

UNITED STATES CELLULAR CORP
Form 10-Q/A
February 23, 2007

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

Amendment No. 1

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

For the quarterly period ended June 30, 2006 OR

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

For the transition period from _____ to _____

Commission File Number 1-9712

UNITED STATES CELLULAR CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

62-1147325

(I.R.S. Employer Identification No.)

8410 West Bryn Mawr, Suite 700, Chicago, Illinois 60631

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: **(773) 399-8900**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant 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):

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Large accelerated filer Accelerated filer Accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

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

Class	Outstanding at August 31, 2006
Common Shares, \$1 par value	54,197,834 Shares
Series A Common Shares, \$1 par value	33,005,877 Shares

Explanatory Note

United States Cellular Corporation. (U.S. Cellular) is filing this Amendment No. 1 to its Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2006, which was originally filed with the Securities and Exchange Commission (SEC) on October 10, 2006 (Original Form 10-Q), to amend Part I Financial Information Item 1 Financial Statements, Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A), Item 3 Quantitative and Qualitative Disclosures About Market Risk, and Item 4 Controls and Procedures, and Item 6 Exhibits and Financial Statement Schedules.

As discussed in Note 1 to the Consolidated Financial Statements, U.S. Cellular and its audit committee concluded on November 6, 2006, that U.S. Cellular would amend its Annual Report on Form 10-K for the year ended December 31, 2005 to restate its consolidated financial statements and financial information for each of the three years in the period ended December 31, 2005, including quarterly information for 2005 and 2004 and certain selected financial data for 2002. U.S. Cellular and its audit committee also concluded that U.S. Cellular would amend its Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, 2006 and June 30, 2006 to restate the consolidated financial statements and financial information included therewith.

The restatement adjustments are described below.

- **Forward contracts and related derivative instruments** - In reviewing the accounting and disclosure of its prepaid forward contracts, U.S. Cellular concluded that its continued designation of the embedded collars within the forward contracts as cash flow hedges of marketable equity securities was not appropriate. U.S. Cellular did not contemporaneously de-designate, re-designate, and assess hedge effectiveness when the embedded collars were contractually modified for differences between the actual and expected dividend rates on the underlying securities in 2002. As a result, the embedded collars no longer qualified for cash flow hedge accounting treatment upon the modification of the terms of the collars for changes in dividend rates and, from that point forward, must be accounted for as derivative instruments that do not qualify for cash flow hedge accounting treatment. Accordingly, all changes in the fair value of the embedded collars from the time of the contractual modification of each collar must be recognized in the statement of operations. The restatement adjustments represent reclassifications of unrealized gains or losses related to changes in the fair value of the embedded collars from other comprehensive income or loss, included in common stockholders' equity, to the statement of operations.
- **Contracts with maintenance and support services** - U.S. Cellular entered into certain equipment and software contracts that included maintenance and support services. In one case, U.S. Cellular did not properly allocate expenditures between equipment purchases and maintenance and support services. In other cases, U.S. Cellular did not properly record fees for maintenance and support services over the specified term of the agreement. The restatement adjustments properly record property, plant and equipment, related depreciation expense and fees for maintenance and support services in the correct periods.
- **Classification of Asset Retirement Obligation on the Statement of Cash Flows** - The additions to property, plant and equipment and other deferred liabilities representing additional asset retirement obligations (ARO) should be treated as non-cash items in the statement of cash flows. From 2004 through the second quarter of 2006, U.S. Cellular included additional ARO liabilities as a change in other assets and liabilities in cash flows from operating activities and the increase in the ARO asset balance as a capital expenditure in cash flows from investing activities resulting in an overstatement of cash flows from operating activities and an overstatement of cash flows required by investing activities. In the restatement, adjustments were recorded in the statement of cash flows to offset the change in ARO liabilities against the ARO asset.
- **Income taxes** - U.S. Cellular is included in a consolidated federal income tax return with other members of the TDS consolidated group. In the restatement, U.S. Cellular adjusted its income tax expense, income taxes payable, goodwill, deferred income tax assets and liabilities and related disclosures for the years ended December 31, 2005, 2004, 2003 and 2002 for items identified based on its annual analysis reconciling its 2005 income tax expense and income tax balance sheet accounts as determined in its comparison of the 2005 year-end income tax provision to the

2005 federal and state income tax returns. These adjustments included corrections for certain accounts that had not previously been included in the financial reporting basis used in determining the cumulative temporary differences in computing deferred income tax assets and liabilities, as well as adjustments to certain cumulative temporary differences that had historically been incorrectly associated with operating license assets which, in this restatement, have been correctly classified as investments in partnership assets. Accordingly, the company has adjusted the deferred tax liabilities related to these assets. Goodwill was adjusted to record the income tax effect of the difference between the financial reporting basis and the income tax basis of certain acquisitions made prior to 2004.

- **Property, plant and equipment** U.S. Cellular did not properly record certain transfers and disposals of equipment removed from service. Also, U.S. Cellular did not properly record depreciation expense for certain leasehold improvements and other equipment due to the use of incorrect asset lives. The restatement adjustments properly record equipment disposals and depreciation expense in the correct amounts and periods.
- **Other items** In addition to the adjustments described above, U.S. Cellular recorded a number of other adjustments to correct and record revenues, expenses and equity in earnings of unconsolidated entities in the periods in which such revenues, expenses and equity in earnings of unconsolidated entities were earned or incurred. Adjustments were also made to correct certain balance sheet amounts. These individual adjustments were not material.

In connection with the restatement, U.S. Cellular concluded that certain material weaknesses existed in its internal control over financial reporting. See Part I Item 4 Controls and Procedures.

For the convenience of the reader, this Form 10-Q/A sets forth the Original Form 10-Q, as amended hereby, in its entirety. However, this Form 10-Q/A amends and restates only Items 1, 2, 3, and 4 of Part I and Item 6 of Part II of the Original Form 10-Q, in each case solely as a result of and to reflect the adjustments discussed above and more fully in Note 1 of the accompanying consolidated financial statements, and no other information in the Original Form 10-Q is amended hereby. The foregoing items have not been updated to reflect other events occurring after the filing of the Original Form 10-Q, or to modify or update those disclosures affected by other subsequent events. In particular, forward-looking statements included in the Form 10-Q/A represented management's views as of the date of filing of the Original Form 10-Q for the quarterly period ended June 30, 2006 on October 10, 2006. Such forward-looking statements should not be assumed to be accurate as of any future date. U.S. Cellular undertakes no duty to update such information whether as a result of new information, future events or otherwise.

As required by Rule 12b-15 under the Securities Exchange Act of 1934, as amended, new certifications by U.S. Cellular's principal executive officer and principal financial officer are being filed with this Form 10-Q/A as Exhibits 31.1, 31.2, 32.1 and 32.2.

UNITED STATES CELLULAR CORPORATION

QUARTERLY REPORT ON FORM 10-Q/A

FOR THE PERIOD ENDED JUNE 30, 2006

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PART I. FINANCIAL INFORMATIONITEM I. FINANCIAL STATEMENTSUNITED STATES CELLULAR CORPORATION AND SUBSIDIARIESCONSOLIDATED STATEMENTS OF OPERATIONSUnaudited

	Three Months Ended June 30, 2006 (As Restated)		Six Months Ended June 30, 2006 (As Restated)	
	2005 (As Restated)	2005 (As Restated)	2005 (As Restated)	2005 (As Restated)
	(Dollars in thousands, except per share amounts)			
OPERATING REVENUES				
Service	\$ 791,705	\$ 689,734	\$ 1,560,927	\$ 1,360,227
Equipment sales	54,432	50,643	121,586	90,199
Total Operating Revenues	846,137	740,377	1,682,513	1,450,426
OPERATING EXPENSES				
System operations (excluding Depreciation, amortization and accretion shown separately below)	150,555	147,401	303,873	286,943
Cost of equipment sold	133,416	116,811	276,732	244,059
Selling, general and administrative (including charges from affiliates of \$25.3 million and \$21.8 million for the three months ended June 30, 2006 and 2005, respectively, and \$49.6 million and \$41.2 million for the six months ended 2006 and 2005, respectively)	342,769	284,789	670,473	563,742
Depreciation, amortization and accretion	140,486	126,120	282,511	254,006
Total Operating Expenses	767,226	675,121	1,533,589	1,348,750
OPERATING INCOME	78,911	65,256	148,924	101,676
INVESTMENT AND OTHER INCOME (EXPENSE)				
Equity in earnings of unconsolidated entities	21,957	17,378	41,440	31,815
Interest and dividend income	9,807	4,643	10,395	6,500
Fair value adjustment of derivative instruments	(922)	20,183	3,893	24,179
Gain on investments				551
Interest expense	(23,007)	(21,444)	(46,215)	(42,182)
Other income, net	(140)	(71)	62	155
Total Investment and Other Income (Expense)	7,695	20,689	9,575	21,018
INCOME BEFORE INCOME TAXES AND MINORITY INTEREST				
INTEREST	86,606	85,945	158,499	122,694
Income tax expense	33,683	33,781	62,393	47,989
INCOME BEFORE MINORITY INTEREST	52,923	52,164	96,106	74,705
Minority share of income	(2,859)	(2,349)	(6,596)	(4,596)
NET INCOME	\$ 50,064	\$ 49,815	\$ 89,510	\$ 70,109
BASIC WEIGHTED AVERAGE SHARES OUTSTANDING (000s)				
	87,281	86,708	87,247	86,558
BASIC EARNINGS PER SHARE (Note 6)				
	\$ 0.57	\$ 0.57	\$ 1.03	\$ 0.81
	88,083	87,375	87,994	87,257

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DILUTED WEIGHTED AVERAGE SHARES
OUTSTANDING (000s)

DILUTED EARNINGS PER SHARE (Note 6)	\$ 0.57	\$ 0.57	\$ 1.02	\$ 0.80
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The accompanying notes to consolidated financial statements are an integral part of these statements.

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UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIESCONSOLIDATED STATEMENTS OF CASH FLOWSUnaudited

	Six Months Ended June 30, 2006 (As Restated) (Dollars in thousands)		2005 (As Restated)
CASH FLOWS FROM OPERATING ACTIVITIES			
Net income	\$	89,510	\$ 70,109
Add (deduct) adjustments to reconcile net income to net cash provided by operating activities			
Depreciation, amortization and accretion		282,511	254,006
Bad debts expense		23,089	14,296
Stock-based compensation expense		10,457	3,533
Deferred income taxes, net		(978)	41,834
Equity in earnings of unconsolidated entities		(41,440)	(31,815)
Distributions from unconsolidated entities		37,176	27,660
Minority share of income		6,596	4,596
Fair value adjustment for derivative instruments		(3,893)	(24,179)
Gain on investments			(551)
Noncash interest expense		890	890
Changes in assets and liabilities from operations			
Change in accounts receivable		(51,819)	(22,584)
Change in inventory		10,770	21,791
Change in accounts payable		(33,462)	(44,594)
Change in customer deposits and deferred revenues		2,978	7,815
Change in accrued taxes		6,416	10,871
Change in accrued interest		749	(123)
Change in other assets and liabilities		(19,326)	(9,353)
		320,224	324,202
CASH FLOWS FROM INVESTING ACTIVITIES			
Additions to property, plant and equipment		(268,607)	(253,535)
Cash received from divestitures			551
Cash paid for acquisitions		(18,546)	(126,033)
Other investing activities		(3,083)	(1,358)
		(290,236)	(380,375)
CASH FLOWS FROM FINANCING ACTIVITIES			
Issuance of notes payable		195,000	310,000
Repayment of notes payable		(225,000)	(290,000)
Common shares reissued		3,856	14,012
Capital (distributions) to minority partners		(11,220)	(1,060)
Other financing activities		342	(196)
		(37,022)	32,756
NET DECREASE IN CASH AND CASH EQUIVALENTS		(7,034)	(23,417)
CASH AND CASH EQUIVALENTS			
Beginning of period		29,003	41,062
End of period	\$	21,969	\$ 17,645

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

UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIESCONSOLIDATED BALANCE SHEETSASSETSUnaudited

	June 30, 2006 (As Restated)	December 31, 2005 (As Restated)
	(Dollars in thousands)	
CURRENT ASSETS		
Cash and cash equivalents	\$ 21,969	\$ 29,003
Accounts receivable		
Customers, less allowance of \$10,494 and \$11,410, respectively	291,453	278,170
Roaming	40,102	27,178
Other	60,079	57,011
Marketable equity securities	218,226	
Inventory	82,239	92,748
Prepaid expenses	44,024	32,068
Deferred income tax asset		8,218
Other current assets	21,763	15,489
	779,855	539,885
INVESTMENTS		
Licenses	1,367,569	1,362,263
Goodwill	485,543	481,235
Customer lists, net of accumulated amortization of \$56,309 and \$44,616, respectively	37,998	47,649
Marketable equity securities	4,076	225,387
Investments in unconsolidated entities	176,653	172,093
Notes and interest receivable	4,847	4,707
	2,076,686	2,293,334
PROPERTY, PLANT AND EQUIPMENT		
In service and under construction	4,862,357	4,615,234
Less accumulated depreciation	2,292,799	2,062,205
	2,569,558	2,553,029
OTHER ASSETS AND DEFERRED CHARGES		
	30,125	29,985
TOTAL ASSETS	\$ 5,456,224	\$ 5,416,233

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

UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIESCONSOLIDATED BALANCE SHEETSLIABILITIES AND SHAREHOLDERS EQUITYUnaudited

	June 30, 2006 (As Restated) (Dollars in thousands)	December 31, 2005 (As Restated)
CURRENT LIABILITIES		
Forward contracts	\$ 159,856	\$
Notes payable	105,000	135,000
Accounts payable		
Affiliated	10,881	7,239
Trade	264,488	301,058
Customer deposits and deferred revenues	114,947	111,407
Accrued taxes	47,785	36,748
Accrued compensation	35,757	42,865
Derivative liability	21,925	
Deferred income tax liability	43,015	
Other current liabilities	41,865	28,404
	845,519	662,721
DEFERRED LIABILITIES AND CREDITS		
Net deferred income tax liability	588,716	647,086
Derivative liability		25,818
Asset retirement obligation	98,319	90,224
Other deferred liabilities and credits	51,074	46,234
	738,109	809,362
LONG-TERM DEBT		
Long-term debt	1,001,612	1,001,385
Forward contracts		159,856
	1,001,612	1,161,241
COMMITMENTS AND CONTINGENCIES (SEE NOTE 19)		
MINORITY INTEREST	37,247	41,871
COMMON SHAREHOLDERS EQUITY		
Common Shares, par value \$1 per share; authorized 140,000,000 shares; issued 55,045,685 shares	55,046	55,046
Series A Common Shares, par value \$1 per share; authorized 50,000,000 shares; issued and outstanding 33,005,877 shares	33,006	33,006
Capital in excess of par value	1,285,611	1,286,964
Treasury Shares, at cost, 847,851 and 962,863 Common Shares, respectively	(40,594)	(47,088)
Accumulated other comprehensive income	42,170	44,122
Retained earnings	1,458,498	1,368,988
	2,833,737	2,741,038
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	\$ 5,456,224	\$ 5,416,233

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

UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accounting policies of United States Cellular Corporation (U.S. Cellular) conform to accounting principles generally accepted in the United States of America (U.S. GAAP). The consolidated financial statements include the accounts of U.S. Cellular, its majority-owned subsidiaries since acquisition, general partnerships in which U.S. Cellular has a majority partnership interest and any entity in which U.S. Cellular has a variable interest that requires U.S. Cellular to recognize a majority of the entity's expected gains or losses, or both. All material intercompany accounts and transactions have been eliminated.

The consolidated financial statements included herein have been prepared by U.S. Cellular, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. However, U.S. Cellular believes that the information and disclosures included herein are adequate to make the information presented not misleading. It is suggested that these consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in U.S. Cellular's Annual Report on Form 10-K/A for the year ended December 31, 2005 (Form 10-K/A).

The accompanying unaudited consolidated financial statements contain all adjustments (consisting of only normal recurring items unless otherwise disclosed) necessary to present fairly the financial position as of June 30, 2006 and December 31, 2005, the results of operations for the three and six months ended June 30, 2006 and 2005, and the cash flows for the three and six months ended June 30, 2006 and 2005. The results of operations for the three and six months ended June 30, 2006 are not necessarily indicative of the results to be expected for the full year.

Restatement

U.S. Cellular and its audit committee concluded on November 6, 2006, that U.S. Cellular would amend its Annual Report on Form 10-K for the year ended December 31, 2005 to restate its consolidated financial statements and financial information for each of the three years in the period ended December 31, 2005, including quarterly information for 2005 and 2004, and certain selected financial data for 2002. U.S. Cellular and its audit committee also concluded that U.S. Cellular would amend its Quarterly Reports on Form 10-Q for the quarterly periods ended March 31, 2006 and June 30, 2006 to restate the consolidated financial statements and financial information included therewith.

The restatement adjustments are described below.

- Forward contracts and related derivative instruments - In reviewing the accounting and disclosure of its prepaid forward contracts, U.S. Cellular concluded that its continued designation of the embedded collars within the forward contracts as cash flow hedges of marketable equity securities was not appropriate. U.S. Cellular did not contemporaneously de-designate, re-designate, and assess hedge effectiveness when the embedded collars were contractually modified for differences between the actual and expected dividend rates on the underlying securities in 2002. As a result, the embedded collars no longer qualified for cash flow hedge accounting treatment upon the modification of the terms of the collars for changes in dividend rates and, from that point forward, must be accounted for as derivative instruments that do not qualify for cash flow hedge accounting treatment. Accordingly, all changes in the fair value of the embedded collars from the time of the contractual modification of each collar must be recognized in the statement of operations. The restatement adjustments represent reclassifications of unrealized gains or losses related to changes in the fair value of the embedded collars from other comprehensive income or loss, included in common stockholders' equity, to the statement of operations.

- **Contracts with maintenance and support services** U.S. Cellular entered into certain equipment and software contracts that included maintenance and support services. In one case, U.S. Cellular did not properly allocate expenditures between equipment purchases and maintenance and support services. In other cases, U.S. Cellular did not properly record fees for maintenance and support services over the specified term of the agreement. The restatement adjustments properly record property, plant and equipment, related depreciation expense and fees for maintenance and support services in the correct periods.
- **Classification of Asset Retirement Obligation on the Statement of Cash Flows** The additions to property, plant and equipment and other deferred liabilities representing additional asset retirement obligations (ARO) should be treated as non-cash items in the statement of cash flows. From 2004 through the second quarter of 2006, U.S. Cellular included additional ARO liabilities as a change in other assets and liabilities in cash flows from operating activities and the increase in the ARO asset balance as a capital expenditure in cash flows from investing activities resulting in an overstatement of cash flows from operating activities and an overstatement of cash flows required by investing activities. In the restatement, adjustments were recorded in the statement of cash flows to offset the change in ARO liabilities against the ARO asset. The reduction in the change in other assets and liabilities in cash flows from operating activities and the reduction in additions to property, plant and equipment in cash flows from investing activities totaled \$3.4 million and \$2.3 million in the six months ended June 30, 2006 and 2005, respectively.
- **Income taxes** U.S. Cellular is included in a consolidated federal income tax return with other members of the TDS consolidated group. In the restatement, U.S. Cellular adjusted its income tax expense, income taxes payable, goodwill, deferred income tax assets and liabilities and related disclosures for the years ended December 31, 2005, 2004, 2003 and 2002 for items identified based on its annual analysis reconciling its 2005 income tax expense and income tax balance sheet accounts as determined in its comparison of the 2005 year-end income tax provision to the 2005 federal and state income tax returns. These adjustments included corrections for certain accounts that had not previously been included in the financial reporting basis used in determining the cumulative temporary differences in computing deferred income tax assets and liabilities, as well as adjustments to certain cumulative temporary differences that had historically been incorrectly associated with operating license assets which, in this restatement, have been correctly classified as investments in partnership assets. Accordingly, the company has adjusted the deferred tax liabilities related to these assets. Goodwill was