PLAYBOY ENTERPRISES INC
Form 10-Q
August 09, 2007

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2007

OR

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

Commission file number 001-14790

Playboy Enterprises, Inc.
(Exact name of registrant as specified in its charter)

Delaware	36-4249478
(State of incorporation)	(I.R.S. Employer Identification Number)
680 North Lake Shore Drive Chicago, IL	60611
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (312) 751-8000

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

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

Large accelerated filer [_] Accelerated filer [X] Non-accelerated filer [_]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).
Yes [_] No [X]

At July 31, 2007, there were 4,864,102 shares of Class A common stock and 28,387,357 shares of Class B common stock outstanding.

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains "forward-looking statements," including statements in Part I, Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations," as to expectations, beliefs, plans, objectives and future financial performance, and assumptions underlying or concerning the foregoing. We use words such as "may," "will," "would," "could," "should," "believes," "estimates," "projects," "potential," "expects," "plans," "anticipates," "intends," "continues" and other similar terminology. These forward-looking statements involve known and unknown risks, uncertainties and other factors, which could cause our actual results, performance or outcomes to differ materially from those expressed or implied in the forward-looking statements. We want to caution you not to place undue reliance on any forward-looking statements. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise.

The following are some of the important factors that could cause our actual results, performance or outcomes to differ materially from those discussed in the forward-looking statements:

(1) Foreign, national, state and local government regulations, actions or initiatives, including:

  (a) attempts to limit or otherwise regulate the sale, distribution or transmission of adult-oriented materials, including print, television, video, Internet and wireless materials,

  (b) limitations on the advertisement of tobacco, alcohol and other products which are important sources of advertising revenue for us, or

  (c) substantive changes in postal regulations which could increase our postage and distribution costs;

(2) Risks associated with our foreign operations, including market acceptance and demand for our products and the products of our licensees;

(3) Our ability to manage the risk associated with our exposure to foreign currency exchange rate fluctuations;

(4) Changes in general economic conditions, consumer spending habits, viewing patterns, fashion trends or the retail sales environment which, in each case, could reduce demand for our programming and products and impact our advertising revenues;

(5) Our ability to protect our trademarks, copyrights and other intellectual property;

(6) Risks as a distributor of media content, including our becoming subject to claims for defamation, invasion of privacy, negligence, copyright, patent or trademark infringement and other claims based on the nature and content of the materials we distribute;

(7) The risk our outstanding litigation could result in settlements or judgments which are material to us;

(8) Dilution from any potential issuance of common stock or convertible debt in connection with financings or acquisition activities;

(9) Competition for advertisers from other publications, media or online providers or any decrease in spending by advertisers, either generally or with respect to the adult male market;

(10) Competition in the television, men's magazine, Internet, new electronic media and product licensing markets;

(11) Attempts by consumers or private advocacy groups to exclude our programming or other products from distribution;

(12) Our television, Internet and wireless businesses' reliance on third parties for technology and distribution, and any changes in that technology and/or unforeseen delays in its implementation which might affect our plans and assumptions;

(13) Risks associated with losing access to transponders or technical failure of transponders or other transmitting or playback equipment that is beyond our control and competition for channel space on linear television platforms or video-on-demand platforms;

(14) Failure to maintain our agreements with multiple system operators, or MSOs, and direct-to-home, or DTH, operators on favorable terms, as well as any decline in our access to, and acceptance by, DTH and/or cable systems and the possible resulting deterioration in the terms, cancellation of fee arrangements or pressure on splits with operators of these systems;

(15) Risks that we may not realize the expected increased sales and profits and other benefits from acquisitions;

(16) Any charges or costs we incur in connection with restructuring measures we may take in the future;

(17) Risks associated with the financial condition of Claxson Interactive Group, Inc., our Playboy TV-Latin America, LLC, joint venture partner;

(18) Increases in paper, printing or postage costs;

(19) Risks associated with certain minimum revenue amounts under certain television distribution agreements;

(20) Effects of the national consolidation of the single-copy magazine distribution system;

(21) Effects of the national consolidation of television distribution companies (e.g., cable MSOs, satellite platforms and telecommunications companies); and

(22) Risks associated with the viability of our subscription-, on demand- and e-commerce-based Internet models.

For a detailed discussion of these and other factors that may affect our performance, see Part I, Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2006.

PLAYBOY ENTERPRISES, INC.
FORM 10-Q

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FINANCIAL INFORMATION

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CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME (LOSS)
for the Quarters Ended June 30 (Unaudited)
(In thousands, except per share amounts)

	2007	2006
Net revenues	$ 85,652	$ 80,477
Costs and expenses		
Cost of sales	(66,532)	(65,567)

Selling and administrative expenses	(15,157)	(14,257)
Restructuring expenses	(110)	(1,906)
Total costs and expenses	(81,799)	(81,730)
Gain on disposal	--	29
Operating income (loss)	3,853	(1,224)
Nonoperating income (expense)		
Investment income	623	602
Interest expense	(1,204)	(1,281)
Amortization of deferred financing fees	(134)	(134)
Other, net	(168)	50
Total nonoperating expense	(883)	(763)
Income (loss) before income taxes	2,970	(1,987)
Income tax expense	(1,059)	(1,320)
Net income (loss)	1,911	(3,307)
Other comprehensive income (loss)		
Unrealized gain (loss) on marketable securities	96	(111)
Unrealized gain (loss) on derivatives	47	(59)
Foreign currency translation gain (loss)	(108)	502
Total other comprehensive income	35	332
Comprehensive income (loss)	$ 1,946	$ (2,975)
Weighted average number of common shares outstanding		
Basic	33,243	33,158
Diluted	33,272	33,158
Basic and diluted earnings (loss) per common share	$ 0.06	$ (0.10)

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

PLAYBOY ENTERPRISES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME (LOSS)
for the Six Months Ended June 30 (Unaudited)
(In thousands, except per share amounts)

	2007	2006
Net revenues	$ 171,067	$ 162,597
Costs and expenses		

Cost of sales	(133,479)	(128,819)
Selling and administrative expenses	(29,740)	(29,594)
Restructuring expenses	(110)	(1,906)
Total costs and expenses	(163,329)	(160,319)
Gain on disposal	--	29
Operating income	7,738	2,307
Nonoperating income (expense)		
Investment income	1,098	1,209
Interest expense	(2,566)	(2,709)
Amortization of deferred financing fees	(268)	(268)
Other, net	(307)	(146)
Total nonoperating expense	(2,043)	(1,914)
Income before income taxes	5,695	393
Income tax expense	(2,310)	(2,911)
Net income (loss)	3,385	(2,518)
Other comprehensive income (loss)		
Unrealized gain on marketable securities	153	9
Unrealized gain (loss) on derivatives	36	(61)
Foreign currency translation gain (loss)	(285)	417
Total other comprehensive income (loss)	(96)	365
Comprehensive income (loss)	$ 3,289	$ (2,153)
Weighted average number of common shares outstanding		
Basic	33,236	33,149
Diluted	33,271	33,149
Basic and diluted earnings (loss) per common share	$ 0.10	$ (0.08)

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

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PLAYBOY ENTERPRISES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

	(Unaudited) June 30, 2007	December 31, 2006
Assets		
Cash and cash equivalents	$ 26,391	$ 26,748

Marketable securities and short-term investments	9,013	9,000
Receivables, net of allowance for doubtful accounts of $4,645 and $3,688, respectively	41,502	47,728
Receivables from related parties	2,066	1,791
Inventories	13,086	12,599
Deferred subscription acquisition costs	9,385	9,931
Other current assets	11,226	9,426
Total current assets	112,669	117,223
Long-term investments	6,279	--
Property and equipment, net	19,962	17,407
Long-term receivables	4,517	4,665
Programming costs, net	54,621	55,183
Goodwill	133,531	132,974
Trademarks	64,705	63,794
Distribution agreements, net of accumulated amortization of $4,119 and $3,435, respectively	29,021	29,705
Other noncurrent assets	13,850	14,832
Total assets	$ 439,155	$ 435,783
Liabilities		
Acquisition liabilities	$ 7,514	$ 10,773
Accounts payable	32,381	28,846
Accrued salaries, wages and employee benefits	4,738	4,896
Deferred revenues	44,325	45,050
Accrued litigation settlement	1,800	1,800
Other liabilities and accrued expenses	14,075	14,124
Total current liabilities	104,833	105,489
Financing obligations	115,000	115,000
Acquisition liabilities	8,048	9,692
Net deferred tax liabilities	19,260	18,422
Other noncurrent liabilities	24,616	23,552
Total liabilities	271,757	272,155
Shareholders' equity		
Common stock, $0.01 par value		
Class A voting - 7,500,000 shares authorized; 4,864,102 issued	49	49
Class B nonvoting - 75,000,000 shares authorized; 28,765,219 and 28,743,914 issued, respectively	288	287
Capital in excess of par value	228,255	227,775
Accumulated deficit	(54,306)	(57,691)
Treasury stock, at cost, 381,971 shares	(5,000)	(5,000)
Accumulated other comprehensive loss	(1,888)	(1,792)
Total shareholders' equity	167,398	163,628
Total liabilities and shareholders' equity	$ 439,155	$ 435,783

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

PLAYBOY ENTERPRISES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
for the Six Months Ended June 30 (Unaudited)
(In thousands)

	2007	2006
Cash flows from operating activities		
Net income (loss)	$ 3,385	$ (2,518)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation of property and equipment	2,232	1,827
Amortization of intangible assets	1,158	612
Amortization of investments in entertainment programming	17,444	17,561
Amortization of deferred financing fees	268	268
Deferred income taxes	838	2,151
Net change in operating assets and liabilities	8,218	180
Investments in entertainment programming	(17,627)	(19,545)
Stock-based compensation	359	1,794
Other, net	301	932
Net cash provided by operating activities	16,576	3,262
Cash flows from investing activities		
Payments for acquisitions	(105)	(7,761)
Purchases of investments	(6,384)	(267)
Proceeds from sales of investments	--	11,000
Additions to property and equipment	(5,030)	(2,826)
Net cash provided by (used for) investing activities	(11,519)	146
Cash flows from financing activities		
Payments of acquisition liabilities	(5,669)	(4,511)
Proceeds from stock-based compensation	82	227
Net cash used for financing activities	(5,587)	(4,284)
Effect of exchange rate changes on cash and cash equivalents	173	343
Net decrease in cash and cash equivalents	(357)	(533)
Cash and cash equivalents at beginning of period	26,748	26,089
Cash and cash equivalents at end of period	$ 26,391	$ 25,556

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

(A) BASIS OF PREPARATION

The financial information included in these financial statements is unaudited but, in the opinion of management, reflects all normal recurring and other adjustments necessary for a fair presentation of the results for the interim periods. The interim results of operations and cash flows are not necessarily indicative of those results and cash flows for the entire year. These financial statements should be read in conjunction with the financial statements and notes to the financial statements contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2006. Certain amounts reported for the prior periods have been reclassified to conform to the current year's presentation.

(B) RECENTLY ISSUED ACCOUNTING STANDARDS

In February 2007, the Financial Accounting Standards Board, or the FASB, issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115, or Statement 159. Statement 159 allows entities to voluntarily elect to measure many financial assets and financial liabilities at fair value. The election is made on an instrument-by-instrument basis and is irrevocable. We are required to adopt Statement 159 at the beginning of 2008. The impact of the adoption of Statement 159 will be dependent upon the extent to which we elect to measure eligible items at fair value. We are currently evaluating the impact, if any, of adopting Statement 159 on our future results of operations and financial condition.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106, and 132(R), or Statement 158. Statement 158 requires an entity to (a) recognize in its statement of financial position an asset or an obligation for a defined benefit postretirement plan's funded status, (b) measure a defined benefit postretirement plan's assets and obligations that determine its funded status as of the end of the employer's fiscal year and (c) recognize changes in the funded status of a defined benefit postretirement plan in comprehensive income in the year in which the changes occur. We adopted the recognition and related disclosure provisions of Statement 158 effective December 31, 2006. The measurement date provision of Statement 158 is effective at the end of 2008. We do not expect the measurement date provision of adopting Statement 158 to have a significant impact on our future results of operations or financial condition.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements, or Statement 157. Statement 157 provides enhanced guidance for using fair value to measure assets and liabilities. We are required to adopt Statement 157 effective at the beginning of 2008. We are currently evaluating the impact, if any, of adopting Statement 157 on our future results of operations and financial condition.

(C) RESTRUCTURING EXPENSES

In 2006, we implemented a cost reduction plan that has resulted in lower overhead costs and annual programming and editorial expenses. As a result of the 2006 restructuring plan, we reported a charge in 2006 of $2.1 million related to costs associated with a workforce reduction of 15 employees.

During the quarter ended June 30, 2007, we recorded an unfavorable adjustment of $47 thousand related to our 2002 and 2001 restructuring plans and an unfavorable adjustment of $63 thousand related to our 2006 restructuring plan as a result of changes in plan assumptions related to excess office space and employee severance. In addition, in 2006, we recorded a favorable adjustment of $0.2 million and an unfavorable adjustment of $0.1 million related to our 2002 and 2001 restructuring plans, respectively, as a result of changes in plan assumptions primarily related to excess office space.

During the six-month period ended June 30, 2007, we made cash payments of $0.5 million related to prior years' restructuring plans. Of the total costs related to our restructuring plans, approximately $12.4 million was paid through June 30, 2007, with the remaining $0.3 million to be paid through 2008.

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The following table sets forth the activity and balances of our restructuring reserves for the year ended December 31, 2006 and for the six-month period ended June 30, 2007 (in thousands):

	Workforce Reduction	Consolidation of Facilities and Operations	Total
Balance at December 31, 2005	$ --	$ 1,210	$ 1,210
Reserve recorded	2,103	--	2,103
Adjustments to previous estimates	--	(105)	(105)
Other	--	(574)	(574)
Cash payments	(1,673)	(263)	(1,936)
Balance at December 31, 2006	430	268	698
Adjustments to previous estimates	63	47	110
Cash payments	(455)	(37)	(492)
Balance at June 30, 2007	$ 38	$ 278	$ 316

(D) EARNINGS PER COMMON SHARE

The following table sets forth the computations of basic and diluted earnings per share, or EPS (in thousands, except per share amounts):

	Quarters Ended June 30,		Six Months En June 30,
	2007	2006	2007
Numerator:			
For basic and diluted EPS - net income (loss)	$ 1,911	$ (3,307)	$ 3,385 $
Denominator:			
For basic EPS - weighted average shares	33,243	33,158	33,236
Effect of dilutive potential common shares:			
Employee stock options and other	29	--	35
Dilutive potential common shares	29	--	35
For diluted EPS - weighted average shares	33,272	33,158	33,271

Basic and diluted earnings (loss)

per common share	$ 0.06	$ (0.10)	$ 0.10	$

The following table sets forth the number of shares related to outstanding options to purchase our Class B common stock, or Class B stock, and the potential shares of Class B stock contingently issuable under our 3.00% convertible senior subordinated notes due 2025, or convertible notes. These shares were not included in the computations of diluted EPS for the quarters and six-month periods ended June 30, 2007 and 2006, as their inclusion would have been antidilutive (in thousands):

	Quarters Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Stock options	3,283	3,975	3,220	3,192
Convertible notes	6,758	6,758	6,758	6,758
Total	10,041	10,733	9,978	9,950

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(E) INVENTORIES

The following table sets forth inventories, which are stated at the lower of cost (specific cost and average cost) or fair value (in thousands):

	June 30, 2007	December 31, 2006
Paper	$ 3,215	$ 2,917
Editorial and other prepublication costs	7,100	7,425
Merchandise finished goods	2,771	2,257
Total inventories	$ 13,086	$ 12,599

(F) INCOME TAXES

Our income tax provision consists of foreign income tax, which relates to our international networks and withholding tax on licensing income, for which we do not receive a current U.S. income tax benefit due to our net operating loss position. Our income tax provision also includes deferred federal and state income taxes related to the amortization of goodwill and other indefinite-lived intangibles, which cannot be offset against deferred tax assets due to the indefinite reversal period of the deferred tax liabilities.

We utilize the liability method of accounting for income taxes as set forth in Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes. We record net deferred tax assets to the extent we believe these assets will more likely than not be realized. In making such determination, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial performance. As a result of our recent cumulative losses in the U.S. and certain foreign jurisdictions, we have concluded that a full valuation allowance should be recorded for such jurisdictions.

In June 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, or FIN 48. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on description, classification, interest and penalties, accounting in interim periods, disclosure and transition. We adopted FIN 48 on January 1, 2007. Pursuant to FIN 48 and as a result of the implementation of FIN 48, we recognized no adjustment in the liability for unrecognized income tax benefits. There have been no material changes to the amount of uncertain tax positions since the adoption of FIN 48. At June 30, 2007, we did not have any material unrecognized income tax benefits. We do not expect to recognize significant increases or decreases in unrecognized income tax benefits over the next 12 months.

Our continuing practice is to recognize interest and/or penalties related to income tax matters in income tax expense.

We file U.S., state and foreign income tax returns in jurisdictions with varying statutes of limitations. The 2003 through 2006 tax years generally remain subject to examination by federal and most state tax authorities.

(G) CONTINGENCIES

In 2006, we recorded a charge of $1.8 million, based on an agreement in principle, for the settlement of litigation with Directrix, Inc., or Directrix. The settlement amount, which was subject to Bankruptcy Court approval, was paid in August 2007. The settlement is a compromise of disputed claims and is not an admission of liability. We believe that we had good defenses against Directrix's claims, but made the reasonable business decision to settle the litigation to avoid further management distraction and defense costs, which we had estimated would have approximately equaled the amount of the settlement.

In 2006, we acquired Club Jenna, Inc. and related companies, a multimedia adult entertainment business, to complement our existing television, online and DVD businesses. We paid $7.7 million at closing and $1.6 million in 2007 with additional payments of $1.7 million, $2.3 million and $4.3 million required in 2008, 2009 and 2010,

respectively. Pursuant to the acquisition agreement, we are also obligated to make future contingent earnout payments based primarily on sales of existing content of the acquired business over a ten-year period and on content produced by the acquired business during the five-year period after the closing of the acquisition. If the required performance benchmarks are achieved, any contingent earnout payments will be recorded as additional purchase price. No earnout payments have been made through June 30, 2007.

In 2005, we acquired an affiliate network of websites to complement our existing online business. We paid $8.0 million at closing and $2.0 million in 2006, and an additional payment of $2.0 million is required in 2007. Pursuant to the asset purchase agreement, we are also obligated to make future contingent earnout payments over a five-year period based primarily on the financial performance of the acquired business. If the required performance benchmarks are achieved, any contingent earnout payments will be recorded as additional purchase price and/or compensation expense. During 2007 and 2006, earnout payments of $0.1 million were made each year and recorded as additional purchase price.

In 2002, a $4.4 million verdict was entered against us by a state trial court in Texas in a lawsuit with a former publishing licensee. We terminated the license in 1998 due to the licensee's failure to pay royalties and other amounts due us under the license agreement. We appealed and the State Appellate Court reversed the judgment by the trial court, rendered judgment for us on the majority of plaintiffs' claims and remanded the remaining claims for a new trial. We filed a petition for review with the Texas Supreme Court. We have posted a bond in the amount of approximately $9.4 million, which represents the amount of the judgment, costs and estimated pre- and post-judgment interest. We, on advice of legal counsel, believe that it is not probable that a material judgment against us will be sustained and have not recorded a liability for this case in accordance with Statement of Financial Accounting Standards No. 5, Accounting for Contingencies.

(H) BENEFIT PLANS

We currently maintain a practice of paying a separation allowance under our salary continuation policy to employees with at least five years of continuous service who voluntarily terminate employment with us and are at age 60 or thereafter, which is not funded. We made cash payments under this policy of $0.1 million and $0.2 million during the quarter and six-month period ended June 30, 2007, respectively, and $0.1 million and $0.2 million during the quarter and six-month period ended June 30, 2006, respectively.

(I) STOCK-BASED COMPENSATION

Upon adoption of Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment, or Statement 123(R), we began estimating the value of options on the date of grant using the Lattice Binomial model, or Lattice model. The Lattice model requires extensive analysis of actual exercise and cancellation data and includes a number of complex assumptions related to expected volatility, risk-free interest rate, expected dividends and option exercises and cancellations.

The following table sets forth the assumptions used for the Lattice model:

	Quarters Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Expected volatility	25% - 41%	29% - 43%	25% - 41%	29% - 43%
Weighted average volatility	34%	38%	34%	38%
Risk-free interest rate	4.67% - 5.04%	4.32% - 4.66%	4.67% - 5.04%	4.32% - 4.66%
Expected dividends	--	--	--	--

The expected life of stock options represents the weighted average period the stock options are expected to remain outstanding and is a derived output of the Lattice model. The expected life of stock options is impacted by all of the underlying assumptions and calibration of the Lattice model. The Lattice model assumes that exercise behavior is a function of the option's contractual term, vesting schedule and the extent to which the option's intrinsic value exceeds the exercise price.

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During the quarter and six-month period ended June 30, 2007, we granted 160,000 stock options, exercisable for shares of our Class B Stock, which will vest over a three-year period from the grant date and expire ten years from the grant date. There were no stock options granted during the second quarter of 2006; during the six-month period ended June 30, 2006, we granted 670,500 stock options. The weighted average expected life for options granted during the current quarter and six-month period was 6.3 years and during the six-month period of 2006 was 5.8 years. The weighted average fair value per share for stock options granted during the current quarter and six-month period was $4.64 and during the six-month period of 2006 was $6.40.

During the quarter and six-month period ended June 30, 2007, we granted 250,625 restricted stock units, which provide for the issuance of our Class B stock if our two-year cumulative operating income target thresholds are met as of December 31, 2008, with an additional one-year holding period for restricted stock units that vest based on performance. There were no restricted stock units granted during the second quarter of 2006; during the six-month period ended June 30, 2006, we granted 188,500 restricted stock units. The weighted average grant date fair value for restricted stock units granted during the current quarter and six-month period was $10.61 and during the six-month period of 2006 was $14.51.

The following table sets forth stock-based compensation expense related to stock options, restricted stock units, other equity awards and our employee stock purchase plan, or ESPP (in thousands):

	Quarters Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Stock options	$ 448	$ 796	$ 165	$ 1,505
Restricted stock units	87	160	87	195
Other equity awards	50	37	92	80
ESPP	8	8	15	14
Total	$ 593	$ 1,001	$ 359	$ 1,794

Statement 123(R) requires that the total amount of compensation expense recognized reflects the number of stock options that actually vest as of the completion of the vesting period. Upon the vesting of certain stock option grants, we adjusted our stock-based compensation expense to reflect actual versus estimated forfeitures. During the quarter ended March 31, 2007, we recorded a favorable adjustment of $1.0 million to reflect that actual forfeitures for vested stock option grants exceeded the estimated amounts.

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(J) SEGMENT INFORMATION

The following table sets forth financial information by reportable segment (in thousands):

	Quarters Ended June 30,	Six Months Ended June 30,

	2007	2006	2007	2006
Net revenues				
Entertainment	$ 51,838	$ 47,545	$ 102,696	$ 98,722
Publishing	22,658	23,790	46,003	47,285
Licensing	11,156	9,142	22,368	16,590
Total	$ 85,652	$ 80,477	$ 171,067	$ 162,597
Income (loss) before income taxes				
Entertainment	$ 7,301	$ 4,881	$ 11,605	$ 12,754
Publishing	(2,273)	(1,752)	(4,669)	(4,049)
Licensing	5,523	4,076	13,200	8,422
Corporate Administration and Promotion	(6,588)	(6,552)	(12,288)	(12,943)
Restructuring expenses	(110)	(1,906)	(110)	(1,906)
Gain on disposal	--	29	--	29
Investment income	623	602	1,098	1,209
Interest expense	(1,204)	(1,281)	(2,566)	(2,709)
Amortization of deferred financing fees	(134)	(134)	(268)	(268)
Other, net	(168)	50	(307)	(146)
Total	$ 2,970	$ (1,987)	$ 5,695	$ 393

	June 30, 2007	Dec. 31, 2006
Identifiable assets		
Entertainment	$ 283,998	$ 288,540
Publishing	35,071	38,146
Licensing	11,368	9,386
Corporate Administration and Promotion	108,718	99,711
Total	$ 439,155	$ 435,783

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This discussion should be read in conjunction with the Condensed Consolidated Financial Statements and accompanying notes in Item 1 and with our Annual Report on Form 10-K for the year ended December 31, 2006. All period references are to our fiscal periods unless otherwise indicated.

RESULTS OF OPERATIONS (1)

The following table sets forth our results of operations (in millions, except per share amounts):

	Quarters Ended June 30,	Six Months Ended June 30,

	2007	2006	2007	2006
Net revenues				
Entertainment				
Domestic TV	$ 21.6	$ 20.9	$ 41.3	$ 43.2
International TV	13.7	11.7	27.5	24.1
Online/mobile	14.6	13.5	30.3	28.8
Other	1.9	1.4	3.6	2.6
Total Entertainment	51.8	47.5	102.7	98.7
Publishing				
Domestic magazine	19.0	20.2	38.1	39.4
International magazine	1.8	1.6	3.7	3.3
Special editions and other	1.9	2.0	4.2	4.6
Total Publishing	22.7	23.8	46.0	47.3
Licensing				
Consumer products	7.5	6.9	16.2	13.7
Location-based entertainment	0.9	--	1.8	--
Marketing events	2.3	2.3	2.6	2.5
Other	0.5	--	1.8	0.4
Total Licensing	11.2	9.2	22.4	16.6
Total net revenues	$ 85.7	$ 80.5	$ 171.1	$ 162.6
Net income (loss)				
Entertainment				
Before programming amortization and online content expenses	$ 17.4	$ 15.2	$ 31.9	$ 32.5
Programming amortization and online content expenses	(10.1)	(10.3)	(20.3)	(19.7)
Total Entertainment	7.3	4.9	11.6	12.8
Publishing	(2.3)	(1.8)	(4.7)	(4.1)
Licensing	5.5	4.1	13.2	8.4
Corporate Administration and Promotion	(6.6)	(6.5)	(12.3)	(12.9)
Segment income	3.9	0.7	7.8	4.2
Restructuring expenses	(0.1)	(1.9)	(0.1)	(1.9)
Operating income (loss)	3.8	(1.2)	7.7	2.3
Nonoperating income (expense)				
Investment income	0.6	0.6	1.1	1.2
Interest expense	(1.1)	(1.3)	(2.5)	(2.7)
Amortization of deferred financing fees	(0.2)	(0.2)	(0.3)	(0.3)
Other, net	(0.1)	0.1	(0.3)	(0.1)
Total nonoperating expense	(0.8)	(0.8)	(2.0)	(1.9)
Income (loss) before income taxes	3.0	(2.0)	5.7	0.4
Income tax expense	(1.1)	(1.3)	(2.3)	(2.9)
Net income (loss)	$ 1.9	$ (3.3)	$ 3.4	$ (2.5)

Basic and diluted earnings (loss) per common share	$ 0.06	$ (0.10)	$ 0.10	$ (0.08)

(1) Certain amounts reported for the prior periods have been reclassified to conform to the current year's presentation.

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Our revenues increased $5.2 million, or 6.4%, and $8.5 million, or 5.2%, for the quarter and six-month period, respectively, driven by higher revenues from our Entertainment and Licensing Groups.

Segment income increased $3.2 million and $3.6 million for the quarter and six-month period, respectively. The quarter comparison reflected increased profits from our Entertainment and Licensing Groups, which were partially offset by lower Publishing Group results. The six-month comparison reflected increased profits from our Licensing Group and lower Corporate Administration and Promotion expenses, partially offset by lower results from our Entertainment and Publishing Groups.

Operating income increased $5.0 million and $5.4 million for the quarter and six-month period, respectively, due to the improved segment income coupled with $1.8 million lower restructuring expenses in the current year.

Net income of $1.9 million and $3.4 million for the quarter and six-month period, respectively, improved by $5.2 million and $5.9 million compared to the respective prior year periods primarily due to the operating results previously discussed.

Several of our businesses may experience variations in quarterly performance. As a result, our performance in any quarter is not necessarily reflective of full-year or longer-term trends. Playboy magazine newsstand revenues vary from issue to issue, with revenues generally higher for holiday issues and any issues including editorial or pictorial features that generate additional public interest. Advertising revenues also vary from quarter to quarter depending on economic conditions, holiday issues and changes in advertising buying patterns. Online subscription revenues and operating results are impacted by decreased Internet traffic during the summer months, and e-commerce revenues and operating results are typically strongest in the fourth quarter due to the holiday buying season.

ENTERTAINMENT GROUP

The following discussion focuses on the revenues and profit contribution of each of our Entertainment Group businesses before programming amortization and online content expenses.

Revenues from our domestic TV networks increased $0.7 million, or 4%, for the quarter and decreased $1.9 million, or 4%, for the six-month period. The increase for the quarter was primarily due to higher video-on-demand, or VOD, revenues net of lower movie network revenues, together with an increase in Playboy TV revenues. The decrease in revenues for the six-month period was principally due to a decrease in movie network revenues, net of higher VOD revenues coupled with lower linear Playboy TV revenues. Favorable variances related to previously estimated revenues also impacted the quarter and six-month period. We believe that second half domestic TV revenues will be approximately equal to the first half, excluding the favorable variances related to previously estimated revenues.

Profit contribution from our domestic TV networks increased $0.9 million for the quarter and decreased $1.1 million for the six-month period. In addition to the previously discussed revenue performance, profit contribution was also impacted by lower marketing expenses related to timing of expenditures, partially offset by increased volume-related VOD distribution expenses and expense related to certain carriage distribution agreements that we began amortizing during the fourth quarter of the prior year.

International TV revenues increased $2.0 million, or 16%, and $3.4 million, or 14%, and profit contribution increased $1.7 million and $1.5 million for the quarter and six-month period, respectively, reflecting revenue growth in our UK and other European networks. While foreign exchange rate fluctuations resulted in increases in both revenues and expenses, the fluctuations had an immaterial impact on profit contribution. We believe that international TV revenues will continue to improve for the remainder of 2007.

Online/mobile revenues increased $1.1 million, or 8%, and $1.5 million, or 5%, and profit contribution increased $0.5 million and $1.1 million for the quarter and six-month period, respectively. Online subscription revenues were higher in both periods primarily due to our acquisition of Club Jenna, Inc. and related companies, or Club Jenna, in June 2006. E-commerce revenues were higher due to improved sales from our Playboy Catalog and revenues from our new BUNNYshop Catalog, more than offsetting the impact of licensing our Spice Catalog in September 2006, leading to lower revenues but higher profit contribution.

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Revenues from other businesses increased $0.5 million, or 37%, and $1.0 million, or 38%, for the quarter and six-month period, respectively. Profit contribution increased $0.2 million for the quarter and decreased $0.5 million for the six-month period. The improvement was largely due to the Club Jenna acquisition, and the six-month negative comparison was largely due to a legal settlement recorded in the current year.

The group's administrative expenses increased $1.0 million, or 23%, and $1.6 million, or 16%, for the quarter and six-month period, respectively, primarily to support the acquired businesses.

Programming amortization and online content expense decreased $0.2 million, or 2%, for the quarter and increased $0.6 million, or 3%, for the six-month period. The six-month period reflected larger investments in online content. We anticipate that 2007 programming amortization and online content expense will be less than $40.0 million, compared to $41.8 million for 2006.

Segment income for the group increased $2.4 million, or 50%, for the quarter and decreased $1.2 million, or 9%, for the six-month period, respectively, due to the operating results previously discussed.

PUBLISHING GROUP

Domestic magazine revenues decreased $1.2 million, or 6%, and $1.3 million, or 3%, for the quarter and six-month period, respectively. A continuation of negative industry trends caused circulation revenues to decrease, with subscription revenues decreasing $0.9 million, or 8%, and $1.9 million, or 8%, for the quarter and six-month period, respectively, primarily due to downward pressure on both renewal rates and direct-to-publisher subscription acquisitions. Newsstand revenues decreased $0.2 million, or 8%, and $0.3 million, or 5%, for the quarter and six-month period, respectively, due to 10% and 7% fewer copies sold, respectively. Advertising revenues were $0.2 million lower for the quarter but $0.9 million higher for the six-month period. The quarter results reflect an 8% decrease in average net revenue per page due to a change in the mix of advertisers, partially offset by a 5% increase in advertising pages. The improvement in the six-month period reflects a 10% increase in advertising pages, partially offset by a 2% decrease in average net revenue per page, again due to a change in the mix of advertisers. Advertising sales for the 2007 third quarter magazine issues are closed, and we expect to report approximately 5% higher advertising revenues and a 9% increase in advertising pages compared to the 2006 third quarter.

International magazine revenues increased $0.2 million, or 14%, and $0.4 million, or 13%, for the quarter and six-month period, respectively.

Special editions and other revenues were flat for the quarter and decreased $0.4 million, or 9%, for the six-month period. Fewer special editions newsstand copies sold in both periods resulted in lower revenues of $0.4 million and $0.6 million for the quarter and six-month period, respectively.

The group's segment loss increased $0.5 million, or 30%, and $0.6 million, or 15%, for the quarter and six-month period, respectively, because the periods also included post-employment benefit costs related to senior editorial employees and additional expensing of subscription collection costs. On a comparable basis, segment results would have improved for the quarter and six-month period as cost reductions more than offset the circulation revenue declines previously discussed and higher editorial costs. As a result of the continuing difficult market trends and the post-employment benefit and subscription collection costs, we believe that the group's segment profitability will likely be in line with what we reported in 2005.

LICENSING GROUP

Licensing Group revenues increased $2.0 million, or 22%, and $5.8 million, or 35%, for the quarter and six-month period, respectively, reflecting royalties from our location-based entertainment venue at the Palms Casino Resort in Las Vegas, which opened in October 2006, and higher consumer products royalties. The quarter and six-month period also reflected $0.4 million and $1.7 million, respectively, in sales of original artwork compared to none and $0.4 million in the prior year periods, respectively. The group's segment income increased $1.4 million, or 36%, and $4.8 million, or 57%, for the quarter and six-month period, respectively, as a result of these revenue

increases, partially offset by growth-related costs. We continue to project growth of approximately 20 to 25% in the Licensing Group's segment income, excluding the impact of sales of original art.

CORPORATE ADMINISTRATION AND PROMOTION

Corporate Administration and Promotion expenses were flat for the quarter and decreased $0.6 million, or 5%, for the six-month period, with both periods reflecting additional expense related to certain trademark costs that were previously capitalized, the previously mentioned allocation of actual post-employment benefit costs to the Publishing Group and lower marketing expenses.

RESTRUCTURING EXPENSES

During the quarter ended June 30, 2007, we recorded an unfavorable adjustment of $0.1 million related to prior restructuring plans as a result of changes in plan assumptions. For the six-month period, we made cash payments of $0.5 million related to our restructuring plans. Of the total costs related to our restructuring plans, approximately $12.4 million was paid through June 30, 2007, with the remaining $0.3 million to be paid through 2008.

INCOME TAX EXPENSE

Our effective income tax rate differs from the U.S. statutory rate. Our income tax provision consists of foreign income tax, which relates to our international networks and withholding tax on licensing income, for which we do not receive a current U.S. income tax benefit due to our net operating loss position. Our income tax provision also includes deferred federal and state income taxes related to the amortization of goodwill and other indefinite-lived intangibles, which cannot be offset against deferred tax assets due to the indefinite reversal period of the deferred tax liabilities.

In June 2006, the Financial Accounting Standards Board, or the FASB, issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109, or FIN 48. We adopted FIN 48 on January 1, 2007. Pursuant to FIN 48 and as a result of the implementation of FIN 48, we recognized no adjustment in the liability for unrecognized income tax benefits. There have been no material changes to the amount of uncertain tax positions since the adoption of FIN 48. At June 30, 2007, we did not have any material unrecognized income tax benefits. We do not expect to recognize significant increases or decreases in unrecognized tax benefits over the next 12 months.

LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2007, we had $26.4 million in cash and cash equivalents compared to $26.7 million in cash and cash equivalents at December 31, 2006. We also had $9.0 million and $3.0 million of auction rate securities, or ARS, included in marketable securities and short-term investments at June 30, 2007 and December 31, 2006, respectively. ARS generally have long-term maturities; however, these investments have characteristics similar to short-term investments because at predetermined intervals, typically every 28 days, there is a new auction process. Total financing obligations were $115.0 million at both June 30, 2007 and December 31, 2006.

At June 30, 2007, cash generated from our operating activities, existing cash and cash equivalents and marketable securities and short-term investments were fulfilling our liquidity requirements. In addition, our $50.0 million credit facility, which can be used for revolving borrowings, issuing letters of credit or a combination of both, had no borrowings and $10.6 million in letters of credit outstanding, resulting in $39.4 million of available borrowings under this facility at June 30, 2007.

CASH FLOWS FROM OPERATING ACTIVITIES

Net cash provided by operating activities for the six months ended June 30, 2007 was $16.6 million, an increase of $13.3 million compared to the prior year period primarily due to changes in working capital.

CASH FLOWS FROM INVESTING ACTIVITIES

Net cash used for investing activities for the six months ended June 30, 2007 was $11.5 million, an increase of $11.7 million compared to the prior year period. This increase was primarily due to the purchase of $6.0 million in ARS and capital expenditures of $5.0 million, which were primarily related to leasehold improvements at our New York office and Los Angeles programming facility and technology-related items. The prior year period reflected proceeds of $11.0 million from the sale of investments and payments of $7.8 million primarily related to the acquisition of Club Jenna.

CASH FLOWS FROM FINANCING ACTIVITIES

Net cash used for financing activities for the six months ended June 30, 2007 was $5.6 million, an increase of $1.3 million compared to the prior year period primarily due to acquisition liability payments related to Califa Entertainment Group, Inc. and Club Jenna.

EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS

The positive effect of foreign currency exchange rates on cash and cash equivalents during the current year and prior year was due to the weakening of the U.S. dollar against the pound sterling and Euro.

RECENTLY ISSUED ACCOUNTING STANDARDS

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115, or Statement 159. Statement 159 allows entities to voluntarily elect to measure many financial assets and financial liabilities at fair value. The election is made on an instrument-by-instrument basis and is irrevocable. We are required to adopt Statement 159 at the beginning of 2008. The impact of the adoption of Statement 159 will be dependent upon the extent to which we elect to measure eligible items at fair value. We are currently evaluating the impact, if any, of adopting Statement 159 on our future results of operations and financial condition.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106, and 132(R), or Statement 158. Statement 158 requires an entity to (a) recognize in its statement of financial position an asset or an obligation for a defined benefit postretirement plan's funded status, (b) measure a defined benefit postretirement plan's assets and obligations that determine its funded status as of the end of the employer's fiscal year and (c) recognize changes in the funded status of a defined benefit postretirement plan in comprehensive income in the year in which the changes occur. We adopted the recognition and related disclosure provisions of Statement 158 effective December 31, 2006. The measurement date provision of Statement 158 is effective at the end of 2008. We do not expect the measurement date provision of adopting Statement 158 to have a significant impact on our future results of operations or financial condition.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements, or Statement 157. Statement 157 provides enhanced guidance for using fair value to measure assets and liabilities. We are required to adopt Statement 157 effective at the beginning of 2008. We are currently evaluating the impact, if any, of adopting Statement 157 on our future results of operations and financial condition.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

At June 30, 2007, we did not have any floating interest rate exposure. All of our outstanding debt as of that date consisted of the 3.00% convertible senior subordinated notes due 2025, or convertible notes, which are fixed-rate obligations. The fair value of the $115.0 million aggregate principal amount of the convertible notes is influenced by changes in market interest rates, the share price of our Class B stock and our credit quality. At June 30, 2007, the convertible notes had an implied fair value of $110.9 million.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act) as of the end of the period covered by this quarterly report. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act.

Internal Control over Financial Reporting

There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II
OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

There have been no material changes to our Legal Proceedings as contained in our Annual Report on Form 10-K for the year ended December 31, 2006.

ITEM 1A. RISK FACTORS

There have been no material changes to our Risk Factors as contained in our Annual Report on Form 10-K for the year ended December 31, 2006.

ITEM 4. SUBMISSIONS OF MATTERS TO A VOTE OF SECURITY HOLDERS

Our annual meeting of shareholders was held on May 23, 2007. At the meeting, the following director nominees were elected:

Nominee (1)	Votes For	Votes Withheld
Dennis S. Bookshester	4,457,959	193,985
David I. Chemerow	4,457,984	193,960
Christie Hefner	4,003,614	648,330
Charles Hirschhorn	4,458,108	193,836
Jerome H. Kern	4,457,954	193,990
Russell I. Pillar	4,435,529	216,415
Sol Rosenthal	4,434,671	217,273
Richard S. Rosenzweig	4,003,121	648,823

(1) On April 30, 2007, Donald G. Drapkin resigned from our Board of Directors, effective immediately, in connection with his appointment as a Vice Chairman of Lazard International and Chairman of the Investment Committee

of Lazard Ltd. He was a member of our Board of Directors since 1997 and a member of the compensation committee. As a result, there were eight nominees for director at our 2007 Annual Meeting of Stockholders.

Also at the meeting, the shareholders approved, with voting as set forth below, (a) an amendment to our Second Amended and Restated 1995 Stock Incentive Plan, or the 1995 Stock Incentive Plan, (b) an amendment to our Amended and Restated 1997 Equity Plan for Non-Employee Directors, or the 1997 Equity Plan for Non-Employee Directors, (c) an amendment to our Employee Stock Purchase Plan, or ESPP, and (d) ratification of Ernst & Young LLP as our independent registered public accounting firm, or Auditors:

Matter	Votes For	Votes Against	Abstain	Broker Non-Votes
1995 Stock Incentive Plan	3,787,067	500,773	788	363,316
1997 Equity Plan for Non-Employee Directors	3,644,118	643,470	1,040	363,316
ESPP	4,270,638	16,974	1,016	363,316
Auditors	4,641,945	4,291	5,712	N/A

ITEM 6. EXHIBITS

Exhibit Number	Description
10.1*	Agreement dated October 4, 2004, between Playboy Enterprises International, Inc. and Fiesta Palms LLC, N-M Ventures II, LLC and Nine Group LLC
10.2	Third Amended and Restated Playboy Enterprises, Inc. 1995 Stock Incentive Plan
10.3	Second Amended and Restated 1997 Equity Plan For Non-Employee Directors of Playboy Enterprises, Inc.
10.4	Playboy Enterprises, Inc. Employee Stock Purchase Plan, as amended and restated
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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* Portions of this exhibit have been omitted and filed separately with the SEC pursuant to a request for confidential treatment pursuant to Rule 24b-2 of the Exchange Act.

SIGNATURES

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

PLAYBOY ENTERPRISES, INC.
(Registrant)

Date: August 9, 2007

By /s/ Linda Havard
Linda G. Havard
Executive Vice President,
Finance and Operations,
and Chief Financial Officer
(Authorized Officer and
Principal Financial and
Accounting Officer)

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