pursuant to the terms of the Stock Purchase Agreement (the "Agreement") dated August 23, 2006. As consideration for the acquisition of Jean Coutu USA (the "Acquisition"), the Company paid \$2,307,747 and issued 250,000

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

2. Acquisition (Continued)

shares of Rite Aid common stock. The Company financed the cash payment via the establishment of a new term loan facility, issuance of senior notes and borrowings under its existing revolving credit facility. The consideration associated with the common stock was \$1,090,000 based on a stock price of \$4.36 per share, representing the average closing price of Rite Aid common stock beginning two days prior to the announcement of the Acquisition on August 24, 2006 and ending two days after the announcement.

At February 28, 2009 the Jean Coutu Group owned approximately 27.6% of total Rite Aid voting power. The Company expanded its Board of Directors to 14 members, with four of the seats being held by members designated by the Jean Coutu Group. In connection with the Acquisition, the Company entered into a Stockholder Agreement (the "Stockholder Agreement") with Jean Coutu Group and certain Coutu family members. The Stockholder Agreement contains provisions relating to Jean Coutu Group's ownership interest in the Company, board and board committee composition, corporate governance, stock ownership, stock purchase rights, transfer restrictions, voting arrangements and other matters. The Company and Jean Coutu Group also entered into a Registration Rights Agreement giving Jean Coutu Group certain rights with respect to the registration under the Securities Act of 1933, as amended, of the shares of Rite Aid common stock issued to Jean Coutu Group or acquired by Jean Coutu Group pursuant to certain stock purchase rights or open market rights under the Stockholder Agreement.

As of February 28, 2009, the Company's financial statements reflect the final purchase accounting adjustments in accordance with SFAS No. 141 "Business Combinations", whereby the purchase price was allocated to the assets acquired and liabilities assumed based upon their estimated fair values on the acquisition date.

The Company's consolidated financial statements for the fiscal year ended March 1, 2008 include Brooks Eckerd results of operations for the thirty-nine week period ended March 1, 2008.

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The following table reflects the final allocation of the purchase price:

<i>Purchase price</i>	
Cash consideration	\$2,307,747
Stock consideration	1,090,000
Capitalized acquisition costs	43,376
Total	\$ 3,441,123
<i>Purchase price allocation</i>	
Cash and cash equivalents	\$ 25,838
Accounts receivable	427,234
Inventories	1,296,984
Other current assets	48,756
Total current assets	1,798,812
Property and equipment	897,640
Intangible assets(1)	1,131,550
Goodwill(2)	1,154,186
Other assets	122,740
Total assets acquired	5,104,928
Accounts payable	579,302
Deferred tax liability	21,301
Other current liabilities(3)	401,522
Total current liabilities	1,002,125
Deferred tax liability non-current	278,990
Other long-term liabilities(4)	382,690
Total liabilities assumed	1,663,805
<i>Net assets acquired</i>	\$ 3,441,123

(1) Included in intangible assets are prescription file intangibles of \$693,500 and intangible assets for operating leases with favorable market terms of \$438,050.

(2) During the quarter ended February 28, 2009, the goodwill was written off due to the fact that the market value of the Company's stock was less than the carrying value of its net assets as of February 28, 2009. See Note 9.

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- (3) Included in other current liabilities is an accrual for severance payments to associates of Brooks Eckerd who were involuntarily terminated of \$11,137.
- (4) Included in other long-term liabilities is an accrual of \$29,504 to reserve for the remaining lease liability of Brooks Eckerd stores for which the Company entered into a formal plan to close. Also included in other long-term liabilities is an intangible liability of \$143,100 for operating leases with unfavorable market terms.

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In connection with the Acquisition, the Company entered into a transition services agreement with the Jean Coudu Group. Under the terms of this agreement, Jean Coudu Group provided certain information technology, network and support services to the Company. This agreement expired in September 2008. The Company recorded an expense of \$894 and \$4,085 for services provided under this agreement for the years ended February 28, 2009 and March 1, 2008, respectively.

The following *unaudited* pro forma consolidated financial data gives effect to the Acquisition as if it had occurred as of the beginning of the periods presented.

	Year Ended	
	March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Net revenues	\$ 26,747,000	\$ 27,315,600
Net loss	(1,133,300)	(79,800)
Basic loss per share	\$ (1.57)	\$ (0.14)
Diluted loss per share	\$ (1.57)	\$ (0.14)

The pro forma combined information assumes the acquisition of Brooks Eckerd occurred at the beginning of each period presented. These results have been prepared by combining the historical results of the Company and historical results of Brooks Eckerd. The pro forma financial data for all periods presented include adjustments to reflect the incremental interest expense that results from the incurrence of the additional debt to finance the acquisition and additional depreciation and amortization expense resulting from the purchase price allocation. The pro forma information for the fiscal year ended March 1, 2008 includes charges of \$154,222 resulting from the integration of the Brooks Eckerd stores. Pro forma results for periods prior to the acquisition have not been adjusted to reflect the divestiture of stores required by the FTC.

The pro forma information does not purport to be indicative of the results that actually would have been achieved if the operations were combined during the periods presented and is not intended to be a projection of future results or trends.

3. Loss Per Share

Basic loss per share is computed by dividing loss available to common stockholders by the weighted average number of shares of common stock outstanding for the period. Diluted loss per share reflects the potential dilution that could occur if securities or other contracts to issue common stock

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were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the income of the Company subject to anti-dilution limitations.

	Year Ended		
	February 28, 2009 (52 Weeks)	March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Numerator for loss per share:			
Net (loss) income	\$(2,915,420)	\$(1,078,990)	\$ 26,826
Accretion of redeemable preferred stock	(102)	(102)	(102)
Cumulative preferred stock dividends	(21,768)	(32,533)	(31,455)
Preferred stock beneficial conversion		(556)	
Loss attributable to common stockholders basic and diluted	\$(2,937,290)	\$(1,112,181)	\$ (4,731)
 Denominator:			
Basic and diluted weighted average shares	840,812	723,923	524,460
Basic and diluted loss per share:			
Basic and diluted loss per share	\$ (3.49)	\$ (1.54)	\$ (0.01)

Due to their antidilutive effect, the following potential common shares have been excluded from the computation of diluted loss per share as of February 28, 2009, March 1, 2008 and March 3, 2007:

	Year Ended		
	February 28, 2009 (52 Weeks)	March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Stock options	70,162	64,662	60,596
Convertible preferred stock	26,091	77,163	94,291
Convertible debt	61,045		
	157,298	141,825	154,887

Also excluded from the computation of diluted loss per share as of February 28, 2009, March 1, 2008 and March 3, 2007 are restricted shares of 6,515, 9,395, and 7,355 which are included in shares outstanding.

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Lease termination and impairment charges consisted of:

	Year Ended		
	February 28, 2009 (52 Weeks)	March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Impairment charges	\$ 157,334	\$ 30,823	\$ 31,425
Store and equipment lease exit charges	136,409	55,343	17,892
	\$ 293,743	\$ 86,166	\$ 49,317

Impairment Charges

In fiscal 2009, 2008, and 2007, store closing and impairment charges included non-cash charges of \$157,334, \$30,823 and \$31,425, respectively, for the total or partial impairment of long-lived assets at 814, 420 and 342 stores, respectively. These amounts included the write-down of long-lived assets at stores that were assessed for impairment because of management's intention to relocate or close the store, or because of changes in circumstances that indicate the carrying value of an asset may not be recoverable. The increase in impairment charges in fiscal 2009 was triggered by current and projected operating results primarily at certain of the Company's Brooks Eckerd stores not being sufficient to cover the asset values at these stores.

Store and Equipment Lease Exit Charges

During fiscal 2009, 2008, and 2007, the Company recorded charges for 161, 66 and 49 stores, respectively, to be closed or relocated under long term leases. Charges to close a store, which principally consist of lease termination costs, are recorded at the time the store is closed and all inventory is liquidated, pursuant to the guidance set forth in SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". The Company calculates its liability for closed stores on a store-by-store basis. The calculation includes the discounted effect of future minimum lease payments and related ancillary costs, from the date of closure to the end of the remaining lease term, net of estimated cost recoveries that may be achieved through subletting properties or through favorable lease terminations. The Company evaluates these assumptions each quarter and adjusts the liability accordingly.

The following table reflects the closed store charges that relate to new closures, changes in assumptions and interest accretion. The table also reflects the increase in the closed store reserve related to the acquisition of 183 closed stores from Jean Coutu USA as well as the additional liability related to 65 stores that Company management planned to close at that time as a result of the acquisition in the fiscal year ended March 1, 2008. These liabilities represent the estimated fair value of

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the respective store lease commitments as of the date of the acquisition and therefore were recorded as part of allocation of the purchase price of Jean Coutu USA.

	Year Ended		
	February 28, 2009 (52 Weeks)	March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Balance beginning of year	\$ 329,682	\$ 195,205	\$ 208,455
Provision for present value of noncancellable lease payments of closed stores	97,667	27,464	14,288
Changes in assumptions about future sublease income, terminations and change of interest rate	20,947	16,482	(4,283)
Reversals of reserves for stores that management has determined will remain open		(1,465)	(812)
Interest accretion	19,837	13,874	9,274
Leased properties of Jean Coutu USA closed or designated to be closed		133,864	
Cash payments, net of sublease income	(86,722)	(55,742)	(31,717)
Balance end of year	\$ 381,411	\$ 329,682	\$ 195,205

The Company's revenues and income before income taxes for fiscal 2009, 2008, and 2007 included results from stores that have been closed or are approved for closure as of February 28, 2009. The revenue and operating losses of these stores for the periods are presented as follows:

	Year Ended		
	February 28, 2009 (52 Weeks)	March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Revenues	\$ 538,108	\$ 1,060,858	\$ 897,666
(Loss) income from operations	(67,157)	(35,721)	(6,151)

Included in loss from operations for fiscal 2009, 2008, and 2007 are depreciation and amortization charges of \$7,359, \$14,350 and \$7,750, respectively, and closed store inventory liquidation charges of \$9,881, \$6,193 and \$5,416, respectively. Also included in loss from operations for fiscal 2009 and 2008 are losses on the sale of assets of \$13,620 and \$2,854, respectively, and for fiscal 2007, the loss from operations includes a gain on the sale of assets of \$2,647. Loss from operations does not include any allocation of corporate level overhead costs. The above results are not necessarily indicative of the impact that these closures will have on revenues and operating results of the Company in the future, as the Company often transfers the business of a closed store to another Company store, thereby retaining a portion of these revenues. The amounts indicated above do not include the results of operations for stores closed related to discontinued operations.

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****5. Discontinued Operations**

During the fourth quarter of fiscal 2008, the Company entered into agreements to sell the prescription files of 28 of its stores in the Las Vegas Nevada area. The Company owned four of these stores and the remaining stores were leased. The Company assigned the lease rights of 17 of those stores to other entities and closed the remaining leased stores. The Company has sold two of the owned stores and plans to sell the remaining two owned stores. The sale and transfer of the prescription files has been completed and the inventory at the stores has been liquidated.

The Company has presented the operating results of and the gain on the sale of Las Vegas as a discontinued operation in the statement of operations for all fiscal years presented. The following amounts have been segregated from continuing operations and included in discontinued operations:

	Year Ended		
	February 28,	March 1,	March 3,
	2009	2008	2007
	(52	(52	(52
	Weeks)	Weeks)	Weeks)
	(Dollars in thousands)		
Revenues	\$ 267	\$ 90,815	\$ 108,336
Costs and expenses:			
Cost of goods sold	1,652	70,171	80,988
Selling, general and administrative expenses	1,936	33,039	32,019
Loss (gain) on sale of assets	48	(8,100)	
Total costs and expenses	3,636	95,110	113,007
Loss from discontinued operations before income taxes	(3,369)	(4,295)	(4,671)
Income tax benefit		(1,505)	(1,635)
Net loss from discontinued operations	\$ (3,369)	\$ (2,790)	\$ (3,036)

The assets and liabilities of the divested stores for the years ended February 28, 2009, March 1, 2008 and March 2, 2007 are not significant and have not been segregated in the consolidated balance sheets.

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****6. Income Taxes**

The provision for income taxes was as follows:

	Year Ended		
	February 28, 2009 (52 Weeks)	March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Current tax expense (benefit):			
Federal	\$ 165	\$ (355)	\$ 3,771
State	6,327	1,183	(3,585)
	6,492	828	186
Deferred tax expense (benefit):			
Federal	260,592	726,167	16,056
State	62,173	75,706	(27,851)
	322,765	801,873	(11,795)
Total income tax expense (benefit)	\$ 329,257	\$ 802,701	\$(11,609)

A reconciliation of the expected statutory federal tax and the total income tax benefit was as follows:

	Year Ended		
	February 28, 2009 (52 Weeks)	March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Expected federal statutory expense at 35%	\$(903,974)	\$(95,725)	\$ 6,388
Nondeductible expenses	9,445	6,476	3,460
State income taxes, net	(54,921)	(25,789)	(24,140)
Recoverable tax and reduction of previously recorded liabilities	9,737	(999)	(5,376)
Credits generated	0	(1,699)	(1,022)
Goodwill Impairment	595,856	0	0
Valuation allowance	673,114	920,437	9,081
Total income tax expense (benefit)	\$ 329,257	\$ 802,701	\$(11,609)

The income tax expense for fiscal 2009 included \$673,114 related to the increase of the valuation allowance on federal and state net deferred tax assets to offset the remaining net deferred tax asset. Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" ("SFAS No. 109") requires a company to evaluate its deferred tax assets on a regular basis to determine if a valuation allowance against the net deferred tax assets is required. According to SFAS No. 109, a cumulative loss in recent years is significant negative evidence in considering whether deferred tax assets are realizable. Based on the negative evidence, SFAS No. 109 precludes relying on projections of future taxable income to support the recognition of deferred tax assets. As such, except for tax planning strategies, the Company has not utilized projections of future taxable income to support the recognition

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****6. Income Taxes (Continued)**

of deferred tax assets. The ultimate realization of deferred tax assets is dependent upon the existence of sufficient taxable income generated in the carryforward periods.

The income tax expense for fiscal 2008 included \$920,437 related to the increase of the valuation allowance on federal and state net deferred tax assets. At March 1, 2008 the Company had a cumulative loss which was primarily due to the recently completed acquisition of Brooks Eckerd and the impact on current year earnings due to planned integration activities, compounded by the weakening economy during the later half of the year.

The income tax benefit for fiscal 2007 included a state tax benefit of \$24,140 which primarily related to an increase in the Company's state tax rate applied to the net deferred tax assets.

The tax effect of temporary differences that gave rise to significant components of deferred tax assets and liabilities consisted of the following at February 28, 2009 and March 1, 2008:

	2009	2008
Deferred tax assets:		
Accounts receivable	\$ 25,634	\$ 31,802
Accrued expenses	303,782	289,033
Liability for lease exit costs	177,837	151,519
Pension, retirement and other benefits	157,867	154,141
Long-lived assets	75,983	(86,546)
Other	5,864	4,892
Credits	74,050	71,920
Net operating losses	1,289,275	1,058,418
Total gross deferred tax assets	2,110,292	1,675,179
Valuation allowance	(1,787,798)	(1,103,973)
Total deferred tax assets	322,494	571,206
Deferred tax liabilities:		
Inventory	322,494	263,417
Total gross deferred tax liabilities	322,494	263,417
Net deferred tax assets	\$	\$ 307,789

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****6. Income Taxes (Continued)**

A reconciliation of the beginning and ending amount of unrecognized tax benefits was as follows:

Unrecognized tax benefits balance at March 1, 2008	\$233,014
Increases to prior year tax positions	5,395
Increases to prior year tax positions for Brooks Eckerd Acquisition	40,670
Decreases to tax positions in prior periods	(2,532)
Increases to current year tax positions	5,189
Settlements	(811)
Lapse of statute of limitations	(531)
Unrecognized tax benefits balance at February 28, 2009	\$280,394

Effective March 4, 2007, the Company adopted the provisions of FIN 48. As of March 4, 2007, unrecognized tax benefits totaled \$37,186, including interest and penalties. As a result of the implementation of FIN 48, the Company's tax contingencies decreased \$6,636, and after the deferred tax impact of \$2,170, the net effect was accounted for as an increase to retained earnings of \$4,466. The decrease in unrecognized tax benefits would have decreased income tax expense in prior periods.

As of June 4, 2007, with the acquisition of Brooks Eckerd, a liability and reduction of deferred tax assets of \$243,471, including tax, interest and penalties was established for uncertain tax positions. The Company is indemnified by Jean Coutu Group for certain tax liabilities incurred for all years ended up to and including June 4, 2007. Although the Company is indemnified by Jean Coutu Group, the Company remains the primary obligor to the tax authorities with respect to any tax liability arising for the years prior to the acquisition. Accordingly, as of February 28, 2009 the Company had a corresponding recoverable indemnification asset from Jean Coutu Group, included in the "Other Assets" line of the Consolidated Balance Sheets, to reflect the indemnification for such liabilities.

As of February 28, 2009 the total amount of unrecognized tax benefits that would have been recorded as an adjustment to goodwill and not impact the effective tax rate in a future period was \$243,471. However, upon the adoption of SFAS 141(R) which applies to our fiscal year 2010, changes in income tax uncertainties recorded in a business combination will also affect income tax expense and will no longer impact goodwill. Additionally, any impact on the effective rate may be mitigated by the valuation allowance that is maintained against the Company's net deferred tax assets. While it is expected that the amount of unrecognized tax benefits will change in the next twelve months, management does not expect the change to have a significant impact on the results of operations or the financial position of the Company.

The Company recognizes interest and penalties related to tax contingencies as income tax expense. Prior to the adoption of FIN 48, the Company included interest as income tax expense and penalties as an operating expense. The Company recognized expense for net interest and penalties in connection with tax matters of \$9,527 and \$238 for 2009 and 2008, respectively. As of February 28, 2009 and March 1, 2008, the total amount of accrued income tax-related interest and penalties was \$46,175 and \$33,608, respectively.

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

6. Income Taxes (Continued)

The Company files U.S. federal income tax returns as well as income tax returns in those states where it does business. The federal income tax returns are closed to examination by the Internal Revenue Service (IRS) through fiscal 2004. However, any net operating losses that were generated in these prior closed years may be subject to examination by the IRS upon utilization. The IRS is currently examining the consolidated U.S. income tax return for Brooks Eckerd for fiscal years 2004 and 2005. In FY09, the IRS completed the examination of the consolidated U.S. income tax return for Rite Aid Corporation and subsidiaries for fiscal years 2006 and 2007. State income tax returns are generally subject to examination for a period of three to five years after filing of the respective return. However, as a result of reporting IRS audit adjustments, the Company has statutes open in some states from fiscal 2003.

Net Operating Losses, Capital Losses and Tax Credits

At February 28, 2009, the Company had federal net operating loss (NOL) carryforwards of approximately \$3,099,152, the majority of which will expire, if not utilized, between fiscal 2019 and 2022.

At February 28, 2009, the Company had state NOL carryforwards of approximately \$5,572,032, the majority of which will expire between fiscal 2018 and 2026.

At February 28, 2009, the Company had federal business tax credit carryforwards of \$54,694, the majority of which will expire between 2012 and 2020. In addition to these credits, the Company has alternative minimum tax credit carryforwards of \$9,545.

Valuation Allowances

The valuation allowances as of February 28, 2009 and March 1, 2008 apply to the net deferred tax assets of the Company. The valuation allowance was increased in the third and fourth quarters of fiscal 2009. The increase for 2009 is primarily related to the impact of the current economic conditions on 2009 operating results. In the fourth quarter of 2008, a non-cash tax charge of \$920,437 was recorded to establish a valuation allowance against the net deferred tax assets. The Company maintained a valuation allowance of \$1,787,798 and \$1,103,973 against net deferred tax assets at fiscal year end 2009 and 2008, respectively.

7. Accounts Receivable

The Company maintains an allowance for doubtful accounts receivable based upon the expected collectibility of accounts receivable. The allowance for uncollectible accounts at February 28, 2009 and March 1, 2008 was \$37,490 and \$41,221, respectively. The Company's accounts receivable are due primarily from third-party payors (e.g., pharmacy benefit management companies, insurance companies or governmental agencies) and are recorded net of any allowances provided for under the respective plans. Since payments due from third-party payors are sensitive to payment criteria changes and legislative actions, the allowance is reviewed continually and adjusted for accounts deemed uncollectible by management.

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****7. Accounts Receivable (Continued)**

The Company maintains securitization agreements (the "first lien facility") with several multi-seller asset-backed commercial paper vehicles ("CPVs"). Under the terms of the first lien facility, the Company sells substantially all of its eligible third party pharmaceutical receivables to a bankruptcy remote Special Purpose Entity (SPE) and retains servicing responsibility. The assets of the SPE are not available to satisfy the creditors of any other person, including any of the Company's affiliates. These agreements provide for the Company to sell, and for the SPE to purchase these receivables. The SPE then transfers an interest in these receivables to various CPVs.

During the thirteen week period ended February 28, 2009, the Company amended certain of the terms of its first lien facility. The effect of the amendment was to make changes to the obligor concentration limits in the borrowing formula, to change the borrowing and liquidity fees charged under the first lien facility and to reduce the amount of interest in receivables that can be transferred to the CPV's to \$345,000.

Under the terms of the first lien facility, the total amount of interest in receivables that could be transferred to the CPVs was \$345,000 and \$650,000 at February 28, 2009 and March 1, 2008, respectively. The amount of transferred receivables outstanding at any one time is dependent upon a formula that takes into account such factors as default history, obligor concentrations and potential dilution ("Securitization Formula"). Adjustments to this amount can occur, at the discretion of the CPV's, on a weekly basis. At February 28, 2009 and March 1, 2008, the total of outstanding receivables that have been transferred to the CPVs were \$330,000 and \$435,000, respectively. The following table details receivable transfer activity for the years presented:

	February 28, 2009 (52 Weeks)	Year Ended March 1, 2008 (52 Weeks)	March 3, 2007 (52 Weeks)
Average amount of outstanding receivables transferred	\$ 471,319	\$ 332,115	\$ 334,588
Total receivable transfers	\$ 6,940,000	\$ 4,992,000	\$ 4,674,000
Collections made by the Company as part of the servicing arrangement on behalf of the CPVs	\$ 7,045,000	\$ 4,907,000	\$ 4,654,000

The Company is charged a program fee and liquidity fee under the first lien facility. The program fee is LIBOR plus 2.0% of the total amount advanced under the facility. The liquidity fee is 3.5% of the total facility commitment of \$345,000. The program and the liquidity fees are recorded as a component of selling, general and administrative expenses. Program and liquidity fees for fiscal 2009, 2008 and 2007 were \$24,903, \$22,314 and \$21,885, respectively.

Rite Aid Corporation guarantees certain performance obligations of its affiliates under the first lien facility, which includes the continued servicing of such receivables, but does not guarantee the collectibility of the receivables and obligor creditworthiness. The CPVs have a commitment to purchase that ends January 2010 with the option to extend to September 14, 2010. Should any of the CPVs fail to renew their commitment under the first lien facility, the Company has access to a backstop credit facility, which is backed by the CPVs and which expires September 14, 2010, to provide liquidity to the Company.

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****7. Accounts Receivable (Continued)**

Proceeds from the collections under the first lien facility are submitted to an independent trustee on a daily basis. The trustee withholds any cash necessary to (1) fund amounts owed to the CPVs as a result of such collections and, (2) fund the CPVs when the Securitization Formula indicates a lesser amount of outstanding receivables transferred is warranted. The remaining collections are swept to the Company's corporate concentration account. At February 28, 2009 and March 1, 2008, the Company had \$1,801 and \$3,277 of cash respectively that is restricted for the payment of trustee fees.

On February 18, 2009, the Company issued a \$225,000 second priority accounts receivable securitization term loan (Second Lien Facility). Net proceeds from the issuance of the Second Lien Facility were used to repay approximately \$210,000 outstanding under the Company's securitization agreements and replace the borrowing availability that was decreased under the first lien facility securitization agreements. The Second Lien Facility has a second priority interest in eligible third party receivables. This interest is subordinate to the interest of the securitization banks.

The Second Lien Facility was sold at a discount of 3% and bears interest at a rate of either, at the Company's option, (a) a base rate equal to the higher of (i) Citibank's base rate, (ii) the federal funds rate plus 0.50% per annum or (iii) an adjusted LIBO rate plus 1.0% per annum, in each case plus 11% or (b) LIBOR plus 12% with a LIBOR floor of 3%. The Second Lien Facility will mature on September 14, 2010. The Company incurred one-time issuance fees of approximately \$8,800 related to the Second Lien Facility, which are recorded in selling, general and administrative expenses. For fiscal 2009, financing fees related to the Second Lien Facility were \$1,161.

The Company has determined that the transactions under the first lien facility and Second Lien Facility meet the criteria for sales treatment in accordance with SFAS No. 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities". Additionally, the Company has determined that it does not hold a variable interest in the CPVs or in the lenders in the Second Lien Facility, pursuant to the guidance in FIN 46R, "Consolidation of Variable Interest Entities", and therefore has determined that the de-recognition of the transferred receivables is appropriate.

At February 28, 2009 and March 1, 2008, the Company's interest in the third party pharmaceutical receivables is as follows:

	February 28, 2009	March 1, 2008
Third party pharmaceutical receivables	\$ 955,827	\$ 963,683
Allowance for uncollectible accounts	(31,421)	(34,850)
Net third party receivables	924,406	928,833
First lien facility	(330,000)	(435,000)
Second lien facility (net of discount of \$6,621)	(218,379)	
Net retained interest	\$ 376,027	\$ 493,833

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****8. Property, Plant and Equipment**

Following is a summary of property, plant and equipment, including capital lease assets, at February 28, 2009 and March 1, 2008:

	2009	2008
Land	\$ 280,391	\$ 358,849
Buildings	798,048	902,281
Leasehold improvements	1,623,136	1,557,125
Equipment	2,239,935	2,021,478
Construction in progress	89,552	239,061
	5,031,062	5,078,794
Accumulated depreciation	(2,443,706)	(2,205,785)
Property, plant and equipment, net	\$ 2,587,356	\$ 2,873,009

Depreciation expense, which included the depreciation of assets recorded under capital leases, was \$383,671, \$309,270 and \$230,168 in fiscal 2009, 2008 and 2007, respectively.

Included in property, plant and equipment was the carrying amount of assets to be disposed of totaling \$33,386 and \$23,908 at February 28, 2009 and March 1, 2008, respectively.

9. Goodwill and Other Intangibles

The Company accounts for goodwill under the guidance set forth in SFAS No. 142, which specifies that goodwill should not be amortized. The Company's policy is to evaluate goodwill for impairment on an annual basis at the end of its fiscal year or more frequently if events or circumstances occur that would indicate a reduction in the fair value of the Company. On February 28, 2009, the carrying value of the Company's net assets, before goodwill impairment testing, was \$610,571 and the market capitalization of the Company's outstanding shares, assuming conversion of outstanding preferred shares, was \$255,417. Accordingly, management performed a goodwill impairment test in accordance with SFAS 142. Management determined the estimated fair value of the Company by using the quoted market value of its common stock for the trading days in the quarterly period ended February 28, 2009. The Company's market value of its common stock, after consideration of a control premium, traded below book value for every trading day in the quarterly period ended February 28, 2009. Based on the length of time that the Company's carrying value has exceeded its market value, management has concluded that the carrying value of the Company exceeds its market value. Management has performed a step two test which values the net assets of the Company as if a purchase combination had occurred. The fair value of the Company's net assets indicates that the entire amount of recorded goodwill should be impaired as of February 28, 2009. Accordingly, goodwill has been written down to zero as of February 28, 2009.

As of February 28, 2009 and March 1, 2008 the Company had goodwill of \$0 and \$1,783,372, respectively and no other indefinite life intangibles.

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The Company's remaining intangible assets are finite-lived and amortized over their useful lives. Following is a summary of the Company's intangible assets as of February 28, 2009 and March 1, 2008.

	2009			2008		
	Gross Carrying Amount	Accumulated Amortization	Remaining Weighted Average Amortization Period	Gross Carrying Amount	Accumulated Amortization	Remaining Weighted Average Amortization Period
Favorable leases and other	\$ 693,455	\$ (279,806)	11 years	\$ 738,855	\$ (240,079)	12 years
Prescription files	1,209,268	(605,906)	7 years	1,152,620	(464,069)	9 years
Total	\$ 1,902,723	\$ (885,712)		\$ 1,891,475	\$ (704,148)	

Also included in other non-current liabilities as of February 28, 2009 and March 1, 2008 are unfavorable lease intangibles with a net carrying amount of \$124,053 and \$147,035, respectively.

Amortization expense for these intangible assets and liabilities was \$202,537, \$163,201 and \$40,139 for fiscal 2009, 2008 and 2007, respectively. The anticipated annual amortization expense for these intangible assets and liabilities is 2010 \$178,293; 2011 \$164,452; 2012 \$130,516; 2013 \$105,805 and 2014 \$48,599.

10. Accrued Salaries, Wages and Other Current Liabilities

Accrued salaries, wages and other current liabilities consisted of the following at February 28, 2009 and March 1, 2008:

	2009	2008
Accrued wages, benefits and other personnel costs	\$ 393,306	\$ 392,753
Accrued sales and other taxes payable	101,083	161,820
Accrued store expense	157,047	173,516
Other	353,326	382,199
	\$ 1,004,762	\$ 1,110,288

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****11. Indebtedness and Credit Agreement**

Following is a summary of indebtedness and lease financing obligations at February 28, 2009 and March 1, 2008:

	2009	2008
Secured Debt:		
Senior secured revolving credit facility due September 2010	\$ 838,000	\$ 849,000
Senior secured credit facility term loan due September 2010	145,000	145,000
Senior secured credit facility term loan due June 2014	1,096,713	1,105,000
Senior secured credit facility term loan due June 2014 (\$349,125 face value less unamortized discount of \$31,549)	317,576	
7.5% senior secured notes due January 2015		200,000
10.375% senior secured notes due July 2016 (\$470,000 face value less unamortized discount of \$41,011)	428,989	
7.5% senior secured notes due March 2017	500,000	500,000
Other secured	4,194	2,740
	3,330,472	2,801,740
Guaranteed Unsecured Debt:		
8.625% senior notes due March 2015	500,000	500,000
9.375% senior notes due December 2015 (\$410,000 face value less unamortized discount of \$4,754 and \$5,458)	405,246	404,542
9.5% senior notes due June 2017 (\$810,000 face value less unamortized discount of \$10,732 and \$12,033)	799,268	797,967
	1,704,514	1,702,509
Unsecured Unguaranteed Debt:		
6.125% fixed-rate senior notes due December 2008		150,000
8.125% notes due May 2010	11,117	358,500
9.25% senior notes due June 2013	6,015	148,739
6.875% senior debentures due August 2013	184,773	184,773
8.5% convertible notes due May 2015	158,000	
7.7% notes due February 2027	295,000	295,000
6.875% fixed-rate senior notes due December 2028	128,000	128,000
	782,905	1,265,012
Lease financing obligations	193,818	216,263
Total debt	6,011,709	5,985,524
Current maturities of long-term debt and lease financing obligations	(40,683)	(185,609)
Long-term debt and lease financing obligations, less current maturities	\$ 5,971,026	\$ 5,799,915

Credit Facility

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The Company has a senior secured credit facility that includes a \$1,750,000 revolving credit facility. Borrowings under the revolving secured credit facility currently bear interest at LIBOR plus 1.50%, if the Company chooses to make LIBOR borrowings, or at Citibank's base rate plus 0.50%. The interest rate can fluctuate between LIBOR plus 1.25% and LIBOR plus 1.75% depending upon the amount of the revolver availability, as specified in the senior secured credit facility. The Company is required to

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

11. Indebtedness and Credit Agreement (Continued)

pay fees of 0.25% per annum on the daily unused amount of the revolving credit facility. The final maturity date on our revolving credit facility is September 30, 2010.

The Company's ability to borrow under the revolving credit facility is based upon a specified borrowing base consisting of inventory and prescription files. At February 28, 2009, the Company had \$838,000 of borrowings outstanding under the revolving credit facility. At February 28, 2009, the Company also had letters of credit outstanding against the revolving credit facility of \$188,345, which gave the Company additional borrowing capacity of \$723,655.

In November 2006, the Company entered into an amendment of its senior secured credit facility and borrowed \$145,000 under a senior secured term loan (the "Tranche 1 Term Loans"). The Tranche 1 Term Loans currently bear interest at LIBOR plus 1.50%, if the Company chooses to make LIBOR borrowings, or at Citibank's base rate plus 0.50%. The interest rate can fluctuate between LIBOR plus 1.25% and LIBOR plus 1.75% depending on the amount of availability under the Company's revolving credit facility, as specified in the senior secured credit facility. The amounts outstanding under the Tranche 1 Term Loans become due and payable on September 30, 2010, or earlier, if total debt outstanding under the senior secured credit facility exceeds the borrowing base.

On June 4, 2007, the Company amended its senior secured credit facility to establish a new senior secured term loan in the aggregate principal amount of \$1,105,000 and borrowed the full amount thereunder. A portion of the proceeds from the borrowings under this senior secured term loan (the "Tranche 2 Term Loans") were used to fund the acquisition of Brooks Eckerd. The Tranche 2 Term Loans will mature on June 4, 2014 and currently bears interest at LIBOR plus 1.75%, if the Company chooses to make LIBOR borrowings, or at Citibank's base rate plus 0.75%. The Company must make mandatory prepayments of the Tranche 2 Term Loans with the proceeds of asset dispositions (subject to certain limitations), with a portion of any excess cash flow generated by the Company and with the proceeds of certain issuances of equity and debt (subject to certain exceptions). If at any time total debt outstanding under the senior secured credit facility exceeds the borrowing base, prepayment of the Tranche 2 Term Loans may also be required.

In July 2008, the Company issued a new senior secured term loan (the "Tranche 3 Term Loan") of \$350,000 under the Company's existing senior secured credit facility. The Tranche 3 Term Loan was issued at a discount of 90% of par. The Tranche 3 Term Loan matures on June 4, 2014 and bears interest at LIBOR (with a minimum LIBOR rate of 3.00%) plus 3.00%, if the Company chooses to make LIBOR borrowings, or at Citibank's base rate (with a minimum base rate of 4.00%) plus 2.00%. The Company must make mandatory prepayments of the Tranche 3 Term Loan with the proceeds of asset dispositions (subject to certain limitations), with a portion of any excess cash flow generated by the Company and with the proceeds of certain issuances of equity and debt (subject to certain exceptions). If at any time total debt outstanding under the senior secured credit facility exceeds the borrowing base, prepayment of the Tranche 3 Term Loan may also be required.

The senior secured credit facility allows the Company to have outstanding, at any time, up to \$1,500,000 in secured second priority debt and unsecured debt in addition to borrowings under the senior secured credit facility and existing indebtedness, provided that not in excess of \$750,000 of such secured second priority debt and unsecured debt shall mature or require scheduled payment of principal prior to three months after June 4, 2014. The senior secured credit facility allows the

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

11. Indebtedness and Credit Agreement (Continued)

Company to incur an unlimited amount of unguaranteed unsecured debt with a maturity beyond three months after June 4, 2014; however, other debentures limit the amount of unsecured debt that can be incurred if certain interest coverage levels are not met at the time of incurrence of said debt. The senior secured credit facility also allows for the repurchase of any debt with a maturity on or before June 4, 2014, and for the voluntary repurchase of debt with a maturity after June 4, 2014, if the Company maintains availability on the revolving credit facility of at least \$100,000 and so long as the senior secured credit facility is not in default.

The senior secured credit facility contains covenants, which place restrictions on the incurrence of debt beyond the restrictions described above, the payments of dividends, sale of assets, mergers and acquisitions and the granting of liens. The senior secured credit facility also requires the Company to maintain a minimum fixed charge coverage ratio, but only if availability on the revolving credit facility is less than \$100,000.

The senior secured credit facility provides for events of default including nonpayment, misrepresentation, breach of covenants and bankruptcy. It is also an event of default if the Company fails to make any required payment on debt having a principal amount in excess of \$50,000 or any event occurs that enables, or which with the giving of notice or the lapse of time would enable, the holder of such debt to accelerate the maturity or require the repurchase of such debt.

Substantially all of Rite Aid Corporation's wholly-owned subsidiaries guarantee the obligations under the senior secured credit facility. The subsidiary guarantees of the senior secured credit facility are secured by a first priority lien on, among other things the inventory, accounts receivable and prescription files of the subsidiary guarantors. Rite Aid Corporation is a holding company with no direct operations and is dependent upon dividends, distributions and other payments from its subsidiaries to service payments due under the senior secured credit facility. The 7.5% senior secured notes due 2015, the 10.375% senior secured notes due 2016 and the 7.5% senior secured notes due 2017 are guaranteed by substantially all of the Company's wholly-owned subsidiaries, which are the same subsidiaries that guarantee the senior secured credit facility and are secured on a second priority basis by the same collateral as the senior secured credit facility. The 8.625% senior notes due 2015, the 9.375% senior notes due 2015, and the 9.5% senior notes due 2017 are also guaranteed by substantially all of the Company's wholly-owned subsidiaries.

The subsidiary guarantees related to the Company's senior secured credit facility and secured notes and on an unsecured basis the guaranteed indentures are full and unconditional and joint and several, and there are no restrictions on the ability of the parent to obtain funds from its subsidiaries. Also, the parent company has no independent assets or operations, and subsidiaries not guaranteeing the credit facility and applicable indentures are minor. Accordingly, condensed consolidating financial information for the parent and subsidiaries is not presented.

The indentures that govern the Company's secured and guaranteed unsecured notes contain restrictions on the amount of additional secured and unsecured debt that can be incurred by the Company. As of February 28, 2009, the amount of additional secured and unsecured debt that could be incurred under these indentures was \$870,045. The amount of additional second priority secured or unsecured debt that the Company could have incurred if we had drawn the maximum amount available on our revolving credit facility as of February 28, 2009 was \$146,390.

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

11. Indebtedness and Credit Agreement (Continued)

Other 2009 Transactions

In July 2008, pursuant to a tender offer and consent solicitation, the Company repurchased substantially all of the outstanding amounts of its 8.125% senior secured notes due May 2010, its 7.5% senior secured notes due January 2015 and its 9.25% senior notes due June 2013. This transaction was done because these notes had restrictions on the incurrence of liens securing the secured debt that prohibited the Company from fully drawing on its revolving credit facility under certain circumstances. The remaining outstanding amounts of such series no longer contain such restrictions and are no longer secured or guaranteed. The Company recorded a loss on debt modification related to these transactions of \$36,558 in fiscal 2009.

These transactions were financed via the issuance of a new senior secured term loan (the Tranche 3 Term Loan described above) and the issuance of a \$470,000 aggregate principal amount of 10.375% senior secured notes due July 2016. These notes are unsecured unsubordinated obligations of Rite Aid Corporation and rank equally in right of payment with all other unsubordinated indebtedness. The Company's obligations under the notes are guaranteed, subject to certain limitations, by subsidiaries that guarantee the obligations under its senior secured credit facility. The guarantees are secured by shared second priority liens with holders of our 7.5% senior secured notes due 2017. The indenture that governs the 10.375% senior secured notes due 2016 contains covenant provisions that, among other things, include limitations on the Company's ability to pay dividends, make investments or other restricted payments, incur debt, grant liens, sell assets and enter into sale-leaseback transactions. The senior 10.375% secured notes due July 2016 were issued at a discount of 90.588% of par.

In May 2008, the Company issued \$158,000 of 8.5% convertible notes due May 2015. These notes are unsecured and are effectively junior to the secured debt of the Company and are structurally subordinated to the guaranteed debt of the Company. The notes are convertible, at the option of the holder, into shares of the Company's common stock at a conversion price of \$2.59 per share, subject to adjustments to prevent dilution, at any time. Proceeds from the issuance of these notes were used to fund the redemption of the Company's 6.125% notes due December 2008. The Company recorded a loss on debt modification of \$3,347 related to the early redemption of the 6.125% notes due 2008, which included payment of a make whole premium to the noteholders and unamortized debt issue costs on the notes.

2008 Transactions

On June 4, 2007 the Company incurred \$1,220,000 aggregate principal amount of senior notes. The issue consisted of \$410,000 of 9.375% senior notes due 2015 and \$810,000 of 9.5% senior notes due 2017. The Company's obligations under each series of notes are fully and unconditionally guaranteed, jointly and severally, by all of the Company's subsidiaries that guarantee its obligations under the existing senior secured credit facility and other outstanding senior secured notes. The notes are unsecured, unsubordinated obligations of Rite Aid Corporation and rank equally in right of payment with all of the Company's other unsecured, unsubordinated debt. The indentures governing the notes contain covenants that limit the Company's ability and the ability of its restricted subsidiaries to, among other things, incur additional debt, pay dividends or make other restricted payments, purchase, redeem or retire capital stock or subordinated debt, make asset sales, enter into transactions with affiliates,

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(In thousands, except per share amounts)

11. Indebtedness and Credit Agreement (Continued)

incur liens, enter into sale-leaseback transactions, provide subsidiary guarantees, make investments and merge or consolidate with any other persons.

2007 Transactions

In February 2007, the Company issued \$500,000 aggregate principal amount of 7.5% senior secured notes due 2017. These notes are unsubordinated obligations of Rite Aid Corporation and rank equally in right of payment with all other unsubordinated indebtedness. The Company's obligations under the notes are guaranteed, subject to certain limitations, by subsidiaries that guarantee the obligations under its senior secured credit facility. The guarantees are secured, subject to the permitted liens, by shared second priority liens, with holders of our 10.375% senior secured notes due July 2016, granted by subsidiary guarantors on all their assets that secure the obligations under the senior secured credit facility, subject to certain exceptions. The indenture governing the 7.5% senior secured notes due 2017 contains covenant provisions that, among other things, include limitations on the Company's ability to pay dividends, make investments or other restricted payments, incur debt, grant liens, sell assets and enter into sale-leaseback transactions. Proceeds from this offering were used to repay outstanding borrowings on the Company's revolving credit facility and to fund the redemption of the Company's 9.5% senior secured notes due 2011, by deposit into an escrow fund with an independent trustee. Per the terms of the indenture that governed the 9.5% senior secured notes due 2011, the Company paid a premium to the noteholders of 104.75% of par. The Company recorded a loss on debt modification of \$18,662 related to the early redemption of the 9.5% senior secured notes due 2011, which included the call premium and unamortized debt issue costs on the notes.

In February 2007, the Company issued \$500,000 aggregate principal amount of 8.625% senior notes due 2015. These notes are unsecured. The indenture governing the 8.625% senior notes due 2015 contains provisions that, among other things, include limitations on the Company's ability to pay dividends, make investments or other restricted payments, incur debt, grant liens, sell assets and enter into sale-leaseback transactions. The 8.625% senior notes due 2015 are guaranteed, subject to certain limitations, by subsidiaries that guarantee the obligations under the senior secured credit facility. Proceeds from the issuance of the notes were used to repay borrowings under the Company's revolving credit facility.

In January 2007, the Company paid at maturity the remaining outstanding principal amount of \$184,074 of the Company's 7.125% notes due January 2007. This payment was funded with borrowings under the revolving credit facility.

In December 2006, the Company paid at maturity the remaining outstanding principal amount of \$250,000 of its 4.75% convertible notes due December 2006. This payment was funded with borrowings under the revolving credit facility.

In September 2006, the Company completed the early redemption of all of its outstanding \$142,025 of its 12.5% senior secured notes due September 2006. This payment was funded with borrowing under the revolving credit facility, which were subsequently repaid with borrowings of the Tranche 1 term loans.

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

11. Indebtedness and Credit Agreement (Continued)

Interest Rates and Maturities

The annual weighted average interest rate on the Company's indebtedness was 6.6%, 7.5%, and 7.6% for fiscal 2009, 2008, and 2007, respectively.

The aggregate annual principal payments of long-term debt for the five succeeding fiscal years are as follows: 2010 \$16,661; 2011 \$1,008,854; 2012 \$14,765; 2013 \$14,764 and \$4,762,847 in 2014 and thereafter. The Company is in compliance with restrictions and limitations included in the provisions of various loan and credit agreements.

Other

On October 16, 2008, Rite Aid was notified by the New York Stock Exchange (NYSE) that the average per share price of its common stock was below the NYSE's continued listing standard relating to minimum average share price. Rule 802.01C of the NYSE's Listed Company Manual requires that a company's common stock trade at a minimum average closing price of \$1.00 over a consecutive 30 trading-day period. Also on October 16, 2008, the Company provided a notice to the NYSE of its intention to affect a reverse stock split, subject to stockholder approval, to cure this deficiency. The Company has six months from receipt of the NYSE notice to regain compliance with the NYSE price condition, or it will be subject to suspension and delisting procedures. Subject to the NYSE's rules, during the six-month cure period, the Company's common stock will continue to be listed and trade on the NYSE. At the end of the six-month cure period, the Company will be in compliance if it has at least a \$1.00 share price and has maintained a \$1.00 average closing price over the preceding 30 consecutive trading days.

At a special meeting of stockholders held on December 2, 2008, the Rite Aid stockholders approved a reverse split of the Company's common stock at a split ratio of 1-for-10, 1-for-15, or 1-for-20, to be selected by the Company's Board of Directors. The exact timing of the split and the ratio selected would be based on the Board's decision as to the most advantageous action.

The Company has outstanding, \$158 million of 8.5% convertible notes. Holders of the convertible notes have the right to require Rite Aid to repurchase their notes if Rite Aid's common stock is not listed on the NYSE or Nasdaq Global Select or Nasdaq Global Markets. The Company's senior secured credit facility and the accounts receivable securitization facility provide that the occurrence of this repurchase right constitutes a default under such facilities.

On February 26, 2009, the NYSE announced that the NYSE will suspend the application of the stock-price criteria set forth in Section 802.01C of the Exchange's Listed Company Manual until June 30, 2009. This suspension was made by the Exchange due to the extreme volatility in U.S. and global equities markets and precipitous decline in trading prices of many securities. As a result of the market conditions, the Exchange has experienced an unusually high number of listed companies having stock prices that have fallen below the \$1.00 price requirement. Based on the rule suspension, any company, like Rite Aid, that is in a compliance period at the time of the rule suspension can return to compliance during the suspension if at the end of any calendar month during the suspension such company has a \$1.00 closing share price on the last trading day of such month and a \$1.00 average share price based on the 30 trading days preceding the end of such month. Furthermore, any such company that does not regain compliance during the suspension period will recommence its compliance period upon reinstatement of the stock price continued listing standard and receive the remaining

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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(In thousands, except per share amounts)

11. Indebtedness and Credit Agreement (Continued)

balance of its compliance period. For the Company, this means that it can regain compliance at the end of the 6-month compliance period, April 16, 2009, or at the end of any calendar month during the suspension, April 30, 2009, May 29, 2009, or June 30, 2009, or August 17, 2009.

On March 9, 2009, the Company announced that our Board of Directors had determined to delay affecting the reverse stock split in light of the NYSE suspension. The Board will determine the exchange ratio and timing of the reverse split, if implemented, prior to or immediately following the end of the suspension period based on market conditions, our share price and the NYSE rules at such time.

In addition to the Company's plans to regain compliance with the NYSE price condition, management may seek to refinance the Convertible Notes to avoid a repurchase. Management believes that these plans sufficiently mitigate the liquidity risks associated with a potential delisting of the Company's stock.

12. Leases

The Company leases most of its retail stores and certain distribution facilities under noncancellable operating and capital leases, most of which have initial lease terms ranging from five to 22 years. The Company also leases certain of its equipment and other assets under noncancellable operating leases with initial terms ranging from 3 to 10 years. In addition to minimum rental payments, certain store leases require additional payments based on sales volume, as well as reimbursements for taxes, maintenance and insurance. Most leases contain renewal options, certain of which involve rent increases. Total rental expense, net of sublease income of \$11,141, \$10,331, and \$7,725, was \$962,840, \$863,801 and \$586,776 in fiscal 2009, 2008, and 2007, respectively. These amounts include contingent rentals of \$31,605, \$35,932 and \$30,786 in fiscal 2009, 2008, and 2007, respectively.

During fiscal 2009, the Company sold 72 owned stores to several independent third parties. Proceeds from these sales totaled \$192,819. The Company entered into agreements to lease these stores back from the purchasers over minimum lease terms of 20 years. Sixty-seven leases are being accounted for as operating leases and five are being accounted for under the financing method as of February 28, 2009, as these lease agreements contain a clause that allows the buyer to force the Company to repurchase the property under certain conditions. Gains on these transactions of \$5,157 have been deferred and are being recorded over the related minimum lease terms. Losses of \$501, which relate to certain stores in these transactions, were recorded as losses on the sale of assets for the year ended February 28, 2009.

During fiscal 2008, the Company sold 22 owned stores to several independent third parties. Proceeds from these sales totaled \$93,252. The Company entered into agreements to lease these stores back from the purchasers over minimum lease terms of 20 years. Fourteen leases were accounted for as operating leases and eight were accounted for under the financing method as of March 1, 2008, as these lease agreements contain a clause that allows the buyer to force the Company to repurchase the property under certain conditions. Subsequent to March 1, 2008, the clause that allowed the buyer to force the Company to repurchase the properties lapsed on five of the eight leases. Therefore, these leases are now accounted for as operating leases. The Company recorded a capital lease obligation of \$17,972 related to the remaining leases.

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****12. Leases (Continued)**

During fiscal 2007, the Company sold a total of 29 owned stores to independent third parties. Proceeds from these sales totaled \$82,090. The Company entered into agreements to lease the stores back from the purchasers over minimum lease terms of 20 years. Twenty-four leases were accounted for as operating leases and the remaining five leases were accounted for using the financing method, as these lease agreements contained a clause that allowed the buyer to force the Company to purchase the properties under certain conditions. Subsequent to March 3, 2007, the clause that allowed the buyer to force the Company to repurchase the properties lapsed on the five leases. Therefore, these leases are now accounted for as operating leases.

The net book values of assets under capital leases and sale-leasebacks accounted for under the financing method at February 28, 2009 and March 1, 2008 are summarized as follows:

	2009	2008
Land	\$ 12,793	\$ 16,193
Buildings	166,460	193,361
Leasehold improvements	6,491	6,654
Equipment	34,712	29,878
Accumulated depreciation	(97,649)	(90,687)
	\$ 122,807	\$ 155,399

Following is a summary of lease finance obligations at February 28, 2009 and March 1, 2008:

	2009	2008
Obligations under capital leases	\$ 156,625	\$ 170,116
Sale-leaseback obligations	37,193	46,147
Less current obligation	(24,127)	(26,837)
Long-term lease finance obligations	\$ 169,691	\$ 189,426

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Following are the minimum lease payments for all properties under a lease agreement that will have to be made in each of the years indicated based on non-cancelable leases in effect as of February 28, 2009:

Fiscal year	Lease Financing Obligations	Operating Leases
2010	39,896	1,049,983
2011	24,775	1,029,943
2012	24,660	979,928
2013	24,571	923,423
2014	24,523	871,335
Later years	155,783	6,669,650
Total minimum lease payments	294,208	11,524,262
Amount representing interest	(100,390)	
Present value of minimum lease payments	193,818	

13. Redeemable Preferred Stock

In March 1999 and February 1999, Rite Aid Lease Management Company, a wholly owned subsidiary of the Company, issued 63,000 and 150,000 shares of Cumulative Preferred Stock, Class A, par value \$100 per share, respectively. The Class A Cumulative Preferred Stock is mandatorily redeemable on April 1, 2019 at a redemption price of \$100 per share plus accumulated and unpaid dividends. The Class A Cumulative Preferred Stock pays dividends quarterly at a rate of 7.0% per annum of the par value of \$100 per share when, as and if declared by the Board of Directors of Rite Aid Lease Management Company in its sole discretion. The amount of dividends payable in respect of the Class A Cumulative Preferred Stock may be adjusted under certain events. The outstanding shares of the Class A Preferred Stock were recorded at their estimated fair value of \$19,253 for the fiscal 2000 issuances, which equaled the sale price on the date of issuance. Because the fair value of the Class A Preferred Stock was less than the mandatory redemption amount at issuance, periodic accretions to expense using the interest method are made so that the carrying amount equals the redemption amount on the mandatory redemption date. Accretion was \$102 in fiscal 2009, 2008 and 2007. The amount of this instrument is \$20,277 and \$20,174 and is recorded in Other Non-Current Liabilities as of February 28, 2009 and March 1, 2008, respectively.

14. Capital Stock

As of February 28, 2009, the authorized capital stock of the Company consists of 1,500,000 shares of common stock and 20,000 shares of preferred stock, each having a par value of \$1.00 per share. Preferred stock is issued in series, subject to terms established by the Board of Directors.

On December 2, 2008, the Company's stockholders approved a decrease in the total number of authorized shares from 1,520,000 shares to 520,000 if the Company implements the reverse stock split.

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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14. Capital Stock (Continued)

After the stock split, the total authorized shares will be comprised of 500,000 shares of common stock, par value of \$1.00 per share and 20,000 shares of preferred stock, par value of \$1.00 per share.

In fiscal 2006, the Company issued 4,820 shares of Series I Mandatory Convertible Preferred Stock ("Series I preferred stock") at an offering price of \$25 per share. Dividends on the Series I preferred stock were \$1.38 per share per year, and were due and payable on a quarterly basis in either cash or common stock or a combination of both at the Company's election. In the first quarter of fiscal 2009 the Company entered into agreements with several of the holders of the Series I preferred stock to convert 2,404 shares into Rite Aid common stock earlier than the mandatory conversion date, November 17, 2008, at a rate of 5.6561 which resulted in the issuance of 14,648 shares of Rite Aid common stock. On the mandatory conversion date, the remaining outstanding 2,416 shares of Series I preferred stock automatically converted at a rate of 5.6561 which resulted in the issuance of 13,665 shares of Rite Aid common stock.

The Company also has outstanding Series G and Series H preferred stock. The Series G preferred stock has a liquidation preference of \$100 per share and pays quarterly dividends at 7% of liquidation preference. In the fourth quarter of 2009, at the election of the holder, substantially all of the Series G preferred stock was converted into 27,137 common shares, at a conversion rate of \$5.50 per share. The remaining Series G preferred stock can be redeemed at the Company's election after January 2009. The Company has not elected to redeem the remaining Series G preferred stock as of February 28, 2009.

The Series H preferred stock pays dividends of 6% of liquidation preference and can be redeemed at the Company's election after January 2010. All dividends can be paid in either cash or in additional shares of preferred stock, at the election of the Company. Any redemptions are at 105% of the liquidation preference of \$100 per share, plus accrued and unpaid dividends. The Series H shares are convertible into common stock of the Company, at the holder's option, at a conversion rate of \$5.50 per share.

15. Stock Option and Stock Award Plans

As disclosed in Note 1, effective March 5, 2006, the Company adopted SFAS No. 123(R), "Share-Based Payment" using the modified prospective transition method. Expense is recognized over the requisite service period of the award, net of an estimate for the impact of forfeitures. Operating results for fiscal 2009, 2008 and 2007 include \$31,448, \$40,439 and \$22,331 of compensation costs related to the Company's stock-based compensation arrangements.

The Company reserved 22,000 shares of its common stock for the granting of stock options and other incentive awards to officers and key associates under the 1990 Omnibus Stock Incentive Plan (the 1990 Plan), which was approved by the shareholders. Options may be granted, with or without stock appreciation rights ("SAR"), at prices that are not less than the fair market value of a share of common stock on the date of grant. The exercise of either a SAR or option automatically will cancel any related option or SAR. Under the 1990 Plan, the payment for SARs will be made in shares, cash or a combination of cash and shares at the discretion of the Compensation Committee.

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In November 1999, the Company adopted the 1999 Stock Option Plan (the 1999 Plan), under which 10,000 shares of common stock are authorized for the granting of stock options at the discretion of the Board of Directors.

In December 2000, the Company adopted the 2000 Omnibus Equity Plan (the 2000 Plan) under which 22,000 shares of common stock are reserved for granting of restricted stock, stock options, phantom stock, stock bonus awards and other stock awards at the discretion of the Board of Directors.

In February 2001, the Company adopted the 2001 Stock Option Plan (the 2001 Plan) which was approved by the shareholders under which 20,000 shares of common stock are authorized for granting of stock options at the discretion of the Board of Directors.

In April 2004, the Board of Directors adopted the 2004 Omnibus Equity Plan, which was approved by the shareholders. Under the plan, 20,000 shares of common stock are authorized for granting of restricted stock, stock options, phantom stock, stock bonus awards and other equity based awards at the direction of the Board of Directors.

In January 2007, the stockholders of Rite Aid Corporation approved the adoption of the Rite Aid Corporation 2006 Omnibus Equity Plan. Under the plan, 50,000 shares of Rite Aid common stock are available for granting of restricted stock, stock options, phantom stock, stock bonus awards and other equity based awards at the discretion of the Board of Directors. The adoption of the 2006 Omnibus Equity Plan became effective upon the closing of the Acquisition.

All of the plans provide for the Board of Directors (or at its election, the Compensation Committee) to determine both when and in what manner options may be exercised; however, it may not be more than 10 years from the date of grant. All of the plans provide that stock options may be granted at prices that are not less than the fair market value of a share of common stock on the date of grant. The aggregate number of shares authorized for issuance for all plans is 103,712 as of February 28, 2009.

The Company has issued options to certain senior executives pursuant to their individual employment contracts. These options were not issued out of the plans listed above, but are included in the option tables herein. As of February 28, 2009, 5,463 of these options remain outstanding.

Stock Options

The Company determines the fair value of stock options issued on the date of grant using the Black-Scholes-Merton option-pricing model. The following assumptions were used for options granted in fiscal 2009, 2008 and 2007:

	2009	2008	2007
Expected stock price volatility	50%	52%	56%
Expected dividend yield	0.00%	0.00%	0.0%
Risk-free interest rate	2.76%	4.96%	4.99%
Expected option life	5.25 years	5.5 years	5.5 years

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The weighted average fair value of options granted during fiscal 2009, 2008, and 2007 was \$0.42, \$3.20, and \$2.47, respectively.

Following is a summary of stock option transactions for the fiscal years ended February 28, 2009, March 1, 2008, and March 3, 2007:

	Shares	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at March 4, 2006	62,718	4.72		
Granted	6,793	4.43		
Exercised	(5,916)	3.44		
Cancelled	(2,999)	9.05		
Outstanding at March 3, 2007	60,596	4.60		
Granted	10,744	6.01		
Exercised	(4,135)	3.09		
Cancelled	(2,543)	6.66		
Outstanding at March 1, 2008	64,662	4.85		
Granted	14,632	.90		
Exercised	(516)	2.16		
Cancelled	(8,616)	6.84		
Outstanding at February 28, 2009	70,162	3.80	5.11	\$
Vested or expected to vest at February 28, 2009	64,485	3.80	4.85	\$
Exercisable at February 28, 2009	46,949	4.37	3.24	\$

As of February 28, 2009, there was \$21,763 of total unrecognized pre-tax compensation costs related to unvested stock options, net of forfeitures. These costs are expected to be recognized over a weighted average period of 2.27 years.

Cash received from stock option exercises for fiscal 2009, 2008, and 2007 was \$1,117, \$12,764, and \$20,386 respectively. There was no income tax benefit from stock options for fiscal 2009 and fiscal 2008. The income tax benefits from stock option exercises totaled \$4,202 for fiscal 2007. The total intrinsic value of stock options exercised for fiscal 2009, 2008, and 2007 was \$239, \$12,705, and \$12,346, respectively.

Restricted Stock

The Company provides restricted stock grants to associates under plans approved by the stockholders. Shares awarded under the plans vest in installments up to three years and unvested shares are forfeited upon termination of employment. Additionally, vesting of 386 shares awarded to certain senior executives is conditional upon the Company meeting specified performance targets. Following is

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a summary of restricted stock transactions for the fiscal years ended February 28, 2009, March 1, 2008, and March 3, 2007:

	Shares	Weighted Average Grant Date Fair Value
Balance at March 4, 2006	5,735	4.00
Granted	5,139	4.37
Vested	(1,899)	4.02
Cancelled	(973)	4.18
Balance at March 3, 2007	8,002	4.21
Granted	7,542	5.94
Vested	(4,004)	4.12
Cancelled	(1,568)	5.25
Balance at March 1, 2008	9,972	5.39
Granted	2,647	0.94
Vested	(4,760)	5.19
Cancelled	(1,160)	4.86
Balance at February 28, 2009	6,699	3.87

Compensation expense related to all restricted stock grants is being recorded over a three year vesting period of these grants. At February 28, 2009, there was \$15,334 of total unrecognized pre-tax compensation costs related to unvested restricted stock grants, net of forfeitures. These costs are expected to be recognized over a weighted average period of 1.39 years.

The total fair value of restricted stock vested during fiscal years 2009, 2008, and 2007 was \$24,707, \$16,488, and \$7,632, respectively.

16. Retirement Plans***Defined Contribution Plans***

The Company and its subsidiaries sponsor several retirement plans that are primarily 401(k) defined contribution plans covering nonunion associates and certain union associates. The Company does not contribute to all of the plans. Per those plan provisions, the Company matches 100% of a participant's pretax payroll contributions, up to a maximum of 3% of such participant's pretax annual compensation. Thereafter, the Company will match 50% of the participant's additional pretax payroll contributions, up to a maximum of 2% of such participant's additional pretax annual compensation. Total expense recognized for the above plans was \$64,111 in fiscal 2009, \$56,318 in fiscal 2008 and \$34,524 in fiscal 2007.

The Chairman of the Board and Chief Executive Officer and a member of the Board of Directors are entitled to supplemental retirement defined contribution arrangements in accordance with their

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

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(In thousands, except per share amounts)

16. Retirement Plans (Continued)

employment agreements, which vest immediately. The Company makes investments to fund these obligations. Other officers, who are not participating in the defined benefit nonqualified executive retirement plan, are included in a supplemental retirement plan, which is a defined contribution plan that is subject to a five year graduated vesting schedule. The (income) expense recognized for these plans was \$(6,287) in fiscal 2009, \$3,180 in fiscal 2008, and \$7,294 in fiscal 2007. The income recognized in fiscal 2009 is due to the impact of market conditions on the plan liabilities.

Defined Benefit Plans

The Company and its subsidiaries also sponsor a qualified defined benefit pension plan that requires benefits to be paid to eligible associates based upon years of service and, in some cases, eligible compensation. The Company's funding policy for The Rite Aid Pension Plan (The "Defined Benefit Pension Plan") is to contribute the minimum amount required by the Employee Retirement Income Security Act of 1974. However, the Company may, at its sole discretion, contribute additional funds to the plan. The Company made discretionary contributions of \$ 1,174 in fiscal 2009, \$10,100 in fiscal 2008, and \$10,700 in fiscal 2007.

The Company has established the nonqualified executive retirement plan for certain officers who, pursuant to their employment agreements, are not participating in the defined contribution supplemental retirement plan. Generally, eligible participants receive an annual benefit, payable monthly over fifteen years, equal to a percentage of the average of the three highest annual base salaries paid or accrued for each participant within the ten fiscal years prior to the date of the event giving rise to payment of the benefit. This defined benefit plan is unfunded.

On March 3, 2007, the last day of the 2007 fiscal year, the Company adopted the provisions of SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" an amendment of FASB Statements No. 87, 88, 106 and 132(R)". This standard requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability on the balance sheet and to recognize changes in the funded status in the year in which the changes occur through other comprehensive income.

The initial incremental recognition of the funded status under SFAS No. 158 is recognized as an adjustment to accumulated other comprehensive loss as of March 3, 2007. The cumulative effect of adopting the provisions of SFAS No. 158 as of March 3, 2007 was not material to the consolidated financial statements. Subsequent changes in the funded status that are not included in net periodic benefit cost will be reflected as a component of other comprehensive loss.

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****16. Retirement Plans (Continued)**

Net periodic pension expense and other changes recognized in other comprehensive income for the defined benefit plans included the following components:

	Defined Benefit Pension Plan			Nonqualified Executive Retirement Plan		
	2009	2008	2007	2009	2008	2007
Service cost	\$ 2,819	\$ 3,254	\$ 3,231	\$ 51	\$ 49	\$ 83
Interest cost	5,741	5,476	5,208	1,199	1,146	1,094
Expected return on plan assets	(5,305)	(5,054)	(4,193)			
Amortization of unrecognized net transition obligation					87	87
Amortization of unrecognized prior service cost	997	997	728			
Amortization of unrecognized net loss (gain)	328	845	1,681	(422)	(445)	776
Net pension expense	\$ 4,580	\$ 5,518	\$ 6,655	\$ 828	\$ 837	\$ 2,040
Other changes recognized in other comprehensive loss:						
Unrecognized net loss (gain) arising during period	\$24,694	\$(3,928)		\$(2,130)	\$(874)	
Prior service cost arising during period	2					
Amortization of unrecognized net transition obligation					(87)	
Amortization of unrecognized prior service costs	(997)	(997)				
Amortization of unrecognized net (loss) gain	(328)	(845)		422	445	
Net amount recognized in other comprehensive loss	23,371	(5,770)		(1,708)	(516)	
Net amount recognized in pension expense and other comprehensive loss	\$27,951	\$ (252)		\$ (880)	\$ 321	

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****16. Retirement Plans (Continued)**

The table below sets forth reconciliation from the beginning of the year for both the benefit obligation and plan assets of the Company's defined benefit plans, as well as the funded status and amounts recognized in the Company's balance sheet as of February 28, 2009 and March 1, 2008:

	Defined Benefit Pension Plan		Nonqualified Executive Retirement Plan	
	2009	2008	2009	2008
Change in benefit obligations:				
Benefit obligation at end of prior year	\$ 92,301	\$ 98,680	\$ 19,678	\$ 21,153
Service cost	2,819	3,255	51	49
Interest cost	5,741	5,476	1,199	1,146
Distributions	(6,017)	(5,456)	(1,708)	(1,797)
Change due to change in assumptions	(6,474)	(9,026)	(439)	(938)
Change due to plan amendment	2			
Actuarial (gain) loss	37	(628)	(1,691)	65
Benefit obligation at end of year	\$ 88,409	\$ 92,301	\$ 17,090	\$ 19,678
Change in plan assets:				
Fair value of plan assets at beginning of year	\$ 87,856	\$ 83,883	\$	\$
Employer contributions	1,174	10,100	1,708	1,797
Actual return on plan assets	(24,490)	547		
Distributions (including expenses paid by the plan)	(7,353)	(6,674)	(1,708)	(1,797)
Fair value of plan assets at end of year	\$ 57,187	\$ 87,856	\$	\$
Funded status	\$(31,222)	\$(4,445)	\$(17,090)	\$(19,678)
Unrecognized net actuarial loss				
Unrecognized prior service cost				
Unrecognized net transition obligation				
Net amount recognized	\$(31,222)	\$(4,445)	\$(17,090)	\$(19,678)
Amounts recognized in consolidated balance sheets consisted of:				
Prepaid pension cost	\$	\$	\$	\$
Accrued pension liability	(31,222)	(4,445)	(17,090)	(19,678)
Pension intangible asset				
Minimum pension liability included in accumulated other comprehensive loss				
Net amount recognized	\$(31,222)	\$(4,445)	\$(17,090)	\$(19,678)
Amounts recognized in accumulated other comprehensive loss consist of:				
Net actuarial gain (loss)	\$(37,240)	\$(12,875)	\$ 473	\$ (1,235)
Prior service cost	(3,423)	(4,418)		

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Net transition obligation

Amount recognized	\$ (40,663)	\$ (17,293)	\$ 473	\$ (1,235)
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The estimated net actuarial loss and prior service cost amounts that will be amortized from accumulated other comprehensive loss into net periodic pension expense in fiscal 2010 are \$3,337 and \$861, respectively.

The accumulated benefit obligation for the defined benefit pension plan was \$87,932 and \$91,786 as of February 28, 2009 and March 1, 2008, respectively. The accumulated benefit obligation for the nonqualified executive retirement plan was \$16,931 and \$19,555 as of February 28, 2009 and March 1, 2008, respectively.

The significant actuarial assumptions used for all defined benefit plans to determine the benefit obligation as of February 28, 2009, March 1, 2008, and March 3, 2007 were as follows:

	Defined Benefit Pension Plan			Nonqualified Executive Retirement Plan		
	2009	2008	2007	2009	2008	2007
Discount rate	7.00%	6.50%	5.75%	7.00%	6.50%	5.75%
Rate of increase in future compensation levels	5.00	5.00	5.00	3.00	3.00	3.00

Weighted average assumptions used to determine net cost for the fiscal years ended February 28, 2009, March 1, 2008 and March 3, 2007 were:

	Defined Benefit Pension Plan			Nonqualified Executive Retirement Plan		
	2009	2008	2007	2009	2008	2007
Discount rate	6.50%	5.75%	5.50%	6.50%	5.75%	5.50%
Rate of increase in future compensation levels	5.00	5.00	5.00	3.00	3.00	3.00
Expected long-term rate of return on plan assets	7.75	7.75	7.75	N/A	N/A	N/A

To develop the expected long-term rate of return on assets assumption, the Company considered the historical returns and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio. This resulted in the selection of the 7.75% long-term rate of return on plan assets assumption for fiscal 2009, 2008 and 2007.

The Company's pension plan asset allocations at February 28, 2009 and March 1, 2008 by asset category were as follows:

	February 28, 2009	March 1, 2008
Equity securities	56%	59%
Fixed income securities	44%	41%
Total	100%	100%

The investment objectives of the Defined Benefit Pension Plan, the only defined benefit plan with assets, are to:

Achieve a rate of return on investments that exceeds inflation over a full market cycle and is consistent with actuarial assumptions;

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

16. Retirement Plans (Continued)

Balance the correlation between assets and liabilities by diversifying the portfolio among various asset classes to address return risk and interest rate risk;

Balance the allocation of assets between the investment managers to minimize concentration risk;

Maintain liquidity in the portfolio sufficient to meet plan obligations as they come due; and

Control administrative and management costs.

The asset allocation established for the pension investment program reflects the risk tolerance of the Company, as determined by:

The current and anticipated financial strength of the Company;

the funded status of the plan; and

plan liabilities.

Investments in both the equity and fixed income markets will be maintained, recognizing that historical results indicate that equities (primarily common stocks) have higher expected returns than fixed income investments. It is also recognized that the correlation between assets and liabilities must be balanced to address higher volatility of equity investments (return risk) and interest rate risk.

The following targets are to be applied to the allocation of plan assets.

Category	Target Allocation
U.S. equities	45%
International equities	15%
U.S. fixed income	40%
Total	100%

The Company expects to contribute \$8,000 to the Defined Benefit Pension Plan and \$1,864 to the nonqualified executive retirement plan during fiscal 2010.

Following are the future benefit payments expected to be paid for the Defined Benefit Pension Plan and the nonqualified executive retirement plan during the years indicated:

Fiscal Year

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	Defined Benefit Pension Plan	Nonqualified Executive Retirement Plan
2010	\$ 5,418	\$ 1,864
2011	5,672	1,515
2012	5,741	1,559
2013	6,055	1,667
2014	6,262	1,649
2015-2019	34,636	6,667
Total	\$ 63,784	\$ 14,921

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RITE AID CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007

(In thousands, except per share amounts)

16. Retirement Plans (Continued)

Other Plans

The Company participates in various multi-employer union pension plans that are not sponsored by the Company. Total expenses recognized for the multi-employer plans were \$10,924 in fiscal 2009, \$13,341 in fiscal 2008 and \$13,326 in fiscal 2007.

17. Commitments, Contingencies and Guarantees

Legal Proceedings

The Company entered into a memorandum of understanding to settle a class action lawsuit brought against it in the U.S. District Court for the Northern District of California for alleged violations of California wage-and-hour law. The plaintiff alleged that the Company improperly classified store managers in California as exempt under the law, making them ineligible for overtime wages. The plaintiff sought to require the Company to pay overtime wages to the class of more than 1,200 current and former store managers since May 9, 2001. Management believes that store managers were and are properly classified as exempt from the overtime provisions of California law. On March 27, 2009, the Company entered into a memorandum of understanding to settle with the plaintiff under which, subject to approval of the court, the Company will resolve this lawsuit for \$6.9 million. Management anticipates obtaining final court approval of the settlement in the fall of 2009.

The Company is subject from time to time to various claims and lawsuits and governmental investigations arising in the ordinary course of business including lawsuits alleging violations by the Company of state and/or federal wage and hour laws pertaining to overtime pay and pay for missed meals and rest periods. Some of these suits purport or have been determined to be class actions and/or seek substantial damages. While the Company's management cannot predict the outcome of these claims with certainty, the Company's management does not believe that the outcome of any of these legal matters will have a material adverse effect on its consolidated results of operations, financial position or cash flows.

Guaranteed Lease Obligations

In connection with certain business dispositions, the Company continues to guarantee lease obligations for 126 former stores. The respective purchasers assume the Company's obligations and are, therefore, primarily liable for these obligations. Assuming that each respective purchaser became insolvent, an event which the Company believes to be highly unlikely, management estimates that it could settle these obligations for amounts substantially less than the aggregate obligation of \$231,395 as of February 28, 2009. The obligations are for varying terms dependent upon the respective lease, the longest of which lasts through February 17, 2024.

In the opinion of management, the ultimate disposition of these guarantees will not have a material effect on the Company's results of operations, financial position or cash flows.

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****18. Supplementary Cash Flow Data**

	February 28, 2009	Year Ended March 1, 2008	March 3, 2007
Cash paid for interest (net of capitalized amounts of \$1,434, \$2,069 and \$1,474)	\$ 462,847	\$ 353,711	\$ 267,807
Cash payments (refunds) from income taxes, net	\$ 5,793	\$ 2,404	\$ (2,676)
Equipment financed under capital leases	\$ 8,117	\$ 11,667	\$ 9,387
Equipment received for noncash consideration	\$ 23,878	\$ 3,411	\$ 3,471
Preferred stock dividends paid in additional shares	\$ 18,302	\$ 17,153	\$ 16,075
Reduction in lease financing obligation	\$ 40,221	\$ 18,406	\$ 13,629
Accrued capital expenditures	\$ 16,529	\$ 37,344	\$ 54,300
Gross borrowings from revolver	\$5,522,000	\$5,006,000	\$3,711,000
Gross repayments to revolver	\$5,533,000	\$4,457,000	\$3,945,000

19. Related Party Transactions

There were receivables from related parties of \$314 and \$507 at February 28, 2009 and March 1, 2008, respectively.

In connection with the acquisition of Jean Coutu, USA, the Company entered into a transition services agreement with the Jean Coutu Group. Under the terms of this agreement, Jean Coutu Group provided certain information technology, network and support services to the Company. The agreement expired in September 2008. The Company recorded an expense of \$894 for services provided under this agreement for the year ended February 28, 2009.

During fiscal 2009, 2008 and 2007, the Company paid Leonard Green & Partners, L.P., fees of \$227, \$276 and \$334, for financial advisory services, respectively. These amounts include expense reimbursements of \$90, \$89 and \$59 for the fiscal years 2009, 2008 and 2007, respectively. Jonathan D. Sokoloff, director, is an equity owner of Leonard Green & Partners, L.P. The Company has entered into a month-to-month agreement with Leonard Green & Partners, L.P., as amended whereby the Company has agreed to pay Leonard Green & Partners, L.P., a monthly fee of \$12.5, paid in arrears, for its consulting services. The consulting agreement also provides for the reimbursement of out-of-pocket expenses incurred by Leonard Green & Partners, L.P.

Prior to being employed by the Company, the Company paid Mr. John Standley a fee of \$32.5 per week for consulting services rendered in July, August and September 2008. The consulting agreement was on a week-to-week basis, which also provided for the reimbursement of out-of-pocket expenses incurred by Mr. Standley. During fiscal year 2009 and prior to his employment as President and Chief Operating Officer, Rite Aid paid Mr. Standley a consulting fee of \$294.

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****20. Interim Financial Results (Unaudited)**

	Fiscal Year 2009				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Revenues	\$ 6,612,856	\$ 6,500,244	\$ 6,468,601	\$ 6,707,567	\$ 26,289,268
Cost of goods sold	4,804,610	4,722,070	4,743,089	4,983,847	19,253,616
Selling, general and administrative expenses	1,792,974	1,780,631	1,711,873	1,699,889	6,985,367
Goodwill impairment charge				1,810,223	1,810,223
Lease termination and impairment charges	36,262	51,825	101,635	104,021	293,743
Interest expense	118,240	118,565	126,615	114,207	477,627
Loss on debt modifications and retirements, net	3,708	36,197			39,905
Loss (gain) on sale of assets and investments, net	5,340	7,607	(1,008)	(358)	11,581
	6,761,134	6,716,895	6,682,204	8,711,829	28,872,062
Loss before income taxes	(148,278)	(216,651)	(213,603)	(2,004,262)	(2,582,794)
Income tax expense	4,993	5,346	29,522	289,396	329,257
Net loss from continuing operations	(153,271)	(221,997)	(243,125)	(2,293,658)	(2,912,051)
Loss from discontinued operations, net of gain on disposal and income tax benefit	(3,369)				(3,369)
Net loss	\$ (156,640)	\$ (221,997)	\$ (243,125)	\$ (2,293,658)	\$ (2,915,420)
Basic loss per share(1)	\$ (0.20)	\$ (0.27)	\$ (0.30)	\$ (2.67)	\$ (3.49)
Diluted loss per share(1)	\$ (0.20)	\$ (0.27)	\$ (0.30)	\$ (2.67)	\$ (3.49)

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****20. Interim Financial Results (Unaudited) (Continued)**

	Fiscal Year 2008				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Year
Revenues	\$4,430,413	\$6,573,699	\$6,497,912	\$6,824,822	\$24,326,846
Cost of goods sold	3,214,834	4,783,888	4,754,057	4,936,493	17,689,272
Selling, general and administrative expenses	1,119,642	1,742,146	1,730,053	1,774,296	6,366,137
Lease termination and impairment charges	4,030	16,587	21,836	43,713	86,166
Interest expense	68,725	123,250	130,306	127,315	449,596
Loss on debt modifications and retirements, net		12,900			12,900
(Gain) Loss on sale of assets and investments, net	(4,230)	1,651	(2,105)	958	(3,726)
	4,403,001	6,680,422	6,634,147	6,882,775	24,600,345
Income (loss) before income taxes	27,412	(106,723)	(136,235)	(57,953)	(273,499)
Income tax (benefit) expense	(900)	(38,570)	(52,739)	894,910	802,701
Net income (loss) from continuing operations	28,312	(68,153)	(83,496)	(952,863)	(1,076,200)
(Loss) income from discontinued operations, net of gain on disposal and income tax benefit	(678)	(1,443)	(1,352)	683	(2,790)
Net income (loss)	\$ 27,634	\$ (69,596)	\$ (84,848)	\$ (952,180)	\$ (1,078,990)
Basic income (loss) per share(1)	\$ 0.04	\$ (0.10)	\$ (0.12)	\$ (1.20)	\$ (1.54)
Diluted income (loss) per share(1)	\$ 0.04	\$ (0.10)	\$ (0.12)	\$ (1.20)	\$ (1.54)

(1)

Income (loss) per share amounts for each quarter may not necessarily total to the yearly income (loss) per share due to the weighting of shares outstanding on a quarterly and year-to-date basis.

During the second quarter of 2009, the Company recorded a loss on debt modification related to the repurchase of several notes as discussed in Note 11. During the fourth quarter of fiscal 2009, the Company recorded a charge for goodwill impairment of \$1,810,223 and store closing and impairment charges of \$85,839. The Company recorded income tax expense of \$280,700 related to the establishment of additional valuation allowance against deferred tax assets. The Company recorded LIFO expense of \$94,569 as inflation was higher than anticipated.

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During the fourth quarter of fiscal 2008, the Company recorded an income tax expense of \$894,910 related primarily to the establishment of a valuation allowance against deferred tax assets. The Company recorded store closing and impairment charges of \$43,713. The Company recorded a credit of \$25,259 to record an adjustment to the LIFO reserve, as inflation on pharmacy products was less than

Table of Contents**RITE AID CORPORATION AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007****(In thousands, except per share amounts)****20. Interim Financial Results (Unaudited) (Continued)**

estimated in previous quarters. The Company recorded a gain on the sale of assets in Las Vegas of \$8,100.

During the second quarter of fiscal 2008, the Company recorded a charge of \$12,900 related to commitment fees for bridge financing of the Acquisition that was never utilized.

21. Financial Instruments

The carrying amounts and fair values of financial instruments at February 28, 2009 and March 1, 2008 are listed as follows:

	2009		2008	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Variable rate indebtedness	\$2,397,288	\$1,674,069	\$2,099,000	\$1,896,705
Fixed rate indebtedness	\$3,420,603	\$1,076,476	\$3,670,262	\$2,902,318

Cash, trade receivables and trade payables are carried at market value, which approximates their fair values due to the short-term maturity of these instruments.

The following methods and assumptions were used in estimating fair value disclosures for financial instruments:

LIBOR-based borrowings under credit facilities:

The carrying amounts for LIBOR-based borrowings under the credit facilities, term loans and term notes are estimated based on the quoted market price of the financial instruments.

Long-term indebtedness:

The fair values of long-term indebtedness are estimated based on the quoted market prices of the financial instruments. If quoted market prices were not available, the Company estimated the fair value based on the quoted market price of a financial instrument with similar characteristics.

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RITE AID CORPORATION AND SUBSIDIARIES
SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS
For the Years Ended February 28, 2009, March 1, 2008 and March 3, 2007
(dollars in thousands)

Allowances deducted from accounts receivable for estimated uncollectible amounts:	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Deductions	Allowances Related to the Purchase of Jean Coutu, USA	Balance at End of Period
Year ended February 28, 2009	\$ 41,221	\$ 31,269	\$ 35,000		\$ 37,490
Year ended March 1, 2008	\$ 30,246	\$ 34,598	\$ 34,015	10,392	\$ 41,221
Year ended March 3, 2007	\$ 32,336	\$ 26,603	\$ 28,693		\$ 30,246

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Table of Contents**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) 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.

RITE AID CORPORATION

By: /s/ MARY F. SAMMONS

Mary F. Sammons
*Chairman of the Board and
Chief Executive Officer*

Dated: April 17, 2009

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in their respective capacities on April 17, 2009.

Signature	Title
<u> /s/ MARY F. SAMMONS </u> Mary F. Sammons /s/ MICHEL COUTU	Chairman of the Board and Chief Executive Officer
<u> Michel Coutu </u> /s/ FRANK G. VITRANO	Non-Executive Co-Chairman of the Board
<u> Frank G. Vitrano </u> /s/ DOUGLAS E. DONLEY	Chief Financial Officer, Chief Administration Officer and Senior Executive Vice President
<u> Douglas E. Donley </u> /s/ JOSEPH B. ANDERSON, JR	Chief Accounting Officer and Senior Vice President
<u> Joseph B. Anderson, Jr </u> /s/ ANDRE BELZILE	Director
<u> Andre Belzile </u> /s/ FRANCOIS J. COUTU	Director
<u> Francois J. Coutu </u>	Director

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Signature	Title
<hr/> <i>/s/ JAMES L. DONALD</i>	
James L. Donald	Director
<hr/> <i>/s/ MICHAEL A. FRIEDMAN, MD</i>	
Michael A. Friedman, MD	Director
<hr/> <i>/s/ ROBERT G. MILLER</i>	
Robert G. Miller	Director
<hr/> <i>/s/ MICHAEL N. REGAN</i>	
Michael N. Regan	Director
<hr/> <i>/s/ PHILIP G. SATRE</i>	
Philip G. Satre	Director
<hr/> <i>/s/ JONATHAN D. SOKOLOFF</i>	
Jonathan D. Sokoloff	Director
<hr/> <i>/s/ MARCY SYMS</i>	
Marcy Syms	Director
<hr/> <i>/s/ DENNIS WOOD</i>	
Dennis Wood	Director