# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**WASHINGTON, D.C. 20549**

# FORM 10-Q

x **Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**for the quarterly period ended June 30, 2012**

**OR**

o **Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**for the transition period from to .**

**COMMISSION FILE NUMBER 000-51446**

# CONSOLIDATED COMMUNICATIONS HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Delaware** | **02-0636095** |

| | |
|---|---|
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |
| **121 South 17th Street**<br>**Mattoon, Illinois** | **61938-3987** |
| (Address of Principal Executive Offices) | (Zip Code) |

**(217) 235-3311**

(Registrant s Telephone Number, including Area Code)

Indicate by checkmark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES x NO o

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

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

| | |
|---|---|
| Large accelerated filer o | Accelerated filer x |
| Non-accelerated filer o<br>(Do not check if a smaller reporting company) | Smaller reporting company o |

Indicate by checkmark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES o NO x

Indicate the number of shares outstanding of each class of Common Stock, as of the latest practicable date

| Class | Outstanding as of August 3, 2012 |
|---|---|
| Common Stock, $0.01 Par Value | 39,917,265 Shares |

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**FORM 10-Q**

**QUARTERLY REPORT**

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## PART I. FINANCIAL INFORMATION

### Item 1. Financial Statements

**Consolidated Communications Holdings, Inc. and Subsidiaries**

**Condensed Consolidated Statements of Operations**

(Unaudited)

| (In thousands, except per share amounts) | Three months ended June 30, 2012 | Three months ended June 30, 2011 | Six months ended June 30, 2012 | Six months ended June 30, 2011 |
|---|---|---|---|---|
| Net revenues | **$ 93,005** | $ 92,623 | **$ 186,369** | $ 188,064 |
| Operating expense: | | | | |
| Cost of services and products (exclusive of depreciation and amortization shown separately below) | **36,526** | 34,267 | **72,390** | 69,951 |
| Selling, general and administrative expenses | **19,996** | 19,147 | **39,524** | 39,846 |
| Financing and other transactions | **562** | 2,540 | **5,384** | 2,540 |
| Depreciation and amortization | **21,869** | 21,987 | **44,006** | 44,145 |
| Operating income | **14,052** | 14,682 | **25,065** | 31,582 |
| Other income (expense): | | | | |
| Interest expense, net of interest income | **(16,893)** | (12,397) | **(31,493)** | (24,336) |
| Investment income | **6,762** | 6,097 | **13,228** | 13,014 |
| Other, net | **185** | 210 | **199** | 437 |
| Income before income taxes | **4,106** | 8,592 | **6,999** | 20,697 |
| Income tax expense | **1,200** | 3,079 | **2,209** | 7,687 |
| Net income | **2,906** | 5,513 | **4,790** | 13,010 |
| Less: net income attributable to noncontrolling interest | **120** | 162 | **245** | 294 |
| Net income attributable to common stockholders | **$ 2,786** | $ 5,351 | **$ 4,545** | $ 12,716 |
| Net income per common share basic | **$ 0.09** | $ 0.18 | **$ 0.15** | $ 0.42 |
| Net income per common share diluted | **$ 0.09** | $ 0.18 | **$ 0.15** | $ 0.42 |
| Cash dividends per common share | **$ 0.38** | $ 0.38 | **$ 0.77** | $ 0.77 |

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

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**Consolidated Communications Holdings, Inc. and Subsidiaries**

**Condensed Consolidated Statements of Comprehensive Income**

(Unaudited)

| **(In thousands)** | **Three months ended June 30, 2012** | **Three months ended June 30, 2011** | **Six months ended June 30, 2012** | **Six months ended June 30, 2011** |
|---|---|---|---|---|
| Net income | **$ 2,906** | $ 5,513 | **$ 4,790** | $ 13,010 |
| Change in prior service cost and net of loss, net of tax of $273 and ($207) for three months ended June 30, 2012 and 2011, and $543 and $80 for the six months ended June 30, 2012 and 2011 | **448** | (357) | **897** | 135 |
| Change in fair value of cash flow hedges, net of tax of $339 and $352 for the three months ended June 30, 2012 and 2011, and $924 and $2,056 for the six months ended June 30, 2012 and 2011 | **581** | 602 | **1,584** | 3,558 |
| Comprehensive income | **3,935** | 5,758 | **7,271** | 16,703 |
| Less: comprehensive income attributable to noncontrolling interest | **120** | 162 | **245** | 294 |
| Total comprehensive income attributable to common stockholders | **$ 3,815** | $ 5,596 | **$ 7,026** | $ 16,409 |

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

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**Consolidated Communications Holdings, Inc. and Subsidiaries**

**Condensed Consolidated Balance Sheets**

| (In thousands, except share and per share amounts) | | June 30, 2012 (Unaudited) | | December 31, 2011 |
|---|---|---|---|---|
| **Assets** | | | | |
| Current assets: | | | | |
| Cash and cash equivalents | $ | 84,984 | $ | 105,704 |
| Restricted cash see footnote 4 | | 315,082 | | |
| Accounts receivable, net of allowance for doubtful accounts of $2,743 in 2012 and $2,547 in 2011 | | 35,165 | | 35,492 |
| Inventories | | 7,233 | | 7,151 |
| Income tax receivable | | 11,276 | | 8,988 |
| Deferred income taxes | | 4,825 | | 4,825 |
| Prepaid expenses and other current assets | | 7,769 | | 6,170 |
| Total current assets | | 466,334 | | 168,330 |
| Property, plant and equipment, net | | 321,047 | | 332,046 |
| Investments | | 99,423 | | 98,069 |
| Goodwill | | 520,562 | | 520,562 |
| Customer lists, net | | 46,742 | | 57,811 |
| Tradenames | | 12,347 | | 12,347 |
| Deferred debt issuance costs, net and other assets | | 12,981 | | 4,904 |
| Total assets | $ | 1,479,436 | $ | 1,194,069 |
| **Liabilities and Stockholders Equity** | | | | |
| Current liabilities: | | | | |
| Accounts payable | $ | 15,128 | $ | 13,673 |
| Advance billings and customer deposits | | 20,974 | | 20,324 |
| Dividends payable | | 11,603 | | 11,571 |
| Accrued expense | | 34,640 | | 24,571 |
| Current portion of senior secured term debt | | 8,800 | | 8,800 |
| Current portion of capital lease obligations | | 216 | | 192 |
| Current portion of derivative liability | | 8,340 | | 3,580 |
| Current portion of pension and postretirement benefit obligations | | 2,579 | | 2,579 |
| Total current liabilities | | 102,280 | | 85,290 |
| Long-term portion of capital lease obligation | | 4,403 | | 4,519 |
| Long-term debt | | 1,164,855 | | 871,200 |
| Deferred income taxes | | 78,794 | | 77,327 |
| Pension and other postretirement obligations | | 89,587 | | 93,754 |
| Other long-term liabilities | | 6,863 | | 14,167 |
| Total liabilities | | 1,446,782 | | 1,146,257 |
| Stockholders equity: | | | | |
| Common stock, par value $0.01 per share; 100,000,000 shares authorized, 29,951,282 and 29,869,512, shares outstanding as of June 30, 2012 and December 31, 2011, respectively | | 299 | | 299 |
| Additional paid-in capital | | 61,968 | | 79,852 |
| Retained earnings | | | | |
| Accumulated other comprehensive loss, net | | (35,352) | | (37,833) |
| Noncontrolling interest | | 5,739 | | 5,494 |
| Total stockholders equity | | 32,654 | | 47,812 |
| Total liabilities and stockholders equity | $ | 1,479,436 | $ | 1,194,069 |

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

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**Consolidated Communications Holdings, Inc. and Subsidiaries**

**Condensed Consolidated Statement of Changes in Stockholders Equity**

(Unaudited)

| **(In thousands, except share amounts)** | **Common Stock Shares** | **Common Stock Amount** | **Additional Paid-in Capital** | **Retained Earnings** | **Accumulated Other Comprehensive Loss, net** | **Non-controlling Interest** | **Total** |
|---|---|---|---|---|---|---|---|
| Balance - December 31, 2011 | 29,869,512 | $ 299 | $ 79,852 | $ | $ (37,833) | $ 5,494 | $ 47,812 |
| Dividends on common stock | | | (9,843) | (1,759) | | | (11,602) |
| Shares issued under employee plan, net of forfeitures | 81,770 | | | | | | |
| Non-cash, stock-based compensation | | | 501 | | | | 501 |
| Comprehensive income | | | | 1,759 | 1,452 | 125 | 3,336 |
| Balance - March 31, 2012 | 29,951,282 | $ 299 | $ 70,510 | $ | $ (36,381) | $ 5,619 | $ 40,047 |
| Dividends on common stock | | | (8,817) | (2,786) | | | (11,603) |
| Other | | | (314) | | | | (314) |
| Non-cash, stock-based compensation | | | 589 | | | | 589 |
| Comprehensive income | | | | 2,786 | 1,029 | 120 | 3,935 |
| Balance June 30, 2012 | 29,951,282 | $ 299 | $ 61,968 | $ | $ (35,352) | $ 5,739 | $ 32,654 |

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

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**Consolidated Communications Holdings, Inc. and Subsidiaries**

**Condensed Consolidated Statements of Cash Flows**

(Unaudited)

| **(In thousands)** | **Six months ended June 30, 2012** | **2011** |
|---|---|---|
| **Operating Activities** | | |
| Net income | **$ 4,790** | $ 13,010 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | **44,006** | 44,145 |
| Deferred income taxes | | 298 |
| Loss on disposal of assets | **206** | 4 |
| Cash distributions from wireless partnerships in excess of (less than) earnings | **(1,171)** | (300) |
| Stock-based compensation expense | **1,090** | 1,090 |
| Amortization of deferred financing costs | **5,020** | 662 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable, net | **327** | 4,954 |
| Income tax receivable | **(2,288)** | 2,564 |
| Inventories | **(82)** | (285) |
| Other assets | **(1,599)** | (982) |
| Accounts payable | **1,455** | 827 |
| Accrued expenses and other liabilities | **(275)** | (4,784) |
| Net cash provided by operating activities | **51,479** | 61,203 |
| **Investing Activities** | | |
| Purchases of property, plant and equipment | **(22,151)** | (20,704) |
| Proceeds from the sale of assets | **28** | 396 |
| Restricted cash for acquisition of SureWest | **(298,035)** | |
| Other | **(314)** | 56 |
| Net cash used for investing activities | **(320,472)** | (20,252) |
| **Financing Activities** | | |
| Proceeds on bond offering | **298,055** | |
| Restricted cash on bond offering | **(17,047)** | |
| Payment of capital lease obligation | **(92)** | (71) |
| Payment on long term debt | **(4,400)** | |
| Payment of financing costs | **(5,070)** | (3,399) |
| Dividends on common stock | **(23,173)** | (23,128) |
| Net cash used for financing activities | **248,273** | (26,598) |
| Net increase in cash and equivalents | **(20,720)** | 14,353 |
| Cash and equivalents at beginning of year | **105,704** | 67,654 |
| Cash and equivalents at end of period | **$ 84,984** | $ 82,007 |

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

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**Consolidated Communications Holdings, Inc. and Subsidiaries**

**Notes to Unaudited Condensed Consolidated Financial Statements**

## 1. Nature of Operations

The accompanying unaudited condensed consolidated financial statements include the accounts of Consolidated Communications Holdings, Inc. and its subsidiaries, which are collectively referred to as Consolidated , the Company , we , our or us , unless the context otherwise requires. A
significant intercompany transactions have been eliminated in consolidation.

We have prepared the unaudited condensed consolidated financial statements included herein pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in statements prepared in accordance with generally accepted accounting principles in the United States have been omitted pursuant to such rules and regulations, although we believe that the disclosures are adequate to make the information presented not misleading. These financial statements should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2011.

The accompanying unaudited condensed consolidated financial statements presented herewith reflect all adjustments (consisting of only normal and recurring adjustments) which, in the opinion of management, are necessary for a fair presentation of the results of operations for the three and six month periods ended June 30, 2012 and 2011. The results of operations for interim periods are not necessarily indicative of results to be expected for an entire year.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates.

As of June 30, 2012, the Company s Summary of Critical Accounting Policies for the year ended December 31, 2011, which are detailed in the Company s Annual Report on Form 10-K, have not changed.

The Company has evaluated subsequent events and transactions for potential recognition or disclosure in the financial statements through the day the financial statements are issued.

*Reclassifications*

Certain prior-quarter amounts have been reclassified in the statement of cash flows from financing activities to operating activities. These reclassifications had no impact on net cash flows.

**2. Recent Accounting Pronouncements**

Effective January 1, 2012, we adopted the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update No. 2011-04 ( ASU 2011-04 ), *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards ( IFRS ).* This pronouncement was issued to provide a consistent definition of fair value and ensure that the fair value measurement and disclosure requirements are similar between U.S. GAAP and IFRS. ASU 2011-04 changes certain fair value measurement principles and enhances

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the disclosure requirements particularly for Level 3 fair value measurements. The adoption of this standard did not have a material impact on our consolidated financial statements.

Effective January 1, 2012, we adopted the FASB issued Accounting Standards Update No. 2011-05 ( ASU 2011-05 ), *Presentation of Comprehensive Income*. ASU 2011-05 requires an entity to either present components of net income and other comprehensive income in one continuous statement or in two separate but consecutive statements. Accordingly, we have presented net income and other comprehensive income in two consecutive statements.

**3. Agreement and Plan of Merger with SureWest Communications**

On February 5, 2012, we entered into a definitive agreement to acquire all the outstanding shares of SureWest Communications ( SureWest ) for $23.00 per share in a cash and stock transaction. SureWest provides a wide range of telecommunications, digital video, Internet, data and other facilities-based communications services in Northern California, primarily in the greater Sacramento region, and in the greater Kansas City, Kansas and Missouri areas.

The merger agreement provided that each record holder of SureWest common stock could make one of the following elections, or a combination of the two, at or prior to the election deadline provided for in the merger agreement, regarding the type of merger consideration they wish to receive in exchange for shares of SureWest common stock:

- a cash election to receive $23.00 in cash, without interest, for each share of SureWest common stock, or
- a stock election to receive shares of our common stock having an equivalent value based on average trading prices for the 20-day period ending two days before the closing date of the merger, subject to a collar so that there would be a maximum exchange ratio of 1.40565 shares of our common stock for each share of SureWest common stock and a minimum of 1.03896 shares of our common stock for each share of SureWest common stock.

Overall elections were subject to a proration so that approximately 50% of the SureWest shares (treating equity award shares as outstanding shares) would be exchanged for cash and approximately 50% for our stock.

The California PUC approved the merger on June 7, 2012. On June 12, 2012, SureWest shareholders and Consolidated s stockholders approved the issuance of our common stock to SureWest shareholders. Final closing on the SureWest transaction occurred July 2, 2012. The price in the acquisition, excluding debt assumed, consisted of cash of $176.7 million and 9,965,983 shares of the Company s common stock (based on average trading prices for the Company s common stock over the 20-day period ending two days before the closing date of the merger), totaled $320.7 million.

The cash portion of the merger consideration and the funds required to repay SureWest outstanding debt was financed with $300.0 million in aggregate principal amount of 10.875% Senior Notes due 2020 ( Senior Notes ). We also used cash on hand and approximately $35.0 million in borrowings from our revolving credit facility to fund the acquisition.

The acquisition of SureWest will be recorded in accordance with the acquisition method, and it is expected that goodwill and intangible assets will be recorded on the consolidated balance sheets. However, as the initial accounting for the business combination has not been completed as of August 6, 2012, including the measurement of certain intangible assets and goodwill.

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**4. Restricted cash**

At June 30, 2012, the Company had restricted cash of $315.1 million on deposit with an Escrow Agent in connection with the acquisition of SureWest. The restricted cash included $298.0 million of net proceeds from the issuance of Senior Notes for the SureWest acquisition and $17.1 million of cash escrowed to ensure coverage of a redemption fee and interest accruing on the financing through November 5, 2012 for the repayment of the financing in the event the SureWest acquisition were not consummated by that date. There was no such restricted cash at December 31, 2011.

**5. Prepaid expense and other current assets**

Prepaid and other current assets are as follows:

| **(In thousands)** | **June 30, 2012** | **December 31, 2011** |
|---|---|---|
| Prepaid maintenance | **$ 2,360** | $ 1,980 |
| Prepaid taxes | **1,784** | 440 |
| Deferred charges | **672** | 784 |
| Prepaid insurance | **470** | 313 |
| Prepaid expense - other | **2,438** | 2,607 |
| Other current assets | **45** | 46 |
| Total | **$ 7,769** | $ 6,170 |

**6. Property, plant and equipment, net**

Property, plant and equipment are as follows:

| **(In thousands)** | **June 30, 2012** | **December 31, 2011** |
|---|---|---|
| Land and buildings | **$ 65,282** | $ 66,704 |
| Network and outside plant facilities | **904,711** | 897,140 |
| Furniture, fixtures and equipment | **50,516** | 73,185 |
| Assets under capital lease | **10,014** | 10,014 |
| Less: accumulated depreciation | **(722,696)** | (721,527) |
| | **307,827** | 325,516 |
| Construction in progress | **13,220** | 6,530 |
| Totals | **$ 321,047** | $ 332,046 |

Depreciation expense totaled $16.3 million and $16.5 million for the three month periods ended June 30, 2012 and 2011, respectively and $32.9 million and $33.1 million for the six months ended June 30, 2012 and 2011, respectively.

**7. Investments**

We own 2.34% of GTE Mobilnet of South Texas Limited Partnership (the Mobilnet South Partnership ). The principal activity of the Mobilnet South Partnership is providing cellular service in the Houston, Galveston, and Beaumont, Texas metropolitan areas. We also own 3.60% of Pittsburgh SMSA Limited Partnership ( Pittsburgh SMSA ), which provides cellular service in and around the Pittsburgh metropolitan area. Because of our limited influence over these partnerships, we use the cost method to account for both of these investments. It is not practicable to estimate fair value of these investments. We did not evaluate any of the investments for impairment as no factors indicating

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impairment existed during the year. For the three month periods ended June 30, 2012 and 2011, we received cash distributions from these partnerships totaling $3.0 million and $2.0 million, respectively. For the six months ended June 30, 2012 and 2011, we received cash distributions from these partnerships totaling $5.5 million and $5.0 million, respectively.

We also own 17.02% of GTE Mobilnet of Texas RSA #17 Limited Partnership ( RSA #17 ), 16.6725% of Pennsylvania RSA 6(I) Limited Partnership ( RSA 6(I) ), and 23.67% of Pennsylvania RSA 6(II) Limited Partnership ( RSA 6(II) ). RSA #17 provides cellular service to a limited rural area in Texas. RSA 6(I) and RSA 6(II) provide cellular service in and around our Pennsylvania service territory. Because we have significant influence over the operating and financial policies of these three entities, we account for the investments using the equity method. For the three months ended June 30, 2012 and 2011, we received cash distributions from these partnerships totaling $2.9 million and $3.8 million, respectively. For the six months ended June 30, 2012 and 2011, we received cash distributions from these partnerships totaling $6.5 million and $7.7 million, respectively.

Our investments are as follows:

| (In thousands) | | June 30, 2012 | | December 31, 2011 |
|---|---|---|---|---|
| Cash surrender value of life insurance policies | **$** | **2,037** | $ | 1,978 |
| Cost method investments: | | | | |
| GTE Mobilnet of South Texas Limited Partnership (2.34% interest) | | **21,450** | | 21,450 |
| Pittsburgh SMSA Limited Partnership (3.60% interest) | | **22,950** | | 22,950 |
| CoBank, ACB Stock | | **3,518** | | 3,394 |
| Other | | **15** | | 15 |
| Equity method investments: | | | | |
| GTE Mobilnet of Texas RSA #17 Limited Partnership (17.02% interest) | | **19,226** | | 19,422 |
| Pennsylvania RSA 6(I) Limited Partnership (16.6725% interest) | | **7,300** | | 7,063 |
| Pennsylvania RSA 6(II) Limited Partnership (23.67% interest) | | **22,927** | | 21,797 |
| Total | **$** | **99,423** | $ | 98,069 |

CoBank is a cooperative bank owned by its customers. Annually, CoBank distributes patronage in the form of cash and stock in the cooperative based on the Company s outstanding loan balance with CoBank, which has traditionally been a significant lender in the Company s credit facility. The investment in CoBank represents the accumulation of the equity patronage paid by CoBank to the Company.

Because the income from our equity method investments exceeded 10% of our pretax income for the first six months of 2012, below is a summary of unaudited summarized income statement and balance sheet information for the three equity investments:

| (In thousands) | Three months ended June 30, | | | | Six months ended June 30, | | | |
|---|---|---|---|---|---|---|---|---|
| | | 2012 | | 2011 | | 2012 | | 2011 |
| Total revenues | **$** | **73,555** | $ | 74,485 | **$** | **145,890** | $ | 143,548 |
| Income from operations | | **22,235** | | 20,631 | | **41,927** | | 40,796 |
| Net income before taxes | | **22,247** | | 20,656 | | **41,956** | | 40,848 |
| Net income | | **22,143** | | 20,556 | | **41,748** | | 40,648 |

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| (In thousands) | | June 30, 2012 | | December 31, 2011 |
|---|---|---|---|---|
| Current assets | $ | **51,801** | $ | 44,739 |
| Non-current assets | | **76,771** | | 79,432 |
| Current liabilities | | **12,163** | | 14,523 |
| Non-current liabilities | | **1,210** | | 1,096 |
| Partnership equity | | **115,199** | | 108,552 |

## 8. Fair Value Measurements

The Company s derivative instruments related to interest rate swap agreements are required to be measured at fair value on a recurring basis. The fair values of the interest rate swaps are determined using an internal valuation model which relies on the expected LIBOR based yield curve and estimates of counterparty and Consolidated s non-performance risk as the most significant inputs. Because each of these inputs are directly observable or can be corroborated by observable market data, we have categorized these interest rate swaps as Level 2 within the fair value hierarchy.

The Company s interest rate swap assets and liabilities measured at fair value on a recurring basis subject to disclosure requirements at June 30, 2012 and December 31, 2011 were as follows:

| | | | Fair Value Measurements at Reporting Date Using | | | | |
|---|---|---|---|---|---|---|---|
| (In thousands) | | June 30, 2012 | Quoted Prices In Active Markets for Identical Assets (Level 1) | | Significant Other Observable Inputs (Level 2) | | Significant Unobservable Inputs (Level 3) |
| Current interest rate swap liabilities | $ | **(8,340)** | $ | $ | **(8,340)** | $ | |
| Long-term interest rate swap liabilities | | **(5,103)** | | | **(5,103)** | | |
| Totals | $ | **(13,443)** | $ | $ | **(13,443)** | $ | |

| | | | Fair Value Measurements at Reporting Date Using | | | | |
|---|---|---|---|---|---|---|---|
| (In thousands) | | December 31, 2011 | Quoted Prices In Active Markets for Identical Assets (Level 1) | | Significant Other Observable Inputs (Level 2) | | Significant Unobservable Inputs (Level 3) |
| Current interest rate swap liabilities | $ | (3,580) | $ | $ | (3,580) | $ | |
| Long-term interest rate swap liabilities | | (12,401) | | | (12,401) | | |
| Totals | $ | (15,981) | $ | $ | (15,981) | $ | |

The change in the fair value of the derivatives is primarily a result of a change in market expectations for future interest rates.

We have not elected the fair value option for any of our financial assets or liabilities. The carrying value of other financial instruments, including cash, accounts receivable, accounts payable and accrued liabilities approximate fair value due to their short maturities or variable-rate nature of the respective balances. The following table presents the other financial instruments that are not carried at fair value but which require fair value disclosure as of June 30, 2012 and December 31, 2011.

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| | As of June 30, 2012 | | As of December 31, 2011 | |
|---|---|---|---|---|
| **(In thousands)** | **Carrying Value** | **Fair Value** | **Carrying Value** | **Fair Value** |
| Investments, equity basis | **$ 49,453** | **n/a** | $ 48,282 | n/a |
| Investments, at cost | **$ 47,933** | **n/a** | $ 47,809 | n/a |
| Long-term debt | **$ 1,173,655** | **$ 1,173,655** | $ 880,000 | $ 880,000 |

The Company s investments at June 30, 2012 and December 31, 2011 accounted for under both the equity and cost methods consist of minority positions in various cellular telephone limited partnerships. These investments are recorded using either the equity or cost methods.

Our senior secured long-term debt of $875.6 million allows us to select a one month LIBOR repricing option, which we have elected. As such, the fair value of this debt approximates its carrying value. Based upon the inputs of the LIBOR based yield curve, which can be corroborated by observable market data, we have categorized the long-term debt as Level 2 within the fair value hierarchy.

Our Senior Notes long term debt of $298.1 million earns interest at a rate of 10.875% per year. The fair value of this debt approximates its carrying value. We have categorized the Senior Notes long-term debt as Level 2 within the fair value hierarchy.

## 9. Goodwill and Other Intangible Assets

In accordance with the applicable accounting guidance, goodwill and indefinite lived intangible assets are not amortized but are subject to impairment testing no less than annually or more frequently if circumstances indicate potential impairment.

The following table presents the carrying amount of goodwill by segment:

| **(In thousands)** | **June 30, 2012** | **December 31, 2011** |
|---|---|---|
| Telephone Operations | **$ 519,542** | $ 519,542 |
| Other Operations | **1,020** | 1,020 |
| Totals | **$ 520,562** | $ 520,562 |

Our most valuable tradename is the federally registered mark CONSOLIDATED, which is used in association with our telephone communication services and is a design of interlocking circles. The Company s corporate branding strategy leverages a CONSOLIDATED naming structure. All of the Company s business units and several of our products and services incorporate the CONSOLIDATED name. These tradenames are indefinitely renewable intangibles. The carrying value of the tradenames was $12.3 million at both June 30, 2012 and December 31, 2011.

The Company s customer lists consist of an established base of customers that subscribe to its services. The carrying amount of customer lists is as follows:

| | Telephone Operations | | Other Operations | |
|---|---|---|---|---|
| **(In thousands)** | **June 30, 2012** | **December 31, 2011** | **June 30, 2012** | **December 31, 2011** |
| Gross carrying amount | **$ 193,124** | $ 193,124 | **$ 4,405** | $ 4,405 |
| Less: accumulated amortization | **(146,602)** | (135,754) | **(4,185)** | (3,964) |
| Net carrying amount | **$ 46,522** | $ 57,370 | **$ 220** | $ 441 |

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Amortization associated with customer lists totaled approximately $5.6 million and $11.1 million in each of the three and six month periods ended June 30, 2012 and 2011, respectively.

## 10. Deferred Debt Issuance Costs, Net and Other Assets

Deferred financing costs, net and other assets are as follows:

| (In thousands) | | June 30, 2012 | | December 31, 2011 |
|---|---|---|---|---|
| Deferred debt issuance costs, net | **$** | **12,927** | $ | 4,833 |
| Other assets | | **54** | | 71 |
| Total | **$** | **12,981** | $ | 4,904 |

Deferred debt issuance costs are subject to amortization. Deferred debt issuance costs of $5.1 million at June 30, 2012 related to our secured credit facility will be amortized over the term of the corresponding debt. The remaining $7.8 million deferred costs relate to the acquisition of SureWest which include $6.8 million of an underwriting commission and $1.0 million for issuance of Senior Notes. The deferred cost associated with the acquisition of SureWest will be amortized over the term of the maturity of the Senior Notes through June 2020.

## 11. Accrued Expenses

Accrued expenses are as follows:

| (In thousands) | | June 30, 2012 | | December 31, 2011 |
|---|---|---|---|---|
| Accrued salaries | **$** | **4,258** | $ | 5,851 |
| Accrued employee benefits | | **4,341** | | 4,384 |
| Accrued financing fees | | **10,910** | | |
| Taxes payable | | **2,754** | | 4,599 |
| Accrued interest | | **3,034** | | 237 |
| Accrued site commissions | | **2,452** | | 3,559 |
| Other accrued expenses | | **6,891** | | 5,941 |
| Total accrued expenses | **$** | **34,640** | $ | 24,571 |

## 12. Debt

Long-term debt consists of the following:

| (In thousands) | June 30, 2012 | December 31, 2011 |
|---|---|---|
| Senior secured credit facility term loan | **$ 875,600** | $ 880,000 |
| Senior notes net of discount | **298,055** | |
| Senior secured credit facility revolving loan | | |
| | **1,173,655** | 880,000 |
| Less: current portion of long-term debt | **(8,800)** | (8,800) |
| Total long-term debt | **$ 1,164,855** | $ 871,200 |

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*Credit Agreement*

The Company, through certain of its wholly owned subsidiaries, has an outstanding credit agreement with several financial institutions, which consists of a $50 million revolving credit facility, $875.6 million term loan facility, and $300.0 million of Senior Notes.  On July 2, 2012, we used $35 million on the revolving credit facility in connection with the SureWest acquisition. Borrowings under the senior secured credit facility are secured by substantially all of the assets of the Company with the exception of Illinois Consolidated Telephone Company.  The Senior Notes are unsecured.

Our term loan credit facility is made up of two separate tranches, resulting in different maturity dates and interest rate margins for each term loan tranche.  The first term loan tranche consists of $468.6 million aggregate principal amount, matures on December 31, 2014 and has an applicable margin (at our election) equal to either 2.50% for a LIBOR-based term loan or 1.50% for an alternative base rate loan.  The second term loan tranche consists of $407.0 million aggregate principal amount, matures on December 31, 2017 and has an applicable margin (at our election) equal to either 3.75% for a LIBOR-based term loan or 2.75% for an alternative base rate term loan.  The applicable margins for each of the term loan tranches are fixed for the duration of the loans.  The amended term loan facility also requires $2.2 million in quarterly principal payments which began on March 31, 2012.

Our revolving credit facility has a maturity date of June 8, 2016 and an applicable margin (at our election) of between 2.75% and 3.50% for LIBOR-based borrowings and between 1.75% and 2.50% for alternative base rate borrowings, depending on our leverage ratio.  Based on our leverage ratio of 4.61:1.00 at June 30, 2012, the borrowing margin for the next three month period ending September 30, 2012 will be at a weighted-average margin of 3.25% for a LIBOR-based loan or 2.25% for an alternative base rate loan.  The applicable borrowing margin for the revolving credit facility is adjusted quarterly to reflect the leverage ratio from the prior quarter-end.  There were no borrowings or letters of credit outstanding under the revolving credit facility as of June 30, 2012 or December 31, 2011, or at any time during the quarter ended June 30, 2012.  On July 2, 2012, we borrowed $35.0 million of the revolving credit facility for the acquisition of SureWest.

The weighted-average interest rate incurred on our credit facilities during the three month periods ended June 30, 2012 and 2011, including amounts paid on our interest rate swap agreements and the applicable margin, was 4.90% and 5.45% per annum, respectively.  Interest is payable at least quarterly.

The credit agreement contains various provisions and covenants, including, among other items, restrictions on the ability to pay dividends, incur additional indebtedness, issue capital stock, and commit to future capital expenditures.  We have agreed to maintain certain financial ratios, including interest coverage, and total net leverage ratios, all as defined in the credit agreement.  As of June 30, 2012, we were in compliance with the credit agreement covenants.

In connection with the acquisition of SureWest described in Note 3, on February 5, 2012 the Company received committed financing for a total of $350.0 million to fund the cash portion of the anticipated transaction, to refinance SureWest s debt and to pay for certain transaction costs. The financing package included a $350.0 million Senior Unsecured Bridge Loan Facility ( Bridge Facility ). As anticipated, permanent financing for the SureWest acquisition was funded by our Senior Note offering, as described below.  As a result, the $4.1 million commitment fee incurred for the Bridge Facility was capitalized as deferred debt issuance costs and was amortized over the expected life of the Bridge Facility, which was four months.

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Effective February 17, 2012, we amended our credit facility to provide us with the ability to escrow proceeds from a high-yield note offering prior to closing the SureWest acquisition and, until closing, exclude the debt from current leverage calculations. The amendment also permitted us additional flexibility for future high yield notes issuances with the same subsidiary guarantees required by our current credit facility, which enabled us to issue the Senior Notes described below. All other terms, coverage and leverage ratios of the credit facility were unchanged. Fees totaling $3.5 million were recognized as expense in connection with the amendment while $1.2 million in fees were capitalized as deferred debt issuance costs and amortized over the remaining life of the term debt.

On May 30, 2012, we completed an offering of $300.0 million aggregate principal amount of 10.875% Senior Notes, due 2020 through our wholly-owned subsidiary, Consolidated Communications Finance Co. ( Finance Co. ) for the acquisition of SureWest. The Senior Notes will mature on June 1, 2020 and earn interest at a rate of 10.875% per year, payable semi-annually in arrears on June 1 and December 1 of each year, commencing on December 1, 2012. The Senior Notes were sold to investors at a price equal to 99.345% of the principal amount thereof, for a yield to maturity of 11.00%. This discount will be amortized over the term of the Senior Notes. The proceeds of the sale of the Senior Notes were held in an escrow account pending closing of the SureWest transaction. Upon closing of the SureWest acquisition on July 2, 2012, Finance Co. merged with and into our wholly-owned subsidiary Consolidated Communications, Inc., which assumed the Senior Notes, and we and certain of our subsidiaries fully and unconditionally guaranteed the Senior Notes.

**13. Derivatives**

In order to manage the risk associated with changes in interest rates, we have entered into interest rate swap agreements that effectively convert a portion of our floating-rate debt to a fixed-rate basis, thereby reducing the impact of interest rate changes on future cash interest payments. We account for these transactions as cash flow hedges under the FASB s ASC Topic 815 ( ASC 815 ), *Derivatives and Hedging*. The swaps are designated as cash flow hedges of our expected future interest payments. In a cash flow hedge, the effective portion of the change in the fair value of the hedging derivative is recorded in accumulated other comprehensive income (loss) and is subsequently reclassified into earnings during the same period in which the hedged item affects earnings. The change in fair value of any ineffective portion of the hedging derivative is recognized immediately in earnings.

The following interest rate swaps, all designated as cash flow hedges, were outstanding at June 30, 2012:

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| (In thousands) | Notional Amount | 2012 Balance Sheet Location | Fair Value |
|---|---|---|---|
| **Fixed to 3-month floating LIBOR** | **$ 100,000** | **Current portion of long-term liabilities** | **$ (1,842)** |
| **Fixed to 3-month floating LIBOR** | **130,000** | **Current portion of long-term liabilities** | **(3,880)** |
| **3-month floating LIBOR minus spread to 1-month floating LIBOR** | **100,000** | **Current portion of long-term liabilities** | **(89)** |
| **3-month floating LIBOR minus spread to 1-month floating LIBOR** | **130,000** | **Current portion of long-term liabilities** | **(168)** |
| **Fixed to 1-month floating LIBOR** | **200,000** | **Other long-term liabilities** | **(3,337)** |
| **Fixed to 1-month floating LIBOR** | **200,000** | **Current portion of long-term liabilities** | **(2,361)** |
| **Forward starting fixed to 1-month floating LIBOR** | **175,000** | **Other long-term liabilities** | **(1,766)** |
| **Total Fair Values** | | | **$ (13,443)** |

The following interest rate swaps, all designated as cash flow hedges, were outstanding at December 31, 2011:

| (In thousands) | Notional Amount | 2011 Balance Sheet Location | Fair Value |
|---|---|---|---|
| Fixed to 3-month floating LIBOR | $ 100,000 | Current portion of long-term liabilities | $ (3,401) |
| Fixed to 3-month floating LIBOR | 130,000 | Other long-term liabilities | (6,053) |
| 3-month floating LIBOR minus spread to 1-month floating LIBOR | 100,000 | Current portion of long-term liabilities | (179) |
| 3-month floating LIBOR minus spread to 1-month floating LIBOR | 130,000 | Other long-term liabilities | (269) |
| Fixed to 1-month floating LIBOR | 300,000 | Other long-term liabilities | (5,343) |
| Forward starting fixed to 1-month floating LIBOR | 200,000 | Other long-term liabilities | (736) |
| Total Fair Values | | | $ (15,981) |

At June 30, 2012 and December 31, 2011, the interest rate on approximately 72% and 60%, respectively, of our outstanding debt (excluding the Senior Notes) was fixed through the use of interest rate swaps.

The counterparties to our various swaps are 5 major U.S. and European banks. None of the swap agreements provide for either us or the counterparties to post collateral nor do the agreements include any covenants related to the financial condition of Consolidated or the counterparties. The swaps of any counterparty that is a Lender as defined in our credit facility are secured along with the other creditors under the credit facility. Each of the swap agreements provides that in the event of a bankruptcy filing by either Consolidated or the counterparty, any amounts owed between the two

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parties would be offset in order to determine the net amount due between parties. This provision allows us to partially mitigate the risk of non-performance by a counterparty.

At June 30, 2012 and December 31, 2011, the pretax deferred losses related to our interest rate swap agreements included in other comprehensive income totaled $13.4 million and $15.9 million, respectively. The change in fair value of any ineffective portion of the hedging derivative is recognized immediately in earnings.

Information regarding our cash flow hedge transactions is as follows:

| **(In thousands)** | **For the three months ended June 30, 2012** | **2011** | **For the six months ended June 30, 2012** | **2011** |
|---|---|---|---|---|
| Loss/(gain) recognized in accumulated other comprehensive income (loss) ( AOCI ) | **$ (581)** | $ (953) | **$ (1,584)** | $ (5,614) |
| Loss/(gain) arising from ineffectiveness increasing/(reducing) interest expense | **(15)** | (24) | **(31)** | (59) |
| Deferred losses/(gains) reclassed from AOCI to interest expense | **(14)** | 402 | **(1)** | 885 |

| **(In thousands, except months)** | **June 30, 2012** | **December 31, 2011** |
|---|---|---|
| Aggregate notional value of current derivatives outstanding | **$ 630,000** | $ 530,000 |
| Aggregate notional value of forward derivatives outstanding | **$ 175,000** | $ 200,000 |
| Period through which derivative positions currently exist | **March 2016** | June 2015 |
| Fair value of derivatives | **$ 13,443** | $ 15,981 |
| Deferred losses included in AOCI (pretax) | **$ 13,425** | $ 15,932 |
| Losses included in AOCI to be recognized in the next 12 months | **$ 41** | $ 65 |
| Number of months over which loss in OCI is to be recognized | **9** | 15 |

## 14. Interest Expense, Net of Interest Income

The following table summarizes interest expense for the periods indicated:

| **(In thousands)** | **Three months ended June 30, 2012** | **2011** | **Six months ended June 30, 2012** | **2011** |
|---|---|---|---|---|
| Interest expense credit facility | **$ 7,377** | $ 6,382 | **$ 14,837** | $ 12,468 |
| Payments on swap liabilities, net | **3,502** | 5,388 | **6,963** | 10,645 |
| Interest expense capital leases | **160** | 165 | **321** | 321 |
| | **1,098** | | **4,160** | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Amortization of deferred financing costs bridge facility | | | | | | | | |
| Interest expense bridge facility | | **1,458** | | | | **1,458** | | |
| Interest expense Senior Notes | | **2,750** | | | | **2,750** | | |
| Uncertain tax position interest accrual | | **10** | | 12 | | **19** | | 24 |
| Other interest | | **162** | | 188 | | **291** | | 362 |
| Amortization of deferred financing fees | | **460** | | 338 | | **860** | | 662 |
| Capitalized interest | | **(42)** | | (39) | | **(82)** | | (72) |
| Total interest expense | | **16,935** | | 12,434 | | **31,577** | | 24,410 |
| Less: interest income | | **(42)** | | (37) | | **(84)** | | (74) |
| Interest expense, net of interest income | **$** | **16,893** | $ | 12,397 | **$** | **31,493** | $ | 24,336 |

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**15. Retirement and Pension Plans**

We have 401(k) plans covering substantially all of our employees. Contributions made under our defined contribution plans include a match, at the Company s discretion, of employee salaries contributed to the plans. We recognized expense with respect to these plans of $0.6 million for each of the three month periods ended June 30, 2012 and 2011 and $1.3 million for each of the six month periods ended June 30, 2012 and 2011.

*Qualified Retirement Plan*

We sponsor a defined-benefit pension plan ( Retirement Plan ) that is non-contributory covering substantially all of our hourly employees who fulfill minimum age and service requirements. Certain salaried employees are also covered by the Retirement Plan, although these benefits have previously been frozen.

The following table summarizes the components of net periodic pension cost for the qualified retirement plan for the periods indicated:

| | For the three months ended June 30, | | For the six months ended June 30, | |
|---|---|---|---|---|
| **(In thousands)** | **2012** | **2011** | **2012** | **2011** |
| Service cost | **$ 357** | $ 222 | **$ 713** | $ 638 |
| Interest cost | **2,627** | 2,902 | **5,255** | 5,451 |
| Expected return on plan assets | **(2,611)** | (2,952) | **(5,222)** | (5,446) |
| Net amortization loss (gain) | **798** | (495) | **1,596** | 375 |
| Prior service credit amortization | **(41)** | (32) | **(83)** | (83) |
| Net periodic pension cost | **$ 1,130** | $ (355) | **$ 2,259** | $ 935 |

*Non-qualified Pension Plan*

The Company also has non-qualified supplemental pension plans ( Restoration Plans ), which we acquired as part of our North Pittsburgh Systems, Inc. ( North Pittsburgh ) and TXU Communications Venture Company ( TXUCV ) acquisitions. The Restoration Plans cover certain former employees of our Pennsylvania and Texas operations. The Restoration Plans restores benefits that were precluded under the Retirement Plan by Internal Revenue Service limits on compensation and benefits applicable to qualified pension plans, and by the exclusion of bonus compensation from the Retirement Plan s definition of earnings.

The following table summarizes the components of net periodic pension cost for the Restoration Plans for the periods indicated:

| (In thousands) | For the three months ended June 30, 2012 | 2011 | For the six months ended June 30, 2012 | 2011 |
|---|---|---|---|---|
| Interest cost | **$ 14** | $ 15 | **$ 28** | $ 29 |
| Net amortization loss | **11** | 5 | **22** | 17 |
| Net periodic pension cost | **$ 25** | $ 20 | **$ 50** | $ 46 |

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*Other Non-qualified Deferred Compensation Agreements*

We also are liable for deferred compensation agreements with former members of the board of directors and certain other former employees of a subsidiary of TXUCV, which was acquired in 2004. The benefits are payable for up to the life of the participant and may begin as early as age 65 or upon the death of the participant. Participants accrue no new benefits as these plans had previously been frozen by TXUCV s predecessor company prior to our acquisition of TXUCV. Payments related to the deferred compensation agreements totaled approximately $0.1 million for both the three month periods ended June 30, 2012 and 2011, respectively, and $0.3 million for both six month periods ended June 30, 2012 and 2011, respectively. The net present value of the remaining obligations was approximately $2.3 million at June 30, 2012 and $2.5 million at December 31, 2011, and is included in pension and postretirement benefit obligations in the accompanying balance sheets.

We also maintain 38 life insurance policies on certain of the participating former directors and employees. We recognized $0.2 million in life insurance proceeds as other non-operating income in the three and six month periods ended June 30, 2012. We did not recognize any proceeds in other income for the three or six month periods ended June 30, 2011 due to the receipt of life insurance proceeds. The excess of the cash surrender value of the remaining life insurance policies over the notes payable balances related to these policies is determined by an independent consultant, and totaled $2.0 million at June 30, 2012 and $2.0 million at December 31, 2011. These amounts are included in investments in the accompanying balance sheets. Cash principal payments for the policies and any proceeds from the policies are classified as operating activities in the statements of cash flows.

**16. Postretirement Benefit Obligation**

We sponsor a healthcare plan and life insurance plan that provides postretirement medical benefits and life insurance to certain groups of retired employees. Retirees share in the cost of healthcare benefits, making contributions that are adjusted periodically either based upon collective bargaining agreements or because total costs of the program have changed. We generally pay the covered expenses for retiree health benefits as they are incurred. Postretirement life insurance benefits are fully insured.

The following table summarizes the components of the net periodic costs for postretirement benefits for the periods indicated:

| | For the three months ended June 30, | | For the six months ended June 30, | |
|---|---|---|---|---|
| **(In thousands)** | **2012** | **2011** | **2012** | **2011** |
| Service cost | **$ 213** | $ 223 | **$ 427** | $ 446 |
| Interest cost | **414** | 398 | **828** | 796 |
| Net prior service cost amortization | **(47)** | (47) | **(95)** | (94) |
| Net periodic postretirement benefit cost | **$ 580** | $ 574 | **$ 1,160** | $ 1,148 |

**17. Other Long-term Liabilities**

Other long-term liabilities are as follows:

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| (In thousands) | | June 30, 2012 | | December 31, 2011 |
|---|---|---|---|---|
| Long-term derivative liabilities | **$** | **5,103** | $ | 12,401 |
| Uncertain tax positions | | **1,224** | | 1,224 |
| Accrued interest on uncertain tax positions | | **70** | | 50 |
| Other long-term liabilities | | **466** | | 492 |
| Total | **$** | **6,863** | $ | 14,167 |

**18. Stock-based Compensation Plans**

Pretax stock-based compensation expense for the periods indicated was as follows:

| (In thousands) | For the three months ended June 30, 2012 | | 2011 | | For the six months ended June 30, 2012 | | 2011 | |
|---|---|---|---|---|---|---|---|---|
| Restricted stock | **$** | **325** | $ | 342 | **$** | **650** | $ | 691 |
| Performance shares | | **264** | | 237 | | **440** | | 399 |
| Total | **$** | **589** | $ | 579 | **$** | **1,090** | $ | 1,090 |

Stock-based compensation expense is included in selling, general and administrative expenses in the accompanying statements of operations.

As of June 30, 2012, we had not yet recognized compensation expense on the following non-vested awards.

| (In thousands) | | Non-recognized Compensation | Average Remaining Recognition Period (years) |
|---|---|---|---|
| Restricted stock | $ | 1,852 | 1.2 |
| Performance shares | | 1,510 | 1.2 |
| Total | $ | 3,362 | 1.2 |

The following table summarizes unvested restricted stock awards outstanding and changes during the six months ended June 30:

| | 2012 # of Shares | | Price(1) | 2011 # of Shares | | Price(1) |
|---|---|---|---|---|---|---|
| Non-vested restricted shares outstanding January 1 | **129,203** | **$** | **17.79** | 101,435 | $ | 17.40 |
| Shares granted | **14,732** | | **19.30** | 127,377 | | 17.92 |
| Shares cancelled | | | | (10,282) | | 18.48 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Shares vested | | | | | | |
| Non-vested restricted shares outstanding | June 30 | **143,935** | **$** | **17.94** | 218,530 | $ 17.65 |

(1) Represents the weighted average fair value on date of grant.

The following table summarizes unvested performance share-based restricted stock awards outstanding and changes during the six months ended June 30:

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| | | 2012 | | | 2011 | | |
|---|---|---|---|---|---|---|---|
| | | # of Shares | | Price(1) | # of Shares | | Price(1) |
| Non-vested performance shares outstanding | January 1 | **50,879** | **$** | **17.04** | 68,880 | $ | 15.74 |
| Shares granted | | **67,040** | | **17.92** | 50,440 | | 17.92 |
| Shares canceled | | | | | (10,768) | | 16.95 |
| Non-vested performance shares outstanding | June 30 | **117,919** | **$** | **17.54** | 108,552 | $ | 16.63 |

(1) Represents the weighted average fair value on date of grant.

**19. Income Taxes**

There have been no changes to the balance of our unrecognized tax benefits reported at December 31, 2011. As of June 30, 2012 and December 31, 2011, the amount of unrecognized tax benefits was $1.2 million. The total amount of unrecognized benefits that, if recognized, would affect the effective tax rate is $0.8 million. We do not expect any changes in our unrecognized tax benefits during the remainder of 2012.

Our practice is to recognize interest and penalties related to income tax matters in interest expense and general and administrative expense, respectively. At June 30, 2012, we had no material liability for interest or penalties and had no material interest or penalty expense.

The only periods subject to examination for our federal return are years 2008 through 2010. The periods subject to examination for our state returns are years 2005 through 2010. We are not currently under examination by federal taxing authorities. We are currently under examination by state taxing authorities. We do not expect any settlement or payment that may result from the audit to have a material effect on our results of operations or cash flows.

Our effective tax rate was 29.2% and 35.8% for the three month periods ended June 30, 2012 and 2011, respectively and 31.6% and 37.1% for the six month periods ended June 30, 2012 and 2011, respectively. The effective tax rates differ from the federal and state statutory rates primarily due to lower forecasted income due to the acquisition of SureWest, state income taxes owed in certain states where we are required to file on a separate legal entity basis, non-deductible expenses and a change in the Illinois state income tax rate.

**20. Accumulated Other Comprehensive Loss, Net**

Accumulated other comprehensive loss, net is comprised of the following components:

| (In thousands) | June 30, 2012 | December 31, 2011 |
|---|---|---|

| | | | | |
|---|---|---|---|---|
| Fair value of cash flow hedges | **$** | **(13,425)** | $ | (15,932) |
| Prior service credits and net losses on postretirement plans | | **(42,661)** | | (44,102) |
| | | **(56,086)** | | (60,034) |
| Deferred taxes | | **20,734** | | 22,201 |
| Totals | **$** | **(35,352)** | $ | (37,833) |

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## 21. Environmental Remediation Liabilities

Environmental remediation liabilities were $0.2 million at June 30, 2012 and $0.3 million at December 31, 2011, and are included in other long-term liabilities. These liabilities relate to anticipated remediation and monitoring costs with respect to two small vacant sites and are undiscounted. The Company believes the amount accrued is adequate to cover the remaining anticipated costs of remediation.

## 22. Capital Leases

The Company has four capital leases, all of which expire in 2021, for the lease of office, warehouse and tech center space. As of June 30, 2012, the present value of the minimum remaining lease commitments was approximately $4.6 million, of which $0.2 million is due and payable within the next 12 months. The leases will require total remaining rental payments to LATEL, a related party entity, of approximately $6.8 million and total remaining rental payments to Spruce of approximately $1.4 million over the term of the leases. These leases have total payments of $8.2 million on the remaining terms of the leases.

## 23. Litigation and Contingencies

Six putative class action lawsuits were filed by alleged SureWest shareholders challenging the Company s merger with SureWest in which the Company, WH Acquisition Corp. and WH Acquisition II Corp, SureWest and members of the SureWest board of directors have been named as defendants. Five shareholder actions were filed in the Superior Court of California, Placer County, and one shareholder action was filed in the United States District Court for the Eastern District of California. The actions are called Needles v. SureWest Communications, et al., filed February 17, 2012, Errecart v. Oldham, et al., filed February 24, 2012, Springer v. SureWest Communications, et al., filed March 9, 2012, Aievoli v. Oldham, et al., filed March 15, 2012, and Waterbury v. SureWest Communications, et al., filed March 26, 2012, and the federal action is called Broering v. Oldham, et al., filed April 18, 2012. The actions generally allege, among other things, that each member of the SureWest board of directors breached fiduciary duties to SureWest and its shareholders by authorizing the sale of SureWest to the Company for consideration that allegedly was unfair to the SureWest shareholders and agreed to terms that allegedly unduly restrict other bidders from making a competing offer. The complaints also allege that the Company and SureWest aided and abetted the breaches of fiduciary duties allegedly committed by the members of the SureWest board of directors. The Broering complaint also alleges, among other things, that the joint proxy statement/prospectus filed with the SEC on March 28, 2012 did not make sufficient disclosures regarding the merger, that SureWest s board should have appointed an independent committee to negotiate the transaction and that SureWest should have gone back to another bidder to create a competitive bid process. The lawsuits seek equitable relief, including an order to prevent the defendants from consummating the merger on the agreed-upon terms and/or an award of unspecified money damages. On March 14, 2012, the Placer County Superior Court entered an order consolidating the Needles, Errecart and Springer actions into a single action under the caption In re SureWest Communications Shareholder Litigation. Under the terms of this order, all cases subsequently filed in the Superior Court for the State of California, County of Placer, that relate to the same subject matter and involve similar questions of law or fact were to be consolidated with these cases as well. This included the Aievoli and Waterbury cases. On April 10, 2012, the plaintiff in Waterbury filed a request for voluntary dismissal of her complaint without prejudice. On May 18, 2012, pursuant to the parties stipulation, the federal court entered an order staying the Broering action for 90 days. On June 1, 2012, the parties entered into a proposed settlement of all of the shareholder actions without any admission of liability by the Company or the other defendants. Pursuant to the proposed settlement, SureWest agreed to make, and subsequently made,

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certain additional disclosures in a Current Report on Form 8-K filed with the SEC in advance of the special meeting of SureWest shareholders held on June 12, 2012. The proposed settlement also provided that plaintiffs counsel collectively are to receive attorneys fees of $525,000, of which the Company is to pay $36,250, with the balance to be paid by SureWest and its insurer. The proposed settlement is subject to approval by the Placer County Superior Court. Upon approval by the court, the consolidated state court actions and the federal action will be dismissed with prejudice.

On April 15, 2008, Salsgiver Inc., a Pennsylvania-based telecommunications company, and certain of its affiliates filed a lawsuit against us and our subsidiaries North Pittsburgh Telephone Company and North Pittsburgh Systems Inc. in the Court of Common Pleas of Allegheny County, Pennsylvania alleging that we have prevented Salsgiver from connecting their fiber optic cables to our utility poles. Salsgiver seeks compensatory and punitive damages as the result of alleged lost projected profits, damage to its business reputation, and other costs. Salsgiver originally claimed to have sustained losses of approximately $125 million and did not request a specific dollar amount in damages. We believe that these claims are without merit and that the alleged damages are completely unfounded. We intend to defend against these claims vigorously. In the third quarter of 2008, we filed preliminary objections and responses to Salsgiver s complaint. However, the court ruled against our preliminary objections. On November 3, 2008, we responded to Salsgiver s amended complaint and filed a counter-claim for trespass, alleging that Salsgiver attached cables to our poles without an authorized agreement and in an unsafe manner. We are currently in the discovery and deposition stage. Consolidated filed a motion for summary judgment on June 18, 2012 and the court is scheduled to hear oral arguments on August 30, 2012. In addition, we have asked the FCC Enforcement Bureau to address Salsgiver s unauthorized pole attachments and safety violations on those attachments. We believe that these are violations of an FCC order regarding Salsgiver s complaint against us. We do not believe that these claims will have a material adverse impact on our financial results.

Two of our subsidiaries, Consolidated Communications of Pennsylvania Company LLC ( CCPA ) and Consolidated Communications Enterprise Services Inc. ( CCES ), received assessment notices from the Commonwealth of Pennsylvania Department of Revenue increasing the amounts owed for Pennsylvania Gross Receipt Taxes for the tax period ending December 31, 2009. These two assessments adjusted the subsidiaries combined total outstanding taxable gross receipts liability (with interest) to approximately $2.3 million. In addition, based upon recently completed audits of CCES for 2008, 2009 and 2010, we believe the Commonwealth of Pennsylvania may issue additional assessments totaling approximately $1.7 million for Gross Receipt Taxes allegedly owed. Our CCPA subsidiary has also been notified by the Commonwealth of Pennsylvania that they will conduct a gross receipts audit for the calendar year 2008. An appeal challenging the 2009 CCPA assessment was filed with the Department of Revenue s Board of Appeals on September 15, 2011, and we filed a similar appeal for CCES with the Board of Appeals on November 11, 2011 challenging the 2009 CCES assessment. We also intend to appeal any adverse decisions from the Board of Appeals involving CCPA or CCES to the Commonwealth s Board of Finance and Revenue. At the Board of Finance and Revenue, we anticipate that these matters will be continued pending the outcome of present litigation in Commonwealth Court between Verizon Pennsylvania, Inc. and the Commonwealth of Pennsylvania (Verizon Pennsylvania, Inc. v. Commonwealth, Docket No. 266 F.R. 2008). The Gross Receipts Tax issues in the Verizon Pennsylvania case are substantially the same as those presently facing CCPA and CCES. In addition, there are numerous telecommunications carriers with Gross Receipts Tax matters dealing with the same issues that are in various stages of appeal before the Board of Finance and Revenue and the Commonwealth Court. Those appeals by other similarly situated telecommunications carriers have been continued until resolution of the Verizon Pennsylvania case. We believe that these assessments and the positions taken by the Commonwealth of Pennsylvania are without substantial merit. We do not believe that the outcome of these claims will have a material adverse impact on our financial results.

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We are from time to time involved in various other legal proceedings and regulatory actions arising out of our operations. We do not believe that any of these, individually or in the aggregate, will have a material adverse effect upon our business, operating results or financial condition.

## 24. Net Income per Common Share

The following illustrates the earnings allocation method as required by the FASB s authoritative guidance on the treatment of participating securities in the calculation of earnings per share which we utilize in the calculation of basic and diluted earnings per share.

| (In thousands, except per share amounts) | For the three months ended June 30, 2012 | 2011 | For the six months ended June 30, 2012 | 2011 |
|---|---|---|---|---|
| Basic and Diluted Earnings Per Share Using Two-class Method: | | | | |
| Net income | **$ 2,906** | $ 5,513 | **$ 4,790** | $ 13,010 |
| Less: net income attributable to noncontrolling interest | **120** | 162 | **245** | 294 |
| Net income attributable to common shareholders before allocation of earnings to participating securities | **2,786** | 5,351 | **4,545** | 12,716 |
| Less: earnings allocated to participating securities | **95** | 119 | **160** | 246 |
| Net income attributable to common stockholders | **$ 2,691** | $ 5,232 | **$ 4,385** | $ 12,470 |
| | | | | |
| Weighted-average number of common shares outstanding (1) | **29,689** | 29,593 | **29,689** | 29,593 |
| | | | | |
| Net income per common share attributable to common stockholders basic and diluted | **$ 0.09** | $ 0.18 | **$ 0.15** | $ 0.42 |

(1) To the extent that restricted shares are anti-dilutive, they have been excluded from the calculation of diluted earnings per share in accordance with the applicable accounting guidance.

An additional 0.3 million and 0.4 million shares were not included in the computation of potentially dilutive securities at June 30, 2012 and 2011, because they were anti-dilutive.

## 25. Business Segments

The Company is viewed and managed as two separate, but highly integrated, reportable business segments: Telephone Operations and Other Operations. Telephone Operations consists of a wide range of telecommunications services, including local and long-distance service, DSL Internet access, IPTV, VOIP service, custom calling features, private line services, carrier access services, network capacity services over a regional fiber optic network, mobile services and directory publishing. The Company also operates two complementary non-core businesses that comprise Other Operations, including telephone services to correctional facilities and equipment sales. Management evaluates the performance of these business segments based upon net revenue and operating income.

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| (In thousands) | For the three months ended June 30, 2012 | 2011 | For the six months ended June 30, 2012 | 2011 |
|---|---|---|---|---|
| Telephone operations | **$ 85,012** | $ 84,809 | **$ 170,095** | $ 172,203 |
| Other operations | **7,993** | 7,814 | **16,274** | 15,861 |
| Total net revenue | **93,005** | 92,623 | **186,369** | 188,064 |
| | | | | |
| Operating expense telephone operations | **50,011** | 48,797 | **102,899** | 97,742 |
| Operating expense other operations | **7,073** | 7,157 | **14,399** | 14,595 |
| Total operating expense | **57,084** | 55,954 | **117,298** | 112,337 |
| | | | | |
| Depreciation and amortization telephone operations | **21,664** | 21,778 | **43,593** | 43,725 |
| Depreciation and amortization other operations | **205** | 209 | **413** | 420 |
| Total depreciation expense | **21,869** | 21,987 | **44,006** | 44,145 |
| | | | | |
| Operating income telephone operations | **13,337** | 14,234 | **23,603** | 30,736 |
| Operating income - other operations | **715** | 448 | **1,462** | 846 |
| Total operating income | **14,052** | 14,682 | **25,065** | 31,582 |
| | | | | |
| Interest expense, net of interest income | **(16,893)** | (12,397) | **(31,493)** | (24,336) |
| Investment income | **6,762** | 6,097 | **13,228** | 13,014 |
| Other, net | **185** | 210 | **199** | 437 |
| Income before taxes | **$ 4,106** | $ 8,592 | **$ 6,999** | $ 20,697 |
| | | | | |
| Capital expenditures: | | | | |
| Telephone operations | **$ 10,904** | $ 10,634 | **$ 22,055** | $ 20,625 |
| Other operations | **23** | 23 | **96** | 79 |
| Total | **$ 10,927** | $ 10,657 | **$ 22,151** | $ 20,704 |

| | June 30, 2012 | December 31, 2011 |
|---|---|---|
| Goodwill: | | |
| Telephone operations | **$ 519,542** | $ 519,542 |
| Other operations | **1,020** | 1,020 |
| Total | **$ 520,562** | $ 520,562 |
| | | |
| Total assets: | | |
| Telephone operations (1) | **$ 1,473,907** | $ 1,187,708 |
| Other operations | **5,529** | 6,361 |
| Total | **$ 1,479,436** | $ 1,194,069 |

(1) Included within the telephone operations segment assets are our equity method investments totaling $49.5 million and $48.3 million at June 30, 2012 and December 31, 2011, respectively.

**26. Subsequent Events**

The Company closed on the acquisition of SureWest on July 2, 2012. Refer to Footnote 3 Agreement and Plan of Merger with SureWest Communications for a description of the acquisition disclosure.

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

The following discussion of our consolidated operating results and financial condition for the three and six month periods ended June 30, 2012 and 2011 should be read in conjunction with the unaudited condensed consolidated financial statements and related notes contained elsewhere in this report.

*Consolidated Communications or the Company refers to Consolidated Communications Holdings, Inc. alone or with its wholly owned subsidiaries as the context requires. When this report uses the words we, our, or us, they refer to the Company and its subsidiaries.*

**Forward-Looking Statements**

Any statements contained in this Report that are not statements of historical fact, including statements about our beliefs and expectations, are forward-looking statements and should be evaluated as such. The words anticipates , believes , expects , intends , plans , estimates , targets should , may , will and similar words and expressions are intended to identify forward-looking statements. These forward-looking statements are contained throughout this Report, including, but not limited to, statements found in this Part I Item 2 Management s Discussion and Analysis of Financial Condition and Results of Operations , Part I Item 3 Quantitative and Qualitative Disclosures about Market Risk and Part II Item 1 Legal Proceedings . Such forward-looking statements reflect, among other things, our current expectations, plans, strategies, and anticipated financial results and involve a number of known and unknown risks, uncertainties, and factors that may cause our actual results to differ materially from those expressed or implied by these forward-looking statements, including but not limited to:

- our ability to successfully integrate the operations of SureWest Communications following the acquisition and to realize the synergies from the acquisition;
- various risks to stockholders of not receiving dividends and risks to our ability to pursue growth opportunities if we continue to pay dividends according to our current dividend policy;
- the current volatility in economic conditions and the financial markets;
- adverse changes in the value of assets or obligations associated with our employee benefit plans;
- various risks to the price and volatility of our common stock;
- our substantial amount of debt and our ability to refinance it or to incur additional debt in the future;
- our need for a significant amount of cash to service our debt and to pay dividends on our common stock;
- restrictions contained in our debt agreements that limit the discretion of our management in operating our business;
- the ability to refinance our existing debt as necessary;

- rapid development and introduction of new technologies and intense competition in the telecommunications industry;
- transport and content costs are substantial and continue to increase;
- risks associated with our possible pursuit of future acquisitions;
- the length and severity of weakened economic conditions in our service areas in Illinois, Texas, Pennsylvania, California, and Kansas;
- system failures;
- loss of large customers or government contracts;

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- risks associated with the rights-of-way for our network;
- disruptions in our relationship with third party vendors;
- loss of key management personnel and the inability to attract and retain highly qualified management and personnel in the future;
- changes in the extensive governmental legislation and regulations governing telecommunications providers, the provision of telecommunications services and access charges and subsidies, which are a material part of our revenues;
- telecommunications carriers disputing and/or avoiding their obligations to pay network access charges for use of our network;
- high costs of regulatory compliance;
- the competitive impact of legislation and regulatory changes in the telecommunications industry;
- liability and compliance costs regarding environmental regulations; and
- the additional risk factors outlined in Part I Item 1A Risk Factors in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011, and the other documents that we file with the SEC from time to time that could cause our actual results to differ from our current expectations and from the forward-looking statements discussed in this Report.

Many of these risks are beyond our ability to control or predict. All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements contained throughout this Report. Because of these risks, uncertainties, and assumptions, you should not place undue reliance on these forward-looking statements. Furthermore, forward-looking statements speak only as of the date they are made. Except as required under the federal securities laws or the rules and regulations of the U.S. Securities and Exchange Commission, we do not undertake any obligation to update or review any forward-looking information, whether as a result of new information, future events or otherwise.

**Overview**

We are an established rural local exchange carrier that provides communications services to residential and business customers in Illinois, Texas and Pennsylvania. As of July 2, 2012 we extended our communication services to Northern California, primarily in the Sacramento region, and the greater Kansas City, Kansas and Missouri areas with the acquisition of SureWest Communications ( SureWest ). We offer a wide range of telecommunications services, including local and long-distance service, high-speed broadband Internet access ( DSL ), standard and high-definition digital television ( IPTV ), digital telephone service ( VOIP ), custom calling features, private line services, carrier access services, network capacity services over our regional fiber optic network, directory publishing and Competitive Local Exchange Carrier ( CLEC ) services. We also operate two non-core complementary businesses: prison services facilities and equipment sales.

**Executive Summary**

On February 5, 2012, we entered into a definitive agreement with SureWest to acquire all of its outstanding shares in a cash and stock transaction. SureWest provides a wide range of telecommunications, digital video, Internet, data and other facilities-based communications services in Northern California, primarily in the greater Sacramento region, and in the greater Kansas City, Kansas and Missouri areas. For the year ended December 31, 2011, SureWest reported $248.1 million in total operating revenues. For the six months ended June 30, 2012, SureWest generated $127.9 million in operating revenues. We closed on the SureWest transaction on July 2, 2012. The purchase price of the acquisition, excluding debt assumed, consisted of cash of $176.7 million and 9,965,983 shares of the

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Company s common stock (based on average trading prices for the Company s common stock over the 20-day period ending two days before the closing date of the merger), totaled $320.7 million. The cash portion of the merger consideration and the funds required to repay SureWest outstanding debt was financed with the sale of $300.0 million in aggregate principal amount of 10.875% Senior Notes due 2020 ( Senior Notes ). The Company also used cash on hand and approximately $35.0 million in borrowings from its revolving credit facility. Because the acquisition closed on July 2, 2012, the Company s financial information for and as of the quarter and six months ended June 30, 2012 does not include any of the results of operations from SureWest.

We generated net income attributable to common stockholders of $2.8 million, or $0.09 per diluted share, in the second quarter of 2012, as compared to net income attributable to common stockholders of $5.4 million, or $0.18 per diluted share, in the second quarter of 2011. The decrease in net income in the second quarter of 2012 resulted from costs incurred associated with the acquisition of SureWest. During the second quarter of 2012, we incurred $0.6 million in expense related to the acquisition and an additional $5.4 million in interest costs of which includes $2.8 million of interest incurred on the Senior Notes obtained for the SureWest acquisition, $1.1 million amortization of fees related to securing the bridge loan commitment to finance the SureWest acquisition, and $1.5 million of interest related to ticking fees associated with the bridge loan financing. This decrease in net income from the second quarter of 2012 compared to the second quarter 2011 was reduced by the $2.5 million incurred in 2011 for professional fees related to our credit agreement amendment.

Revenue in the second quarter of 2012 increased to $93.0 million as compared to $92.6 million in the second quarter of 2011. Revenue growth in the second quarter 2012 was due to an increase of $2.1 million in revenue from our data and internet sales due to increased DSL and IPTV subscribers. This increase was partially offset by a loss of access lines (which includes local calling services, network access services, subsidies and long-distance services).

**General**

The following general factors should be considered in analyzing our results of operations:

***Revenues***

*Telephone Operations and Other Operations.* Our revenues are derived primarily from the sale of voice and data communication services to residential and business customers in our rural telephone companies service areas. Because we operate primarily in rural service areas, we do not anticipate significant growth in revenues in either of our two operating segments except for through acquisitions, such as that of SureWest.

*Local access lines and bundled services.* An access line is the telephone line connecting a home or business to the public switched telephone network. The number of local access lines in service directly affects the monthly recurring revenue we generate from end users, the amount of traffic on our network, the access charges we receive from other carriers, the federal and state subsidies we receive, and most other revenue streams. We had 225,025, 227,992 and 232,360 local access lines in service as of June 30, 2012, December 31, 2011 and June 30, 2011, respectively.

Most wireline telephone companies have experienced a loss of local access lines due to increased competition from wireless providers, competitive local exchange carriers and, in some cases, cable television operators, along with challenging economic conditions.  We have not been immune to these conditions.  Cable competitors in all of our markets offer a competing voice product.  We estimate

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that cable companies offer voice service to all of their addressable customers, covering 85% of our entire service territory.

In addition, we expect to continue to experience modest erosion in access lines both due to market forces and through our own competing VOIP product.

We have been able in some instances to offset the decline in local access lines with increased average revenue per access line by:

- Aggressively promoting DSL service, including selling DSL as a stand-alone offering;
- Value bundling services, such as DSL or IPTV, with a combination of local service and custom calling features;
- Maintaining excellent customer service standards; and
- Keeping a strong local presence in the communities we serve.

We have implemented a number of initiatives to gain new local access lines and retain existing lines by making bundled service packages more attractive (for example, by adding unlimited long-distance) and by announcing special promotions, like discounted second lines.

We also market a triple play bundle, which includes local telephone service, DSL, and IPTV. As of June 30, 2012, IPTV was available to almost 212,000 homes in our Illinois, Texas and Pennsylvania markets. Our IPTV subscriber base continues to grow and totaled 35,834, 34,356 and 31,218 subscribers as of June 30, 2012, December 31, 2011 and June 30, 2011, respectively.

We also continue to experience growth in the number of DSL subscribers we serve. We had 113,856, 110,913 and 108,581 DSL lines in service as of June 30, 2012, December 31, 2011 and June 30, 2011, respectively. Currently, over 95% of our rural telephone companies local access lines are DSL-capable.

In addition to our access line, DSL and video initiatives, we intend to continue to integrate best practices across our markets. We also continue to look for ways to enhance current products and introduce new services to ensure that we remain competitive and continue to meet our customers needs. These initiatives have included:

- Hosted VOIP service in all of our markets to meet the needs of small- to medium-sized business customers that want robust functionality without having to purchase a traditional key or PBX phone system;
- VOIP service for residential customers, which is being offered to our customers as a growth opportunity and as an alternative to the traditional phone line for customers who are considering a switch to a cable competitor;

- DSL service even to users who do not have our access line which expands our customer base and creates additional revenue-generating opportunities;
- Metro-Ethernet services delivered over our copper infrastructure with speeds of 25 mega-bits per second ( mbps ) to 40 mbps;
- DSL product with speeds up to 20 mbps for those customers desiring greater Internet speed; and
- High definition video service and digital video recorders in all of our IPTV markets.

These efforts may mitigate the financial impact of any access line loss we experience.

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***Expenses***

Our primary operating expenses consist of the cost of services; selling, general and administrative expenses; and depreciation and amortization expenses.

*Cost of services and products.* Our cost of services includes the following:

- Operating expenses relating to plant costs, including those related to the network and general support costs, central office switching and transmission costs, and cable and wire facilities;
- General plant costs, such as testing, provisioning, network, administration, power, and engineering;
- The cost of transport and termination of long-distance and private lines outside our rural telephone companies service area; and
- Costs associated with our standard and high definition video products.

We have agreements with various carriers to provide long-distance transport and termination services. We believe we will meet all of our commitments in these agreements and will be able to procure services for periods after our current agreements expire. We do not expect any material adverse effects from any changes in any new service contract.

*Selling, general and administrative expenses*. Selling, general and administrative expenses include expenses associated with customer care; billing and other operating support systems; and corporate expenses, such as professional service fees and non-cash, stock-based compensation.

Our operating support and back-office systems enter, schedule, provision, and track customer orders; test services and interface with trouble management; and operate inventory, billing, collections, and customer care service systems for the local access lines in our operations. We have migrated most key business processes onto a single company-wide system and platform. We hope to improve profitability by reducing individual company costs through centralizing, standardizing, and sharing best practices.

*Depreciation and amortization expenses.* The provision for depreciation on property and equipment is recorded using the straight-line method based upon the following useful lives:

| | **Years** |
|---|---|
| Buildings | 18 - 40 |
| Network and outside plant facilities | 3 - 50 |
| Furniture, fixtures and equipment | 3 - 15 |

| | |
|---|---|
| Capital leases | 11 |

Amortization expenses are recognized primarily for our intangible assets considered to have finite useful lives on a straight-line basis. In accordance with the applicable authoritative guidance, goodwill and intangible assets that have indefinite useful lives are not amortized but rather are tested at least annually for impairment. Because tradenames have been determined to have indefinite lives, they are not amortized. Customer relationships are amortized over their useful life. The net carrying value of customer lists at June 30, 2012 is being amortized at a weighted-average life of approximately 2.5 years.

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**Results of Operations**

***Segments***

We have two reportable business segments, Telephone Operations and Other Operations. The discussion below covers our consolidated results and results by segment.

Certain prior year amounts have been reclassified to conform to the current year s presentation. These reclassifications had no effect on total stockholders equity, total revenue, income from operations or net income.

***For the Three Months Ended June 30, 2012 Compared to June 30, 2011***

The following summarizes our revenues and operating expenses on a consolidated basis for the three months ended June 30, 2012 and 2011:

| | 2012 | | 2011 | |
|---|---|---|---|---|
| **(In millions, except for percentages)** | **$** | **%** | **$** | **%** |
| Revenue | | | | |
| Telephone operations | | | | |
| Local calling services | **$ 19.7** | **21.2%** | $ 21.4 | 23.1% |
| Network access services | **19.6** | **21.1** | 19.3 | 20.8 |
| Subsidies | **11.2** | **12.0** | 11.1 | 12.0 |
| Long-distance services | **3.5** | **3.8** | 4.1 | 4.4 |
| Data and Internet services | **22.7** | **24.4** | 20.6 | 22.3 |
| Other services | **8.3** | **8.9** | 8.3 | 9.0 |
| Total telephone operations | **85.0** | **91.4** | 84.8 | 91.6 |
| Other operations | **8.0** | **8.6** | 7.8 | 8.4 |
| | | | | |
| Total operating revenue | **93.0** | **100.0** | 92.6 | 100.0 |
| | | | | |
| Expenses | | | | |
| Telephone operations | **49.3** | **53.0** | 46.3 | 50.0 |
| Other operations | **7.1** | **7.6** | 7.1 | 7.7 |
| Transaction/Debt refinancing costs | **0.6** | **0.6** | 2.5 | 2.7 |
| Depreciation and amortization | **21.9** | **23.5** | 22.0 | 23.8 |
| Total operating expense | **78.9** | **84.8** | 77.9 | 84.2 |
| | | | | |
| Income from operations | **14.1** | **15.2** | 14.7 | 15.8 |
| | | | | |
| Interest expense, net | **16.9** | **18.2** | 12.4 | 13.4 |
| Other income | **6.9** | **7.4** | 6.3 | 6.8 |
| Income tax expense | **1.2** | **1.3** | 3.1 | 3.3 |

| | | | | | |
|---|---|---|---|---|---|
| Net income | | **2.9** | **3.1** | 5.5 | 5.9 |
| Net income attributable to noncontrolling interest | | **0.1** | **0.1** | 0.2 | 0.2 |
| | | | | | |
| Net income attributable to common stockholders | **$** | **2.8** | **3.0%** | $ 5.3 | 5.7% |

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*Revenue*

Revenue in the second quarter of 2012 increased by $0.4 million, or 0.4%, to $93.0 million from $92.6 million in the second quarter 2011. Revenue growth in the second quarter 2012 was due to an increase of $2.1 million of revenue from our data and internet sales due to increased DSL and IPTV subscribers. This increase was partially offset by decreases in the number of access lines, which reduced revenues for local calling services and long-distance services.

Access line loss continues to moderate and is being offset by growth in our number of broadband connections. VOIP, DSL and IPTV connections all increased during the second quarter of 2012 as compared to the second quarter of 2011. Connections by type are as follows:

| | June 30, | |
|---|---|---|
| | **2012** | **2011** |
| Residential access lines in service | **136,047** | 138,538 |
| Business access lines in service | **88,978** | 93,822 |
| Total local access lines in service | **225,025** | 232,360 |
| | | |
| IPTV subscribers | **35,834** | 31,218 |
| ILEC DSL subscribers | **113,856** | 108,581 |
| Total broadband connections | **149,690** | 139,799 |
| | | |
| VOIP subscribers | **9,891** | 8,799 |
| CLEC access line equivalents (1) | **94,715** | 81,746 |
| | | |
| Total connections | **479,321** | 462,704 |
| | | |
| Long-distance lines (2) | **182,311** | 175,439 |

(1) CLEC access line equivalents represent a combination of voice services and data circuits. The calculations represent a conversion of data circuits to an access line basis. Equivalents are calculated by converting data circuits (basic rate interface, primary rate interface, DSL, DS-1, DS-3 and Ethernet) and SONET-based (optical) services (OC-3 and OC-48) to the equivalent of an access line.

(2) Reflects the inclusion of long-distance service provided as part of our VOIP offering while excluding CLEC long-distance subscribers.

Telephone Operations Revenue

*Local calling services* revenue decreased by $1.7 million, or 7.9%, to $19.7 million in the second quarter of 2012 compared to $21.4 million in the second quarter of 2011. The decrease is primarily due to the decline in local access lines.

*Network access services* revenue increased by $0.3 million, or 1.6%, to $19.6 million for the second quarter of 2012 compared to $19.3 million in the second quarter of 2011. The increase is primarily due to an increase in federal universal service fees.

*Subsidy* revenues increased by $0.1 million, or 0.9%, to $11.2 million in the second quarter of 2012 compared to $11.1 million in the second quarter of 2011. The increase is principally due to an increase in interstate common line revenue.

*Long-distance services* revenue decreased by $0.6 million, or 14.6%, to $3.5 million in the second quarter of 2012 compared to $4.1 million in the second quarter of 2011. The decrease is

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primarily due to a decline in billable minutes as a result of customers moving to unlimited long-distance plans.

*Data and Internet* revenue increased by $2.1 million, or 10.2%, to $22.7 million in the second quarter of 2012 compared to $20.6 million in the second quarter of 2011. The increase is primarily due to an increase in the number of DSL and IPTV subscribers.

*Other services* revenue was $8.3 million for both the second quarter of 2012 and the second quarter of 2011. Increases in transport revenues were offset by declines in directory revenue.

Other Operations Revenue

Other Operations revenue increased by $0.2 million, or 2.6%, to $8.0 million in the second quarter of 2012 compared to $7.8 million in the second quarter of 2011. The increases were from our prison systems business and our equipment sales and installation business.

*Operating Expenses*

Operating expenses increased in the second quarter of 2012 by $3.0 million, or 5.6%, to $56.4 million as compared to $53.4 million in the second quarter of 2011. Operating expenses by segment are discussed below.

Telephone Operations Operating Expenses

Operating expenses for Telephone Operations increased by $3.0 million, or 6.5%, to $49.3 million in the second quarter of 2012 as compared to $46.3 million in the second quarter of 2011. The increase in operating expense was principally related to higher costs associated with video programming for both increased subscribers and higher programming costs. Telephone operating expenses also increased due to higher pension costs in 2012.

Other Operations Operating Expenses

Operating expenses for Other Operations were $7.1 million for both the second quarter of 2012 and the second quarter of 2011. Increases in professional fees were offset by decreases in bad debt for Other Operations.

*Transaction/Debt refinancing costs*

In connection with the acquisition of SureWest, we incurred $0.6 million of transaction related fees which were recognized as a non-recurring expense in the second quarter of 2012. In the second quarter of 2011, we amended our credit agreement and incurred fees totaling to $2.5 million which were also recognized as a non-recurring expense.

*Depreciation and Amortization*

Depreciation and amortization expense remained relatively flat with a slight decrease of $0.1 million, or 0.5%, to $21.9 million in the second quarter of 2012 as compared to $22.0 million in the second quarter of 2011.

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*Interest Expense, Net*

Interest expense, net of interest income, increased by $4.5 million, or 36.3%, to $16.9 million for the second quarter of 2012 as compared to $12.4 million for the second quarter of 2011. Interest expense in the second quarter of 2012 included $2.8 million of interest expense related to the Senior Notes associated with the SureWest acquisition as well as $1.1 million of amortization related to the financing costs for the bridge loan commitment and $1.5 million of interest related to ticking fees associated with the bridge loan commitment obtained for the SureWest acquisition. This increase was partially offset by decreased interest payments related to our interest rate swaps.

*Other Income (Expense)*

Other income (expense) increased by $0.6 million to $6.9 million in the second quarter of 2012 compared to $6.3 million in the second quarter of 2011. The increase was principally due to higher earnings from our wireless partnership interests.

*Income Taxes*

Our provision for income taxes was $1.2 million in the second quarter of 2012 compared to $3.1 million in the second quarter of 2011. Our effective tax rate was 29.2% for the three months ended June 30, 2012 compared to 35.8% for the three months ended June 30, 2011. The effective tax rates differ from the federal and state statutory rates primarily due to lower forecasted income due to the acquisition of SureWest, state income taxes owed in certain states where we are required to file on a separate legal entity basis and non-deductible expenses.

*Net Income Attributable to Noncontrolling Interest*

The net income attributable to noncontrolling interest totaled $0.1 million in the second quarter of 2012 and $0.2 in the second quarter of 2011. The income for our East Texas Fiber Line, Inc. subsidiary (a joint venture owned 63% by the Company and 37% by Eastex Celco) remained flat period over period.

***For the Six Months Ended June 30, 2012 Compared to June 30, 2011***

The following summarizes our revenues and operating expenses on a consolidated basis for the six months ended June 30, 2012 and 2011:

| | 2012 | | 2011 | |
|---|---|---|---|---|
| **(In millions, except for percentages)** | **$** | **%** | **$** | **%** |

| | | | | | | |
|---|---|---|---|---|---|---|
| Revenue | | | | | | |
| Telephone operations | | | | | | |
| Local calling services | **$** | **39.6** | **21.2** | $ | 43.0 | 22.9 |
| Network access services | | **39.4** | **21.1** | | 40.7 | 21.6 |
| Subsidies | | **22.7** | **12.2** | | 22.7 | 12.1 |
| Long-distance services | | **7.0** | **3.8** | | 8.4 | 4.5 |
| Data and Internet services | | **44.7** | **24.0** | | 40.6 | 21.5 |
| Other services | | **16.7** | **9.0** | | 16.8 | 8.9 |
| Total telephone operations | | **170.1** | **91.3** | | 172.2 | 91.5 |
| Other operations | | **16.3** | **8.7** | | 15.9 | 8.5 |
| | | | | | | |
| Total operating revenue | | **186.4** | **100.0** | | 188.1 | 100.0 |
| | | | | | | |
| Expenses | | | | | | |
| Telephone operations | | **97.5** | **52.3** | | 95.3 | 50.7 |
| Other operations | | **14.4** | **7.7** | | 14.6 | 7.8 |
| Transaction/Debt refinancing costs | | **5.4** | **2.9** | | 2.5 | 1.3 |
| Depreciation and amortization | | **44.0** | **23.6** | | 44.1 | 23.4 |
| Total operating expense | | **161.3** | **86.5** | | 156.5 | 83.2 |
| | | | | | | |
| Income from operations | | **25.1** | **13.5** | | 31.6 | 16.8 |
| | | | | | | |
| Interest expense, net | | **31.5** | **16.9** | | 24.3 | 12.9 |
| Other income | | **13.4** | **7.2** | | 13.4 | 7.1 |
| Income tax expense | | **2.2** | **1.1** | | 7.7 | 4.1 |
| | | | | | | |
| Net income | | **4.8** | **2.6** | | 13.0 | 6.9 |
| Net income attributable to noncontrolling interest | | **0.3** | **0.1** | | 0.3 | 0.2 |
| | | | | | | |
| Net income attributable to common stockholders | **$** | **4.5** | **2.4** | $ | 12.7 | 6.7 |

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*Revenue*

Revenue in the first half of 2012 declined by $1.7 million, or 0.9%, to $186.4 million from $188.1 million in the first half of 2011.  For the first half of the year, revenue was negatively impacted by a decline in revenues related to our traditional wireline telephone business, which impacted revenue for local calling services, network access, subsidies, long-distance services and directory.  Revenue was positively impacted in 2012 by a $4.1 million increase due to the continued growth in our data and internet services (including DSL and IPTV).

Telephone Operations Revenue

*Local calling services* revenue decreased by $3.4 million, or 7.9%, to $39.6 million in the first half of 2012 compared to $43.0 million in the first half of 2011. The decrease is primarily due to a decline in local line revenues as a result of the decline in local access lines.

*Network access services* revenue decreased by $1.3 million, or 3.2%, to $39.4 million in the first half of 2012 compared to $40.7 million in the first half of 2011. The decrease is primarily due to a decline in switched access minutes of use. These decreases were partially offset by higher special access and federal universal service revenues.

*Subsidy* revenue was $22.7 million for both the first half of 2012 and the first half of 2011.

*Long-distance services* revenue decreased by $1.4 million, or 16.7%, to $7.0 million in the first half of 2012 compared to $8.4 million in the first half of 2011. The decrease is primarily due to a decline in billable minutes, primarily due to customers moving to unlimited long-distance plans and the decline in access lines.

*Data and Internet* revenue increased by $4.1 million, or 10.1%, to $44.7 million in the first half of 2012 compared to $40.6 million in the first half of 2011. The increase is primarily due to an increase in the number of DSL and IPTV subscribers.

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*Other services* revenue decreased by $0.1 million, or 0.6%, to $16.7 million in the first half of 2012 compared to $16.8 million in the first half of 2011. The decrease is primarily due to a decline in directory revenue partially offset by an increase in transport revenues.

Other Operations Revenue

Other Operations revenue increased by $0.4 million, or 2.5%, to $16.3 million in the first half of 2012 compared to $15.9 million in the first half of 2011. The increases were from our prison systems business and our equipment sales and installation business.

*Operating Expenses*

Operating expenses increased in the first half of 2012 by $2.0 million, or 1.8%, to $111.9 million as compared to $109.9 million in the first half of 2011. Operating expenses by segment are discussed below.

Telephone Operations Operating Expenses

Operating expenses for Telephone Operations increased by $2.2 million, or 2.3%, to $97.5 million in the first half of 2012 as compared to $95.3 million in the first half of 2011. The increase in operating expense was principally related to higher costs associated with video programming for both increased subscribers and higher programming costs. Telephone operating expenses also increased due to higher pension costs in 2012.

Other Operations Operating Expenses

Operating expenses for Other Operations decreased by $0.2 million, or 1.4%, to $14.4 million in the first half of 2012 as compared to $14.6 million in the first half of 2011. Operating expenses in our other Operations Segment declined as a result of the elimination of costs totaling $4.3 million related to the sale of our telemarketing and operator service businesses. This decrease in cost was partially offset by higher commission payments to the State of Illinois necessitated by an increase in revenue from our prison services business.

*Transaction/Debt refinancing costs*

In connection with the acquisition of SureWest, we incurred $5.4 million of transaction related fees which were recognized as a non-recurring expense in the first half of 2012. In the first half of 2011, we amended our credit agreement and incurred fees totaling $2.5 million that were recognized as a non-recurring expense during 2011.

*Depreciation and Amortization*

Depreciation and amortization expense remained relatively flat with a slight decrease of $0.1 million, or 0.2%, to $44.0 million in the first half of 2012 as compared to $44.1 million in the first half of 2011.

*Interest Expense, Net*

Interest expense, net of interest income, increased by $7.2 million, or 29.6%, to $31.5 million for the first half of 2012 as compared to $24.3 million for the first half of 2011.  Interest expense for the first half of 2012 included $2.8 million of interest expense related to the Senior Notes associated with

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the SureWest acquisition, $4.2 million of amortization related to the financing costs for the bridge loan commitment, and $1.5 million of interest related to ticking fees associated with the bridge loan commitment obtained for the SureWest acquisition.  This increase was partially offset by lower interest payments related to our interest rate swaps.

*Other Income (Expense)*

Other income (expense) was $13.4 million for both the first half of 2012 and the first half of 2011.

*Income Taxes*

Our provision for income taxes was $2.2 million for the first six months of 2012 compared to $7.7 million for the first six months of 2011.  The effective tax rate was 31.6% for the six months ended June, 30, 2012 compared to 37.1% for the six months ended June 30, 2011.  Our effective tax rate differs from the federal and state statutory rates primarily due to lower forecasted income due to the acquisition of SureWest, state income taxes owed in certain states where we are required to file on a separate legal entity basis, non-deductible expenses and a change in Illinois state income tax rates.

*Net Income Attributable to Noncontrolling Interest*

The net income attributable to noncontrolling interest was $0.3 million for both the first half of 2012 and the first half of 2011.  The income for our East Texas Fiber Line, Inc. subsidiary (a joint venture owned 63% by the Company and 37% by Eastex Celco) was stable period over period.

**Liquidity and Capital Resources**

*Outlook and Overview*

The following table sets forth selected information regarding our financial condition.

| (In thousands, except for ratio) | | June 30, 2012 | | December 31, 2011 |
|---|---|---|---|---|
| Cash and cash equivalents | **$** | **84,984** | $ | 105,704 |
| Restricted cash     see footnote 4 | | **315,082** | | |

| | | |
|---|---|---|
| Working capital excluding restricted cash | **48,972** | 83,040 |
| Total debt and capital leases | **1,178,274** | 884,711 |
| Current ratio excluding restricted cash | **1.48** | 1.97 |

Our operating requirements have historically been funded from cash flows generated from our business and borrowings under our credit facilities. We expect that our future operating requirements will continue to be funded from cash flows generated from our business and, if needed, from borrowings under our revolving credit facility.

As a general matter, we expect that our liquidity needs for the remainder of 2012 will arise primarily from: (i) dividend payments of between $30.3 million and $31.3 million; (ii) interest payments on our indebtedness of between $39.0 million and $40.0 million and principal payment on debt of $4.4 million; (iii) capital expenditures of between $50.0 million and $55.5 million; (iv) cash income tax payments; (v) pension, 401(k) and other post retirement obligations of between $15.0 million and $17.5 million; (vi) change of control payments of between $7.6 million and $12.1 million

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for the SureWest acquisition, and (vii) certain other costs. On July 2, 2012, we used $298.0 million of the restricted cash, $73.4 million in cash from the balance sheet, and $35.0 million from our revolver to fund the acquisition of SureWest and repayment of certain of its outstanding debt. However, in the future our ability to use cash may be limited by our other expected uses of cash, including our dividend policy, and our ability to incur additional debt will be limited by our existing and future debt agreements.

While we expect the SureWest acquisition to be de-leveraging, it was necessary for us to take on additional debt to fund the transaction. See Part II Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Credit Facilities . We believe that cash flows from operating activities, together with our existing cash and borrowings available under our revolving credit facility will be sufficient for at least the next twelve months to fund our current anticipated uses of cash. After that, our ability to fund these expected uses of cash and to comply with the financial covenants under our debt agreements will depend on the results of future operations, performance and cash flow. Our ability to fund these expected uses from the results of future operations will be subject to prevailing economic conditions and to financial, business, regulatory, legislative and other factors, many of which are beyond our control.

We may be unable to access the cash flows of our subsidiaries since certain of our subsidiaries are parties to credit or other borrowing agreements, or subject to statutory or regulatory restrictions, that restrict the payment of dividends or making intercompany loans and investments, and those subsidiaries are likely to continue to be subject to such restrictions and prohibitions for the foreseeable future. In addition, future agreements that our subsidiaries may enter into governing the terms of indebtedness may restrict our subsidiaries ability to pay dividends or advance cash in any other manner to us.

To the extent that our business plans or projections change or prove to be inaccurate, we may require additional financing or require financing sooner than we currently anticipate. Sources of additional financing may include commercial bank borrowings, other strategic debt financing, sales of nonstrategic assets, vendor financing or the private or public sales of equity and debt securities. There can be no assurance that we will be able to generate sufficient cash flows from operations in the future, that anticipated revenue growth will be realized, or that future borrowings or equity issuances will be available in amounts sufficient to provide adequate sources of cash to fund our expected uses of cash. Failure to obtain adequate financing, if necessary, could require us to significantly reduce our operations or level of capital expenditures which could have a material adverse effect on our financial condition and the results of operations.

As discussed below, the margin for each tranche of our term loan is fixed for the duration of the loan and we had $50 million available under our revolving credit facility as of June 30, 2012. On July 2, 2012, we drew $35.0 million on this revolver to help fund the acquisition of SureWest. Based on our discussion with banks participating in the bank group, we expect the remaining $15.0 million of the funds to be available under the revolving credit facility if necessary.

*Sources of Liquidity*

Our current principal sources of liquidity are cash and cash equivalents, working capital, and cash available under our secured revolving credit facility.

*Cash and cash equivalents*. For the first half of 2012, cash and cash equivalents decreased by $20.7 million as compared to an increase in cash and cash equivalents of $14.3 million during the first half of 2011. During the second quarter of 2012, $17.0 million of cash moved from cash to cash equivalents to restricted cash. Refer to Item 1 Footnote 4. Restricted Cash for a description of the

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restrictions.  The remaining decrease is a result of SureWest acquisition related-costs as well as quarterly principal payments on our outstanding debt.

*Working capital, excluding restricted cash*.  Our net working capital position decreased by $22.1 million at June 30, 2012 versus June 30, 2011.  Our decreased working capital position in 2012 is principally the result of the decrease in cash and cash equivalents, as noted above, for the move of cash to restricted cash. The remainder of this decrease in our working capital position for 2012 is related to increased accrued transaction expenses and financing costs related to the acquisition of SureWest.

*Cash available under our secured revolving credit facility*.  At June 30, 2012 and 2011, we had no borrowings outstanding under our secured revolving credit facility and $50.0 million of availability.  On July 2, 2012 we used $35.0 million to fund the acquisition of SureWest, leaving $15.0 million of fund availability on the revolving credit facility after the closing.

*Uses of Liquidity*

Our principal uses of liquidity are dividend payments, interest expense and other payments on our debt, capital expenditures, payments made to fund our pension and other postretirement obligations, and transaction costs related to the SureWest acquisition.

*Dividend payments*.  We used $11.6 million of cash to make dividend payments to shareholders during the second quarter of 2012 and 2011.  We used $23.2 million of cash to make dividend payments to shareholders during the first half of 2012 and $23.1 million in the first half of 2011.  Our current quarterly dividend rate is $0.38738 per share.

*Interest and other payments related to outstanding debt and capital leases*.  During the second quarter of 2012, we used $10.9 million of cash to make required interest payments on our outstanding debt and $47 thousand of cash to reduce our capital lease obligations.  We also used $2.2 million of cash to reduce our total outstanding debt obligations during the second quarter of 2012.  During the second quarter of 2011, we used $11.8 million of cash to make required interest payments on our outstanding debt and $37 thousand of cash to reduce our capital lease obligations.

For the first half of 2012, we used $21.9 million of cash to make required interest payments on our outstanding debt and $92 thousand of cash to reduce our capital lease obligations.  For the first half of 2011, we used $23.2 million of cash to make required interest payments on our outstanding debt and $71 thousand of cash to reduce our capital lease obligations.  We also used $4.4 million of cash to reduce our total outstanding debt obligations during the first half of 2012.

*Pension and postretirement obligations*.  In the second quarter of 2012, we used $3.9 million of cash to fund pension, 401(k) and other postretirement obligations.  In the second quarter of 2011, we used $3.6 million of cash to fund pension, 401(k) and other postretirement obligations.  The increase in pension and postretirement payments in the second quarter of 2012 versus 2011 primarily reflects a $0.6 million payment to our qualified pension plan.

In the first half of 2012, we used $7.2 million of cash to fund pension, 401(k) and other postretirement obligations.  In the first half of 2011, we used $7.0 million of cash to fund pension, 401(k) and other postretirement obligations.  The increase for the first six months of 2012 is related to higher funding requirements.

*Capital expenditures*.  During the second quarter of 2012, we spent approximately $10.9 million on capital projects.  During the second quarter of 2011, we spent approximately $10.7 million

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on capital projects. For the first six months of 2012, we spent approximately $22.2 million on capital projects. During the first six months of 2011, we spent approximately $20.7 million on capital projects.

*Transaction costs related to SureWest Acquisition.* We used $0.6 million of cash for transaction related costs for the acquisition of SureWest during the second quarter of 2012. We used $5.4 million of cash for transaction costs for the acquisition of SureWest during the first half of 2012. No cash was used in 2011 related to the SureWest transaction.

*Debt*

The following table summarizes our indebtedness as of June 30, 2012:

| **(In thousands)** | | **Balance** | **Maturity Date** | **Rate (1)** |
|---|---|---|---|---|
| Capital leases | $ | 4,619 | May 31, 2021 | 13.7% (2) |
| $50 million revolving credit facility | | | June 8, 2016 | LIBOR plus 3.25%(3) |
| Senior Notes net of discount | $ | 298,055 | June 1, 2020 | 10.875% |
| Term loan tranche A | $ | 468,593 | December 31, 2014 | LIBOR plus 2.50% |
| Term loan tranche B | $ | 407,007 | December 31, 2017 | LIBOR plus 3.75% |

(1) As of June 30, 2012, the 1-month LIBOR rate in effect on our borrowings was 0.246%.

(2) Weighted-average rate.

(3) On July 2, 2012, we used $35.0 million of the revolving credit facility with the acquisition of SureWest.

*Credit Facilities*

Borrowings under our secured credit agreement are secured by substantially all of our assets (other than our Illinois Consolidated Telephone Company subsidiary, and certain future subsidiaries). The credit agreement contains customary affirmative covenants, which require us and our subsidiaries to furnish specified financial information to the lenders, comply with applicable laws, maintain our properties and assets and maintain insurance on our properties, among others, and contains customary negative covenants which restrict our and our subsidiaries ability to incur additional debt and issue capital stock, create liens, repay other debt, sell assets, make investments, loans, guarantees or advances, pay dividends, repurchase equity interests or make other restricted payments, engage in affiliate transactions, make capital expenditures, engage in mergers, acquisitions or consolidations, enter into sale-leaseback transactions, amend specified documents, enter into agreements that restrict dividends from subsidiaries and change the business we conduct. In addition, the credit agreement requires us to comply with specified financial ratios that are summarized below under Covenant Compliance .

As of June 30, 2012, the first term loan tranche consists of $468.6 million aggregate principal amount, matures on December 31, 2014 and has an applicable margin (at our election) equal to either 2.50% for a LIBOR-based term loan or 1.50% for an alternative base rate loan.  The second term loan tranche consists of $407.0 million aggregate principal amount, matures on December 31, 2017 and has an applicable margin (at our election) equal to either 3.75% for a LIBOR-based term loan or 2.75% for an alternative base rate term loan.  The applicable margins for each of the term loan tranches are fixed for the duration of the loans.

Our revolving credit facility has a maturity date of June 8, 2016 and an applicable margin (at our election) of between 2.75% and 3.50% for LIBOR-based borrowings and between 1.75% and 2.50% for alternative base rate borrowings, depending on our leverage ratio.  Based on our leverage ratio of 4.61:1.00 at June 30, 2012, the borrowing margin for the next three month period ending

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September 30, 2012 will be at a weighted-average margin of 3.25% for a LIBOR-based loan or 2.25% for an alternative base rate loan. There were no borrowings or letters of credit outstanding under the revolving credit facility as of June 30, 2012 or December 31, 2011, or at any time during the quarter ended June 30, 2012. On July 2, 2012, we used $35.0 million of the revolving credit facility with the acquisition of SureWest.

For the quarter ended June 30, 2012, the weighted-average interest rate incurred on our secured term debt, including payments made under our interest rate swap agreement, was 4.90% per annum.

On May 30, 2012, we completed an offering of $300.0 million aggregate principal amount of its 10.875% Senior Notes due 2020 (the Senior Notes ) through our wholly-owned subsidiary, Consolidated Communications Finance Co. ( Finance Co. ). The Senior Notes were sold in the United States to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933 (the Securities Act ) and outside in the Unites States in compliance with Regulation S under the Securities Act. In addition, some of the Senior Notes were sold to certain accredited investors (as defined in Rule 501 under the Securities Act). Upon closing of the SureWest acquisition on July 2, 2012, Finance Co. merged with and into our wholly-owned subsidiary Consolidated Communications, Inc., which assumed the Senior Notes, and we and certain of our subsidiaries also fully and unconditionally guaranteed the Senior Notes. The net proceeds of the Senior Notes were used to finance the acquisition of SureWest. The Senior Notes will mature on June 1, 2020. Interest is payable on the Senior Notes at a rate of 10.875% per year, payable semi-annually in arrears on June 1 and December 1 of each year, commencing on December 1, 2012.

For the quarter ended June 30, 2012, the weighted-average interest rate incurred on all of our debt, including the unsecured Senior Notes, was 6.42% per annum.

*Derivative Instruments*

At June 30, 2012, we had $400 million notional amount of floating to fixed interest rate swap agreements outstanding and $230 million notional amount of basis swaps outstanding. The swaps are in place to hedge the change in overall cash flows related to our term loan, the driver of which is changes in the underlying variable interest rate.

The $230 million notional amount of floating to fixed basis swap agreements outstanding are setup whereby we receive 3-month LIBOR-based interest payments from the swap counterparties and pay a fixed rate. The basis swap agreements are structured so that we pay 3-month LIBOR-based payments less a fixed percentage to the basis swap counterparties, and receive 1-month LIBOR. Concurrent with the execution of the basis swaps, we began electing 1-month LIBOR resets on our credit facility.

The $400 million notional amount of floating to fixed interest rate swap agreements are setup whereby we make fixed payments to the swap counterparties and receive 1-month LIBOR. These swaps have staggered maturity dates.

In addition, we also currently have in place $175 million notional amounts of forward floating to fixed interest rate swap agreement that become effective and mature on staggered dates. For these swap agreements, we will make fixed payments to the swap counterparty and receive 1-month LIBOR.

*Covenant Compliance*

In general, our amended credit agreement restricts our ability to pay dividends to the amount of our Available Cash accumulated after October 1, 2005, plus $23.7 million and minus the aggregate amount of dividends paid after July 27, 2005. Available Cash for any period is defined in our credit facility as Consolidated EBITDA (a) minus, to the extent not deducted in the determination of Consolidated EBITDA, (i) non-cash dividend income for such period; (ii) consolidated interest expense for such period net of amortization of debt issuance costs incurred (A) in connection with or prior to the consummation of the acquisition of North Pittsburgh or (B) in connection with the redemption of our then outstanding senior notes; (iii) capital expenditures from internally generated funds; (iv) cash income taxes for such period; (v) scheduled principal payments of Indebtedness, if any; (vi) voluntary repayments of indebtedness, mandatory prepayments of term loans and net increases in outstanding revolving loans during such period; (vii) the cash costs of any extraordinary or unusual losses or charges; and (viii) all cash payments made on account of losses or charges expensed prior to such period (b) plus, to the extent not included in Consolidated EBITDA, (i) cash interest income; (ii) the cash amount realized in respect of extraordinary or unusual gains; and (iii) net decreases in revolving loans. Based on the results of operations from October 1, 2005 through June 30, 2012, and after taking into consideration dividend payments (including the $11.6 million dividend declared in May 1, 2012 and paid on August 1, 2012), we continue to have $182.3 million in dividend availability under the credit facility covenant.

Under our amended credit agreement, if our total net leverage ratio (as such term is defined in the amended credit agreement), as of the end of any fiscal quarter, is greater than 5.10:1.00, we will be required to suspend dividends on our common stock unless otherwise permitted by an exception for dividends that may be paid from the portion of proceeds of any sale of equity not used to make mandatory prepayments of loans and not used to fund acquisitions, capital expenditures or make other investments. During any dividend suspension period, we will be required to repay debt in an amount equal to 50.0% of any increase in available cash (as such term is defined in our credit agreement) during such dividend suspension period, among other things. In addition, we will not be permitted to pay dividends if an event of default under the amended credit agreement has occurred and is continuing. Among other things, it will be an event of default if our interest coverage ratio as of the end of any fiscal quarter is below 2.25:1.00. As of June 30, 2012, our total net leverage ratio was 4.61:1.00 and our interest coverage ratio was 3.27:1.00.

The descriptions of the covenants above and of our amended credit agreement and our Senior Notes generally in this Report are summaries only. They do not contain a full description, including definitions, of the provisions summarized. As such, these summaries are qualified in their entirety by these documents, which are filed as exhibits to our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K.

*Dividends*

The cash required to fund dividend payments is in addition to our other expected cash needs, which we expect to fund with cash flows from our operations. In addition, we expect we will have sufficient availability under our revolving credit facility to fund dividend payments in addition to any expected fluctuations in working capital and other cash needs, although we do not intend to borrow under this facility to pay dividends.

We believe that our dividend policy will limit, but not preclude, our ability to grow. If we continue paying dividends at the level currently anticipated under our dividend policy, we may not retain a sufficient amount of cash, and may need to seek refinancing, to fund a material expansion of our business, including any significant acquisitions or to pursue growth opportunities requiring capital expenditures significantly beyond our current expectations. In addition, because we expect a significant portion of cash available will be distributed to holders of common stock under our dividend policy, our ability to pursue any material expansion of our business will depend more than it otherwise would on our ability to obtain third-party financing.

We anticipate no change to the dividend policy as a result of the SureWest acquisition that closed on July 2, 2012.

*Capital Leases*

The Company has four capital leases, all of which expire in 2021, for the lease of office, warehouse and tech center space. As of June 30, 2012, the present value of the minimum remaining lease commitments was approximately $4.6 million, of which $0.2 million is due and payable within the next 12 months. The leases require total remaining rental payments of approximately $8.2 million over the remaining term of the leases.

*Surety Bonds*

In the ordinary course of business, we enter into surety, performance, and similar bonds. As of June 30, 2012, we had approximately $1.2 million of these bonds outstanding.

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

We are exposed to market risk from changes in interest rates. Market risk is the potential loss arising from adverse changes in market interest rates on our variable rate obligations. We calculate the potential change in interest expense caused by changes in market interest rates by determining the effect of the hypothetical rate increase on the portion of our variable rate debt that is not hedged through the interest rate swap agreements.

During the first six months of 2012, the interest rate on approximately $346.7 million of our floating rate debt was not fixed through the use of interest rate swaps, thereby subjecting this portion of our debt to potential changes in interest rates. If market interest rates changed by 1.0% from the average rates that prevailed during the first six months of this year, interest expense would have increased or decreased by approximately $1.8 million for this six month period.

As of June 30, 2012, the fair value of our interest rate swap agreements amounted to a net liability of $8.6 million, net of deferred taxes, which is recognized as a deferred loss within accumulated other comprehensive loss.

**Item 4. Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed by us in our reports that we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures. Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of June 30, 2012. Based upon that evaluation and subject to the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective. No change in our

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internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) occurred during our fiscal quarter ended June 30, 2012 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

Six putative class action lawsuits were filed by alleged SureWest shareholders challenging the Company s merger with SureWest in which the Company, WH Acquisition Corp. and WH Acquisition II Corp, SureWest and members of the SureWest board of directors have been named as defendants. Five shareholder actions were filed in the Superior Court of California, Placer County, and one shareholder action was filed in the United States District Court for the Eastern District of California. The actions are called Needles v. SureWest Communications, et al., filed February 17, 2012, Errecart v. Oldham, et al., filed February 24, 2012, Springer v. SureWest Communications, et al., filed March 9, 2012, Aievoli v. Oldham, et al., filed March 15, 2012, and Waterbury v. SureWest Communications, et al., filed March 26, 2012, and the federal action is called Broering v. Oldham, et al., filed April 18, 2012. The actions generally allege, among other things, that each member of the SureWest board of directors breached fiduciary duties to SureWest and its shareholders by authorizing the sale of SureWest to the Company for consideration that allegedly was unfair to the SureWest shareholders and agreed to terms that allegedly unduly restrict other bidders from making a competing offer. The complaints also allege that the Company and SureWest aided and abetted the breaches of fiduciary duties allegedly committed by the members of the SureWest board of directors. The Broering complaint also alleges, among other things, that the joint proxy statement/prospectus filed with the SEC on March 28, 2012 did not make sufficient disclosures regarding the merger, that SureWest s board should have appointed an independent committee to negotiate the transaction and that SureWest should have gone back to another bidder to create a competitive bid process. The lawsuits seek equitable relief, including an order to prevent the defendants from consummating the merger on the agreed-upon terms and/or an award of unspecified money damages. On March 14, 2012, the Placer County Superior Court entered an order consolidating the Needles, Errecart and Springer actions into a single action under the caption In re SureWest Communications Shareholder Litigation. Under the terms of this order, all cases subsequently filed in the Superior Court for the State of California, County of Placer, that relate to the same subject matter and involve similar questions of law or fact were to be consolidated with these cases as well. This included the Aievoli and Waterbury cases. On April 10, 2012, the plaintiff in Waterbury filed a request for voluntary dismissal of her complaint without prejudice. On May 18, 2012, pursuant to the parties stipulation, the federal court entered an order staying the Broering action for 90 days. On June 1, 2012, the parties entered into a proposed settlement of all of the shareholder actions without any admission of liability by the Company or the other defendants. Pursuant to the proposed settlement, SureWest agreed to make, and subsequently made, certain additional disclosures in a Current Report on Form 8-K filed with the SEC in advance of the special meeting of SureWest shareholders held on June 12, 2012. The proposed settlement also provided that plaintiffs counsel collectively are to receive attorneys fees of $525,000, of which the Company is to pay $36,250, with the balance to be paid by SureWest and its insurer. The proposed settlement is subject to approval by the Placer County Superior Court. Upon approval by the court, the consolidated state court actions and the federal action will be dismissed with prejudice.

On April 15, 2008, Salsgiver Inc., a Pennsylvania-based telecommunications company, and certain of its affiliates filed a lawsuit against us and our subsidiaries North Pittsburgh Telephone Company and North Pittsburgh Systems Inc. in the Court of Common Pleas of Allegheny County, Pennsylvania alleging that we have prevented Salsgiver from connecting their fiber optic cables to our utility poles. Salsgiver seeks compensatory and punitive damages as the result of alleged lost projected profits, damage to its business reputation, and other costs. Salsgiver originally claimed to have sustained losses of approximately $125 million and did not request a specific dollar amount in damages. We believe that these claims are without merit and that the alleged damages are completely unfounded. We intend to defend against these claims vigorously. In the third quarter of 2008, we filed preliminary

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objections and responses to Salsgiver s complaint. However, the court ruled against our preliminary objections. On November 3, 2008, we responded to Salsgiver s amended complaint and filed a counter-claim for trespass, alleging that Salsgiver attached cables to our poles without an authorized agreement and in an unsafe manner. We are currently in the discovery and deposition stage. Consolidated filed a motion for summary judgment on June 18, 2012 and the court is scheduled to hear oral arguments on August 30, 2012. In addition, we have asked the FCC Enforcement Bureau to address Salsgiver s unauthorized pole attachments and safety violations on those attachments. We believe that these are violations of an FCC order regarding Salsgiver s complaint against us. We do not believe that these claims will have a material adverse impact on our financial results.

Two of our subsidiaries, Consolidated Communications of Pennsylvania Company LLC ( CCPA ) and Consolidated Communications Enterprise Services Inc. ( CCES ), received assessment notices from the Commonwealth of Pennsylvania Department of Revenue increasing the amounts owed for Pennsylvania Gross Receipt Taxes for the tax period ending December 31, 2009. These two assessments adjusted the subsidiaries combined total outstanding taxable gross receipts liability (with interest) to approximately $2.3 million. In addition, based upon recently completed audits of CCES for 2008, 2009 and 2010, we believe the Commonwealth of Pennsylvania may issue additional assessments totaling approximately $1.7 million for Gross Receipt Taxes allegedly owed. Our CCPA subsidiary has also been notified by the Commonwealth of Pennsylvania that they will conduct a gross receipts audit for the calendar year 2008. An appeal challenging the 2009 CCPA assessment was filed with the Department of Revenue s Board of Appeals on September 15, 2011, and we filed a similar appeal for CCES with the Board of Appeals on November 11, 2011 challenging the 2009 CCES assessment. We also intend to appeal any adverse decisions from the Board of Appeals involving CCPA or CCES to the Commonwealth s Board of Finance and Revenue. At the Board of Finance and Revenue, we anticipate that these matters will be continued pending the outcome of present litigation in Commonwealth Court between Verizon Pennsylvania, Inc. and the Commonwealth of Pennsylvania (Verizon Pennsylvania, Inc. v. Commonwealth, Docket No. 266 F.R. 2008). The Gross Receipts Tax issues in the Verizon Pennsylvania case are substantially the same as those presently facing CCPA and CCES. In addition, there are numerous telecommunications carriers with Gross Receipts Tax matters dealing with the same issues that are in various stages of appeal before the Board of Finance and Revenue and the Commonwealth Court. Those appeals by other similarly situated telecommunications carriers have been continued until resolution of the Verizon Pennsylvania case. We believe that these assessments and the positions taken by the Commonwealth of Pennsylvania are without substantial merit. We do not believe that the outcome of these claims will have a material adverse impact on our financial results.

We are from time to time involved in various other legal proceedings and regulatory actions arising out of our operations. We do not believe that any of these, individually or in the aggregate, will have a material adverse effect upon our business, operating results or financial condition.

**Item 1A. Risk Factors**

The Company included in its Annual Report on Form 10-K as of December 31, 2011 a description of certain risks and uncertainties that could affect the Company s business, future performance or financial condition ( Risk Factors ). The following risk factors were identified in addition to those risk factors presented on Form 10-K as of December 31, 2011.

***Transport and content costs are substantial and continue to increase***. We expect the cost of video transport and content costs to continue to be one of our largest operating costs associated with providing video service. Video programming content includes cable-oriented programming designed to be shown in linear channels, as well as the programming of local over-the-air television stations that we retransmit. In addition, on-demand programming is being made available in response to customer

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demand. In recent years, the cable industry has experienced rapid increases in the cost of programming, especially the costs for sports programming and for local broadcast station retransmission consent. Programming costs are generally assessed on a per-subscriber basis, and therefore are related directly to the number of subscribers to which the programming is provided. Our relatively small base of subscribers limits our ability to negotiate lower per-subscriber programming costs. Larger cable companies often can qualify for discounts based on the number of their subscribers. This cost difference can cause us to experience reduced operating margins, while our competitors with a larger subscriber base may not experience similar margin compression. In addition, escalators in existing content agreements cause cost increases that are out of line with general inflation. While we expect these increases to continue we may not be able to pass our programming cost increases on to our customers, particularly as an increasing amount of programming content becomes available via the Internet at little or no cost. Also, some competitors (or their affiliates) own programming in their own right and we may be unable to secure license rights to that programming. As our programming contracts with content providers expire, there can be no assurance that they will be renewed on acceptable terms or that they will be renewed at all, in which case we may be unable to provide such programming as part of our video services packages and our business and results of operations may be adversely affected.

***If key suppliers or other communications companies that our business relies on experience financial difficulties it may adversely affect our operations and results of operations.*** We depend on third party vendors to supply us with a significant amount of hardware, software and operational support necessary to provide certain of our services and to maintain, upgrade and enhance our network facilities and operations. Our video platform is made available through a third party vendor. If any of our third party vendors, some of whom represent our primary source of supply for products and services for which there are few substitutes, should experience financial difficulties or elect to exit an area in which we depend upon them, it could cause us to experience delays or service interruptions, and to incur additional expenses.

We originate and terminate calls for long distance carriers and other interexchange carriers over our network in exchange for access charges that represent a significant revenue stream. If any of these carriers go bankrupt or experience substantial financial difficulties, our inability to timely collect access charges from them could have a negative effect on our business and results of operations. Increasingly, the services of third parties that trigger access charges that we receive are being replaced by other services and treated as being outside the access charge structure. Therefore, we may receive significantly lower sums as compensation for originating and terminating these services. In addition, we are dependent on easements, franchises and licenses from various private parties such as established telephone companies and other utilities, railroads, long-distance companies and from state highway authorities, local governments and transit authorities for access to aerial pole space, underground conduits and other rights-of-way in order to construct and operate our networks. The failure to maintain in effect the necessary third party arrangements on acceptable terms would have an adverse effect on our ability to conduct our business.

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

None

**Item 3. Defaults Upon Senior Securities**

None

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**Item 4.** **Mine Safety Disclosures**

Not Applicable

**Item 5.** **Other Information**

None

**Item 6.** **Exhibits**

(a) Exhibits

4.1 Indenture, dated as of May 30, 2012, between Consolidated Communications, Inc. ( CCI ) (as successor to Consolidated Communications Finance Co. ( CCFC )) and Wells Fargo Bank, National Association, as trustee (incorporated by reference to Exhibit 4.1 to Form 8-K dated May 30, 2012).

4.2 Form of 10.875% Senior Note due 2020 (included as Exhibit A to Exhibit 4.1).

4.3 Registration Rights Agreement, dated as of May 30, 2012, between CCFC and Morgan Stanley & Co. LLC (incorporated by reference to Exhibit 4.4 to Form 8-K dated May 30, 2012).

31.1 Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes- Oxley Act of 2002.

31.2 Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101* The following financial information from Consolidated Communications Holdings, Inc. Quarterly Report on Form 10-Q for the quarter ended June 30, 2012, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Statements of Operations, (ii) the Condensed Consolidated Balance Sheets, (iii) the Condensed Consolidated Statements of Changes in Stockholders Equity, (iv) the Condensed Consolidated Statements of Cash Flows, and (v) Notes to Unaudited Condensed Consolidated Financial Statements.

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* Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files in Exhibit 101 hereto are not deemed filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are not deemed filed for purposes of

Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

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**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.

CONSOLIDATED COMMUNICATIONS HOLDINGS, INC.

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| August 6, 2012 | By: | /s/ Robert J. Currey<br>Robert J. Currey<br>President and Chief Executive Officer<br>(Principal Executive Officer) |
| August 6, 2012 | By: | /s/ Steven L. Childers<br>Steven L. Childers<br>Chief Financial Officer<br>(Principal Financial Officer and Chief Accounting Officer) |