

UNITED STATES CELLULAR CORP
Form 10-Q
August 03, 2018

UNITED STATES
SECURITIES AND
EXCHANGE
COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period
ended June 30, 2018

OR

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

For the transition period
from
to

Commission file number
001-09712

UNITED STATES
CELLULAR
CORPORATION
(Exact name of Registrant
as specified in its charter)
Delaware 62-1147325
(State or (IRS Employer
other Identification

jurisdictionNo.)
of
incorporation
or
organization)

8410 West Bryn Mawr,
Chicago, Illinois 60631
(Address of principal
executive offices) (Zip
code)

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

Yes No

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

[x] []

Indicate by check [x] []
mark whether the
registrant has
submitted
electronically
every Interactive
Data File required
to be submitted
and posted
pursuant to Rule
405 of Regulation

S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

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

Large accelerated filer	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	Smaller reporting company	<input type="checkbox"/>
	Emerging growth company	<input type="checkbox"/>

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Exchange Act).

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

Class	Outstanding at June 30, 2018
Common Shares, \$1 par value	52,545,519 Shares
Series A Common Shares, \$1 par value	33,005,877 Shares

United States Cellular Corporation

Quarterly Report on Form 10-Q
For the Period Ended June 30, 2018

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Signatures

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United States Cellular Corporation

Management's Discussion and Analysis of

Financial Condition and Results of Operations

Executive Overview

The following discussion and analysis compares United States Cellular Corporation's (U.S. Cellular) financial results for the three and six months ended June 30, 2018, to the three and six months ended June 30, 2017. It should be read in conjunction with U.S. Cellular's interim consolidated financial statements and notes included herein, and with the description of U.S. Cellular's business, its audited consolidated financial statements and Management's Discussion and Analysis (MD&A) of Financial Condition and Results of Operations included in U.S. Cellular's Annual Report on Form 10-K (Form 10-K) for the year ended December 31, 2017. Certain numbers included herein are rounded to millions for ease of presentation; however, calculated amounts and percentages are determined using the unrounded numbers.

This report contains statements that are not based on historical facts, including the words "believes," "anticipates," "estimates," "expects," "plans," "intends," "projects," and similar expressions. These statements constitute and represent "forward looking statements" as this term is defined in the Private Securities Litigation Reform Act of 1995. Such forward looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, events or developments to be significantly different from any future results, events or developments expressed or implied by such forward looking statements. See Private Securities Litigation Reform Act of 1995 Safe Harbor Cautionary Statement for additional information.

U.S. Cellular uses certain "non-GAAP financial measures" and each such measure is identified in the MD&A. A discussion of the reason U.S. Cellular determines these metrics to be useful and a reconciliation of these measures to their most directly comparable measures determined in accordance with accounting principles generally accepted in the United States of America (GAAP) are included in the Supplemental Information Relating to Non-GAAP Financial Measures section within the MD&A of this Form 10-Q Report.

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General

U.S. Cellular owns, operates, and invests in wireless markets throughout the United States. U.S. Cellular is an 83%-owned subsidiary of Telephone and Data Systems, Inc. (TDS). U.S. Cellular's strategy is to attract and retain wireless customers through a value proposition comprised of a high-quality network, outstanding customer service, and competitive devices, plans, and pricing, all provided with a local focus.

OPERATIONS

- ◆ Serves customers with approximately 5.1 million connections including 4.5 million postpaid, 0.5 million prepaid and 0.1 million reseller and other connections
- ◆ Operates in 22 states
- ◆ Employs approximately 5,700 associates
- ◆ 6,478 cell sites including 4,105 owned towers in service

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U.S. Cellular Mission and Strategy

U.S. Cellular's mission is to provide exceptional wireless communication services which enhance consumers' lives, increase the competitiveness of local businesses, and improve the efficiency of government operations in the mid-sized and rural markets served.

In 2018, U.S. Cellular continues to execute on its strategies to protect its current customer base, grow revenues, drive improvements in the overall cost structure, and invest in its network and online platforms. Strategic efforts include:

- ◆ U.S. Cellular continues to offer economical and competitively priced service plans and devices to its customers, and is focused on increasing revenues from sales of related products such as accessories and device protection plans and from new services such as fixed wireless broadband. In addition, U.S. Cellular is focused on expanding its solutions available to business and government customers, including a growing suite of connected machine-to-machine solutions and software applications across various categories.
- ◆ U.S. Cellular continues to devote efforts to enhance its network capabilities. To date, VoLTE technology has been launched successfully in California, Iowa, Oregon, Washington and Wisconsin, and deployments in several additional operating markets will occur later this year. VoLTE technology allows customers to utilize a 4G LTE network for both voice and data services, and offers enhanced services such as high definition voice and simultaneous voice and data sessions. In addition, the deployment of VoLTE technology expands U.S. Cellular's ability to offer roaming services to other wireless carriers.
- ◆ U.S. Cellular is committed to continuous technology innovation as demonstrated by its ongoing evaluation of 5G technology. U.S. Cellular has successfully tested 5G technology in both indoor and outdoor environments and is currently engaged in efforts related to the development of 5G standards and identifying potential use cases for the technology. When deployed commercially, 5G technology is expected to help address customers' growing demand for data services as well as create opportunities for new services requiring high speed and reliability as well as low latency.
- ◆ U.S. Cellular assesses its existing wireless interests on an ongoing basis with a goal of improving the competitiveness of its operations and maximizing its long-term return on capital. As part of this strategy, U.S. Cellular actively seeks attractive opportunities to acquire wireless spectrum, including pursuant to FCC auctions.

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Terms Used by U.S. Cellular

The following is a list of definitions of certain industry terms that are used throughout this document:

- ◆ 4G LTE – fourth generation Long-Term Evolution which is a wireless broadband technology.
- ◆ 5G – fifth generation wireless broadband technology.
- ◆ Account – represents an individual or business financially responsible for one or multiple associated connections. An account may include a variety of types of connections such as handsets and connected devices.
- ◆ Auctions 1000, 1001, and 1002 – Auction 1000 is an FCC auction of 600 MHz spectrum licenses that started in 2016 and concluded in 2017 involving: (1) a “reverse auction” in which broadcast television licensees submitted bids to voluntarily relinquish spectrum usage rights in exchange for payments (referred to as Auction 1001); (2) a “repacking” of the broadcast television bands in order to free up certain broadcast spectrum for other uses; and (3) a “forward auction” of licenses for spectrum cleared through this process to be used for wireless communications (referred to as Auction 1002).
- ◆ ASU 2014-09 – the Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2014-09, Revenue from Contracts with Customers, including any subsequent modifications to such guidance. This ASU replaces existing revenue recognition rules with a single comprehensive model to use in accounting for revenue arising from contracts with customers.
- ◆ Churn Rate – represents the percentage of the connections that disconnect service each month. These rates represent the average monthly churn rate for each respective period.
- ◆ Connections – individual lines of service associated with each device activated by a customer. Connections include all types of devices that connect directly to the U.S. Cellular network.
- ◆ Connected Devices – non-handset devices that connect directly to the U.S. Cellular network. Connected devices include products such as tablets, watches, modems, and hotspots.
- ◆ EBITDA – refers to earnings before interest, taxes, depreciation, amortization and accretion and is used in the non-GAAP metric Adjusted EBITDA throughout this document. See Supplemental Information Relating to Non-GAAP Financial Measures within this MD&A for additional information.
- ◆ Eligible Telecommunications Carrier (ETC) – designation by states for providing specified services in “high cost” areas which enables participation in universal service support mechanisms.
- ◆ Free Cash Flow – non-GAAP metric defined as Cash flows from operating activities less Cash paid for additions to property, plant and equipment.
- ◆ Gross Additions – represents the total number of new connections added during the period, without regard to connections that were terminated during that period.
- ◆ Machine-to-Machine or M2M – technology that involves the transmission of data between networked devices, as well as the performance of actions by devices without human intervention. U.S. Cellular sells and supports M2M solutions to customers, provides connectivity for M2M solutions via the U.S. Cellular network, and has agreements with device manufacturers and software developers which offer M2M solutions.
- ◆ Net Additions – represents the total number of new connections added during the period, net of connections that were terminated during that period.
- ◆ OIBDA – refers to operating income before depreciation, amortization and accretion and is used in the non-GAAP metric Adjusted OIBDA throughout this document. See Supplemental Information Relating to Non-GAAP Financial Measures within this MD&A for additional information.
- ◆ Postpaid Average Billings per Account (Postpaid ABPA) – non-GAAP metric which is calculated by dividing total postpaid service revenues plus equipment installment plan billings by the average number of postpaid accounts and by the number of months in the period.

- ◆ Postpaid Average Billings per User (Postpaid ABPU) – non-GAAP metric which is calculated by dividing total postpaid service revenues plus equipment installment plan billings by the average number of postpaid connections and by the number of months in the period.
- ◆ Postpaid Average Revenue per Account (Postpaid ARPA) – metric which is calculated by dividing total postpaid service revenues by the average number of postpaid accounts and by the number of months in the period.
- ◆ Postpaid Average Revenue per User (Postpaid ARPU) – metric which is calculated by dividing total postpaid service revenues by the average number of postpaid connections and by the number of months in the period.
- ◆ Retail Connections – the sum of postpaid connections and prepaid connections.
- ◆ Tax Act – refers to comprehensive federal tax legislation enacted on December 22, 2017, which made broad and complex changes to the U.S. tax code. Now titled H.R.1, the Tax Act was originally identified as the Tax Cuts and Jobs Act of 2017.
- ◆ Universal Service Fund (USF) – a system of telecommunications collected fees and support payments managed by the FCC intended to promote universal access to telecommunications services in the United States.
- ◆ VoLTE – Voice over Long-Term Evolution is a technology specification that defines the standards and procedures for delivering voice communications and related services over 4G LTE networks.

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Operational Overview

As of June 30, Retail Connections – End of Period			2018	2017
Postpaid			4,468,000	4,478,000
Prepaid			527,000	484,000
Total			4,995,000	4,962,000
	Q2 2018	Q2 2017	YTD 2018	YTD 2017
Postpaid Activity:				
Gross Additions	146,000	174,000	275,000	320,000
Net Additions (Losses)	(13,000)	23,000	(50,000)	(4,000)
Churn	1.19%	1.13%	1.21%	1.21%

The decrease in postpaid net additions for the three months ended June 30, 2018, when compared to the same period last year, was driven mainly by both lower handset and tablet gross additions as well as an increase in tablet churn. The decline in tablet gross additions reflects U.S. Cellular's decision to curtail promotions of heavily discounted tablets.

The increase in postpaid net losses for the six months ended June 30, 2018, when compared to the same period last year, was driven mainly by lower tablet gross additions and higher tablet churn.

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Postpaid Revenue

	Three Months Ended June 30, 2018		Six Months Ended June 30, 2017	
Average Revenue Per User (ARPU)	\$44.74	\$44.60	\$44.54	\$45.00
Average Billings Per User (ABPU) ¹	\$57.75	\$55.19	\$57.42	\$55.49
Average Revenue Per Account (ARPA)	\$118.57	\$119.73	\$118.38	\$120.46
Average Billings Per Account (ABPA) ¹	\$153.03	\$148.15	\$152.63	\$148.54

¹ Postpaid ABPU and Postpaid ABPA are non-GAAP financial measures. Refer to Supplemental Information Relating to Non-GAAP Financial Measures within this MD&A for a reconciliation of these measures.

On January 1, 2018, U.S. Cellular adopted the provisions of ASU 2014-09, using a modified retrospective method. Under this method, the new accounting standard is applied only to the most recent period presented, recognizing the cumulative effect of the accounting change as an adjustment to retained earnings at January 1, 2018. See Note 2 — Revenue Recognition in the Notes to Consolidated Financial Statements for additional details.

Postpaid ARPU increased for the three months ended June 30, 2018, when compared to the same period last year, driven by increases in device protection plan and regulatory recovery revenues. Such factors were partially offset by the impact of adopting the provisions of ASU 2014-09. Postpaid ARPA decreased for the three months ended June 30, 2018, when compared to the same period last year, due primarily to a decrease in postpaid connections per account driven by higher tablet churn. Application of the new accounting standard had the impact of reducing ARPU and ARPA for the three months ended June 30, 2018, by \$0.41 and \$1.07, respectively.

Postpaid ARPU and Postpaid ARPA decreased for the six months ended June 30, 2018, when compared to the same periods last year, due primarily to the impact of adopting the provisions of ASU 2014-09, as well as the impact of overall price reductions on plan offerings. Such factors were partially offset by the increases in device protection plan and regulatory recovery revenues. Application of the new accounting standard had the impact of reducing ARPU and ARPA for the six months ended June 30, 2018, by \$0.47 and \$1.24, respectively.

Under equipment installment plans, customers pay for their wireless devices in installments over a period of time. In order to show the trend in estimated cash collections from postpaid customer billings for both service and equipment, U.S. Cellular has presented Postpaid ABPU and Postpaid ABPA, which are calculated as Postpaid ARPU and Postpaid ARPA plus average monthly equipment installment plan billings per connection and account, respectively.

Postpaid ABPU and ABPA increased for the three and six months ended June 30, 2018, due primarily to an increase in equipment installment plan billings driven primarily by increased penetration of equipment installment plans.

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Financial Overview

	Three Months Ended June 30,			Six Months Ended June 30,		
	2018 ¹	2017	2018 vs. 2017	2018 ¹	2017	2018 vs. 2017
(Dollars in millions)						
Retail service	\$ 652	\$ 647	1%	\$ 1,301	\$ 1,304	–
Inbound roaming	39	31	26%	66	58	15%
Other	50	62	(20)%	98	124	(22)%
Service revenues	741	740	–	1,465	1,486	(1)%
Equipment sales	233	223	5%	450	413	9%
Total operating revenues	974	963	1%	1,915	1,899	1%
System operations (excluding depreciation, amortization and accretion reported below)						
Cost of equipment sold	240	260	(8)%	459	488	(6)%
Selling, general and administrative	342	351	(2)%	668	691	(3)%
Depreciation, amortization and accretion	159	155	3%	317	307	3%
(Gain) loss on asset disposals, net	1	5	(84)%	2	9	(75)%
(Gain) loss on license sales and exchanges, net	(11)	(2)	>(100)%	(17)	(19)	8%
Total operating	918	958	(4)%	1,794	1,840	(2)%

expenses

Operating income	\$ 56	\$ 5	>100%	\$ 121	\$ 59	>100%
Net income	\$ 52	\$ 12	>100%	\$ 107	\$ 40	>100%
Adjusted OIBDA (Non-GAAP) ²	\$ 205	\$ 163	26%	\$ 423	\$ 356	19%
Adjusted EBITDA (Non-GAAP) ²	\$ 248	\$ 198	25%	\$ 507	\$ 426	19%
Capital expenditures	\$ 86	\$ 84	2%	\$ 155	\$ 145	7%

As of January 1, 2018, U.S. Cellular adopted ASU 2014-09 using a modified retrospective approach. Under this method, the new accounting standard is applied only to the most recent period presented. See Note 2 — Revenue Recognition in the Notes to Consolidated Financial Statements for additional information.

1

Refer to Supplemental Information Relating to Non-GAAP Financial Measures within this MD&A for a reconciliation of this measure.

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Service revenues consist of:

- ◆ Retail Service – Charges for access, airtime, recovery of regulatory costs and value added services, including data services and products

- ◆ Inbound Roaming – Charges to other wireless carriers whose customers use U.S. Cellular’s wireless systems when roaming

- ◆ Other Service – Amounts received from the Federal USF and tower rental revenues. Imputed interest on equipment installment plan contracts is included in 2017; however, it is not included in 2018 due to the impact of adopting the provisions of ASU 2014-09

Equipment revenues consist of:

- ◆ Sales of wireless devices and related accessories to new and existing customers, agents, and third-party distributors

Key components of changes in the statement of operations line items were as follows:

Total operating revenues

Retail service revenues increased for the three months ended June 30, 2018, and decreased for the six months ended June 30, 2018, as a result of the changes in Postpaid ARPU as previously discussed in the Operational Overview section.

Inbound roaming revenues increased for the three and six months ended June 30, 2018, primarily driven by higher data roaming usage.

Other service revenues decreased for the three and six months ended June 30, 2018, reflecting the exclusion of imputed interest income in 2018 due to the impact of adopting the provisions of ASU 2014-09. Federal USF revenues remained flat at \$23 million and \$46 million for the three and six months ended June 30, 2018. See the Regulatory Matters section in this MD&A for a description of the FCC Mobility Fund II Order (MF2 Order) and its expected impacts on U.S. Cellular's current Federal USF support.

Equipment sales revenues increased for the three and six months ended June 30, 2018, due to the impact of adopting the provisions of ASU 2014-09, an increase in the average revenue per device sold, a mix shift from feature phones and connected devices to higher end smartphone devices, and an increase in accessories revenue. Such factors were partially offset by a decrease in the number of devices sold and a reduction in guarantee liability amortization for equipment installment contracts as a result of changes in plan offerings.

See Note 2 — Revenue Recognition in the Notes to Consolidated Financial Statements for additional details on the financial statement impact of ASU 2014-09.

Cost of equipment sold

Cost of equipment sold decreased for the three and six months ended June 30, 2018, due primarily to a decrease in the number of devices sold, as well as the impact of adopting the provisions of ASU 2014-09. Such factors were partially offset by increases due to a higher average cost per device sold, an increase in accessories cost, and a mix shift from feature phones and connected devices to higher cost smartphones.

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Selling, general and administrative expenses

Selling, general and administrative expenses decreased by \$9 million and \$23 million for the three and six months ended June 30, 2018, respectively, due to lower commissions, advertising and bad debts expenses.

Depreciation, amortization and accretion

Depreciation, amortization, and accretion increased for the three and six months ended June 30, 2018, due primarily to an increase in amortization expense related to billing system upgrades.

(Gain) loss on asset disposals, net

Loss on asset disposals, net decreased primarily as a result of fewer disposals of certain network assets.

(Gain) loss on license sales and exchanges, net

Net gains in 2018 and 2017 were due to gains recognized on license sale and exchange transactions with various third parties.

Components of
Other Income
(Expense)

	Three Months Ended			Six Months Ended		
	June 30,		2018 vs. 2017	June 30,		2018 vs. 2017
	2018 ¹	2017		2018 ¹	2017	
(Dollars in millions)						
Operating income	\$56	\$5	>100%	\$121	\$59	>100%
Equity in earnings of unconsolidated entities	40	33	20%	78	66	18%
Interest and dividend income	3	2	63%	7	5	45%
Interest expense	(29)	(28)	(2)%	(58)	(56)	(3)%
Other, net	–	–	>100%	(1)	(1)	14%
	14	7	>100%	26	14	85%

Total
investment and
other income

Income before income taxes	70	12	>100%	147	73	>100%
Income tax expense (benefit)	18	–	>100%	40	33	21%
Net income	52	12	>100%	107	40	>100%
Less: Net income attributable to noncontrolling interests, net of tax	3	–	>100%	14	2	>100%
Net income attributable to U.S. Cellular	\$49	\$12	>100%	\$93	\$38	>100%

shareholders

1 As of January 1, 2018, U.S. Cellular adopted ASU 2014-09 using a modified retrospective approach. Under this method, the new accounting standard is applied only to the most recent period presented. See Note 2 — Revenue Recognition in the Notes to Consolidated Financial Statements for additional information.

Equity in earnings of unconsolidated entities

Equity in earnings of unconsolidated entities represents U.S. Cellular's share of net income from entities in which it has a noncontrolling interest and that are accounted for by the equity method. U.S. Cellular's investment in the Los Angeles SMSA Limited Partnership (LA Partnership) contributed \$20 million and \$17 million in earnings of unconsolidated entities for the three months ended June 30, 2018 and 2017, respectively, and \$38 million and \$33 million for the six months ended June 30, 2018 and 2017, respectively. See Note 8 — Investments in Unconsolidated Entities in the Notes to Consolidated Financial Statements for additional information.

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Income tax expense

The effective tax rate on Income before income taxes for the three and six months ended June 30, 2018, was 26.1% and 27.5%, respectively. The effective tax rate for the three and six months ended June 30, 2017, was 2.7% and 45.6% respectively. The lower rate for the six months ended June 30, 2018, as compared to the six months ended June 30, 2017, is due primarily to the reduction of the U.S. federal corporate tax rate from 35% to 21% as a result of the Tax Act enacted in December 2017. The effective rate for the three months ended June 30, 2017 was not meaningful due primarily to the relatively low pretax income for the quarter combined with adjustments to the estimated annual tax rate, resulting in a distortive impact on the tax rate for the quarter. Due to difficulty in reliably projecting an annual tax rate, U.S. Cellular calculated income taxes for the six months ended June 30, 2017, based on an estimated year-to-date rate.

The bonus depreciation provision of the Tax Act is expected to substantially reduce U.S. Cellular's current federal income tax liability in 2018. See Note 5 — Income Taxes in the Notes to Consolidated Financial Statements for additional information related to income taxes.

Net income attributable to noncontrolling interests, net of tax

Net income attributable to noncontrolling interests, net of tax increased during the six months ended June 30, 2018, due primarily to an out-of-period adjustment recorded in the first quarter of 2018. U.S. Cellular determined that this adjustment was not material to any of the periods impacted. See Note 10 — Variable Interest Entities in the Notes to Consolidated Financial Statements for additional information.

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Liquidity and Capital Resources

Sources of Liquidity

U.S. Cellular operates a capital-intensive business. Historically, U.S. Cellular has used internally-generated funds and also has obtained substantial funds from external sources for general corporate purposes. In the past, U.S. Cellular's existing cash and investment balances, funds available under its revolving credit agreement, funds from other financing sources, including a term loan and other long-term debt, and cash flows from operating, certain investing and financing activities, including sales of assets or businesses, provided sufficient liquidity and financial flexibility for U.S. Cellular to meet its normal day-to-day operating needs and debt service requirements, to finance the build-out and enhancement of markets and to fund acquisitions, primarily of spectrum licenses. There is no assurance that this will be the case in the future. See Market Risk for additional information regarding maturities of long-term debt.

Although U.S. Cellular currently has a significant cash balance, U.S. Cellular has incurred negative free cash flow at times in the past and this could occur in the future. However, U.S. Cellular believes that existing cash and investment balances, funds available under its revolving credit agreement, receivables securitization agreement and expected cash flows from operating and investing activities will provide sufficient liquidity for U.S. Cellular to meet its normal day-to-day operating needs and debt service requirements for the coming year.

U.S. Cellular may require substantial additional capital for, among other uses, funding day-to-day operating needs including working capital, acquisitions of providers of wireless telecommunications services, spectrum license or system acquisitions, system development and network capacity expansion, debt service requirements, the repurchase of shares, the payment of dividends, or making additional investments. It may be necessary from time to time to increase the size of the existing revolving credit agreement, to put in place a new credit agreement, or to obtain other forms of financing in order to fund potential expenditures. U.S. Cellular's liquidity would be adversely affected if, among other things, U.S. Cellular is unable to obtain short or long-term financing on acceptable terms, U.S. Cellular makes significant spectrum license purchases, the LA Partnership discontinues or reduces distributions compared to historical levels, or Federal USF and/or other regulatory support payments decline. In addition, although sales of assets or businesses by U.S. Cellular have been an important source of liquidity in prior periods, U.S. Cellular does not expect a similar level of such sales in the future.

U.S. Cellular's credit rating currently is sub-investment grade. There can be no assurance that sufficient funds will continue to be available to U.S. Cellular or its subsidiaries on terms or at prices acceptable to U.S. Cellular. Insufficient cash flows from operating activities, changes in its credit ratings, defaults of the terms of debt or credit agreements, uncertainty of access to capital, deterioration in the capital markets, reduced regulatory capital at banks which in turn limits their ability to borrow and lend, other changes in the performance of U.S. Cellular or in market conditions or other factors could limit or restrict the availability of financing on terms and prices acceptable to U.S. Cellular, which could require U.S. Cellular to reduce its acquisition, capital expenditure and business development programs, reduce the acquisition of spectrum licenses, and/or reduce or cease share repurchases and/or the payment of dividends. U.S. Cellular cannot provide assurance that circumstances that could have a material adverse effect on its liquidity or capital resources will not occur. Any of the foregoing would have an adverse impact on U.S. Cellular's businesses, financial condition or results of operations.

Cash and Cash Equivalents

Cash and cash equivalents include cash and money market investments. The primary objective of U.S. Cellular's Cash and cash equivalents is for use in its operations and acquisition, capital expenditure and business development programs.

At June 30, 2018, U.S. Cellular's Cash and cash equivalents totaled \$596 million compared to \$352 million at December 31, 2017.

The majority of U.S. Cellular's Cash and cash equivalents was held in bank deposit accounts and in money market funds that purchase only debt issued by the U.S. Treasury or U.S. government agencies across a range of eligible money market investments that may include, but are not limited to, government agency repurchase agreements, government agency debt, U.S. Treasury repurchase agreements, U.S. Treasury debt, and other securities collateralized by U.S. government obligations. U.S. Cellular monitors the financial viability of the money market funds and direct investments in which it invests and believes that the credit risk associated with these investments is low.

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Financing

In May 2018, U.S. Cellular entered into a new \$300 million revolving credit agreement with certain lenders and other parties. Amounts under the new revolving credit agreement are available for general corporate purposes, including spectrum purchases and capital expenditures, and may be borrowed, repaid and reborrowed from time to time until maturity in May 2023. As a result of the new agreement, U.S. Cellular's previous revolving credit agreement due to expire in June 2021 was terminated. As of June 30, 2018, there were no outstanding borrowings under the revolving credit agreement, except for letters of credit, and the unused borrowing capacity was \$298 million. See Note 9 — Debt in the Notes to Consolidated Financial Statements for additional information.

In May 2018, U.S. Cellular also amended its senior term loan credit agreement in order to align with the new revolving credit agreement. There were no significant changes to the maturity date or other key terms of the agreement.

U.S. Cellular believes it was in compliance with all of the financial covenants and requirements set forth in its revolving credit agreement and the senior term loan credit agreement as of June 30, 2018.

U.S. Cellular, through its subsidiaries, also has a receivables securitization agreement to permit securitized borrowings using its equipment installment plan receivables for general corporate purposes. The unused capacity under this agreement was \$200 million as of June 30, 2018, subject to sufficient collateral to satisfy the asset borrowing base provisions of the agreement. As of June 30, 2018, the USCC Master Note Trust (Trust) held \$27 million of assets available to be pledged as collateral for the receivables securitization agreement. U.S. Cellular believes it was in compliance with all of the financial covenants and requirements set forth in its receivables securitization agreement as of that date.

U.S. Cellular has in place an effective shelf registration statement on Form S-3 to issue senior or subordinated debt securities.

Long-term debt payments due for the remainder of 2018 and the next four years are \$214 million, which represent 13% of the total gross long-term debt obligation at June 30, 2018.

Capital Expenditures

Capital expenditures (i.e., additions to property, plant and equipment and system development expenditures), which include the effects of accruals and capitalized interest, for the six months ended June 30, 2018 and 2017, were as follows:

U.S. Cellular's capital expenditures for the six months ended June 30, 2018 and 2017, were \$155 million and \$145 million, respectively.

Capital expenditures for the full year 2018 are expected to be between \$500 million and \$550 million. These expenditures are expected to be used principally for the following purposes:

- ◆ Enhance network coverage by continuing to deploy VoLTE technology in certain markets and providing additional capacity to accommodate increased network usage, principally data usage, by current customers; and
- ◆ Invest in and replace end of life platforms.

U.S. Cellular plans to finance its capital expenditures program for 2018 using primarily Cash flows from operating activities, existing cash balances and, if required, its receivables securitization and/or revolving credit agreements.

Acquisitions, Divestitures and Exchanges

U.S. Cellular may be engaged from time to time in negotiations (subject to all applicable regulations) relating to the acquisition, divestiture or exchange of companies, properties or wireless spectrum. In general, U.S. Cellular may not disclose such transactions until there is a definitive agreement. U.S. Cellular assesses its existing wireless interests on an ongoing basis with a goal of improving the competitiveness of its operations and maximizing its long-term return on capital. As part of this strategy, U.S. Cellular actively seeks attractive opportunities to acquire wireless spectrum, including pursuant to FCC auctions. U.S. Cellular also may seek to divest outright or include in exchanges for other wireless interests those interests that are not strategic to its long-term success.

Variable Interest Entities

U.S. Cellular consolidates certain “variable interest entities” as defined under GAAP. See Note 10 — Variable Interest Entities in the Notes to Consolidated Financial Statements for additional information related to these variable interest entities. U.S. Cellular may elect to make additional capital contributions and/or advances to these variable interest entities in future periods in order to fund their operations.

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Common Share Repurchase Program

U.S. Cellular has repurchased and expects to continue to repurchase its Common Shares, subject to its repurchase program. However, there were no share repurchases made under this program in the six months ended June 30, 2018, or in the year ended December 31, 2017.

As of June 30, 2018, the total cumulative amount of U.S. Cellular Common Shares authorized to be purchased is 5,900,849. For additional information related to the current repurchase authorization, see Unregistered Sales of Equity Securities and Use of Proceeds.

Contractual and Other Obligations

There were no material changes outside the ordinary course of business between December 31, 2017 and June 30, 2018, to the Contractual and Other Obligations disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations included in U.S. Cellular's Form 10-K for the year ended December 31, 2017.

Off-Balance Sheet Arrangements

U.S. Cellular had no transactions, agreements or other contractual arrangements with unconsolidated entities involving "off-balance sheet arrangements," as defined by SEC rules, that had or are reasonably likely to have a material current or future effect on its financial condition, results of operations, liquidity, capital expenditures or capital resources.

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Consolidated Cash Flow Analysis

U.S. Cellular operates a capital- and marketing-intensive business. U.S. Cellular makes substantial investments to acquire wireless licenses and properties and to construct and upgrade wireless telecommunications networks and facilities as a basis for creating long-term value for shareholders. In recent years, rapid changes in technology and new opportunities have required substantial investments in potentially revenue enhancing and cost-reducing upgrades to U.S. Cellular's networks. U.S. Cellular utilizes cash on hand, cash from operating activities, cash proceeds from divestitures and dispositions of investments, and short-term and long-term debt financing to fund its acquisitions (including spectrum licenses), construction costs, operating expenses and share repurchases. Cash flows may fluctuate from quarter to quarter and year to year due to seasonality, the timing of acquisitions and divestitures, capital expenditures and other factors. The following discussion summarizes U.S. Cellular's cash flow activities for the six months ended June 30, 2018 and 2017.

2018 Commentary

U.S. Cellular's Cash, cash equivalents and restricted cash increased \$245 million in 2018. Net cash provided by operating activities was \$365 million in 2018 due to net income of \$107 million plus non-cash items of \$292 million and distributions received from unconsolidated entities of \$70 million, including \$33 million in distributions from the LA Partnership. This was partially offset by changes in working capital items which decreased net cash by \$104 million. The working capital changes were primarily influenced by an increase in equipment installment plan receivables and the timing of annual employee bonus payments and vendor and tax payments, partially offset by collections of customer and agent receivables. The adoption of ASU 2014-09 caused fluctuations in working capital items in the Consolidated Balance Sheet; however, it did not have an impact on total Net cash provided by operating activities.

Cash flows used for investing activities were \$101 million. Cash paid in 2018 for additions to property, plant and equipment totaled \$173 million. This was partially offset by Cash received from the redemption of short-term Treasury bills of \$50 million and Cash received from divestitures and exchanges of \$21 million.

Cash flows used for financing activities were \$19 million, reflecting ordinary activity such as the scheduled repayments of debt.

2017 Commentary

U.S. Cellular's Cash, cash equivalents and restricted cash decreased \$114 million in 2017. Net cash provided by operating activities was \$220 million in 2017, due to net income of \$40 million plus non-cash items of \$266 million and distributions received from unconsolidated entities of \$65 million, including \$30 million in distributions from the LA Partnership. This was partially offset by changes in working capital items which decreased cash by \$151 million. The working capital changes were due to a \$107 million increase in equipment installment plan receivables and a \$53 million decrease in accounts payable.

The net cash provided by operating activities was offset by Cash flows used for investing activities of \$327 million. Cash paid for additions to property, plant and equipment in 2017 totaled \$155 million. Cash paid for acquisitions and licenses was \$189 million which included the remaining \$186 million due to the FCC for licenses U.S. Cellular won in Auction 1002. This was partially offset by Cash received from divestitures and exchanges of \$17 million.

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Consolidated Balance Sheet Analysis

The following discussion addresses certain captions in the consolidated balance sheet and changes therein. This discussion is intended to highlight the significant changes and is not intended to fully reconcile the changes. Changes in financial condition during 2018 were as follows:

Cash and cash equivalents

See the Consolidated Cash Flow Analysis above for a discussion of cash and cash equivalents.

Short-term investments

Short-term investments decreased \$50 million due to the maturity of U.S. Treasury Bills with original maturities of six months.

Other assets and deferred charges

Other assets and deferred charges increased \$146 million due primarily to the creation of contract assets and contract cost assets as a result of the adoption of ASU 2014-09. See Note 2 — Revenue Recognition in the Notes to Consolidated Financial Statements for additional information.

Accounts payable — Trade

Accounts payable – Trade decreased \$61 million due primarily to reduction of expenses as well as payment timing differences.

Customer deposits and deferred revenues

Customer deposits and deferred revenues decreased \$58 million due primarily to the reclassification of certain deferred revenues to Other current assets to reflect the net contract position for each customer contract on the Consolidated Balance Sheet as required by ASU 2014-09, which was adopted on January 1, 2018. See Note 2 — Revenue Recognition in the Notes to Consolidated Financial Statements for additional information.

Accrued compensation

Accrued compensation decreased \$26 million due primarily to employee bonus payments in March 2018.

Deferred income tax liability, net

Deferred income tax liability, net, increased \$61 million due primarily to the adoption of ASU 2014-09 increasing the net basis of assets on a U.S. GAAP basis without a corresponding increase in tax basis, as well as the impact of full expensing of qualified property additions following the enactment of the Tax Act.

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Supplemental Information Relating to Non-GAAP Financial Measures

U.S. Cellular sometimes uses information derived from consolidated financial information but not presented in its financial statements prepared in accordance with U.S. GAAP to evaluate the performance of its business. Certain of these measures are considered “non-GAAP financial measures” under U.S. Securities and Exchange Commission Rules. Specifically, U.S. Cellular has referred to the following measures in this Form 10-Q Report:

- ◆ EBITDA
- ◆ Adjusted EBITDA
- ◆ Adjusted OIBDA
- ◆ Free cash flow
- ◆ Postpaid ABPU

- ◆ Postpaid ABPA

Following are explanations of each of these measures.

EBITDA, Adjusted EBITDA and Adjusted OIBDA

EBITDA, Adjusted EBITDA and Adjusted OIBDA are defined as net income adjusted for the items set forth in the reconciliation below. EBITDA, Adjusted EBITDA and Adjusted OIBDA are not measures of financial performance under GAAP and should not be considered as alternatives to Net income or Cash flows from operating activities, as indicators of cash flows or as measures of liquidity. U.S. Cellular does not intend to imply that any such items set forth in the reconciliation below are non-recurring, infrequent or unusual; such items may occur in the future.

Management uses Adjusted EBITDA and Adjusted OIBDA as measurements of profitability and, therefore, reconciliations to Net income are deemed appropriate. Management believes Adjusted EBITDA and Adjusted OIBDA are useful measures of U.S. Cellular’s operating results before significant recurring non-cash charges, gains and losses, and other items as presented below as they provide additional relevant and useful information to investors and other users of U.S. Cellular’s financial data in evaluating the effectiveness of its operations and underlying business trends in a manner that is consistent with management’s evaluation of business performance. Adjusted EBITDA shows adjusted earnings before interest, taxes, depreciation, amortization and accretion, and gains and losses, while Adjusted OIBDA reduces this measure further to exclude Equity in earnings of unconsolidated entities and Interest and dividend income in order to more effectively show the performance of operating activities excluding investment activities. The following table reconciles EBITDA, Adjusted EBITDA and Adjusted OIBDA to the corresponding GAAP measure, Net income.

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