

TELEPHONE & DATA SYSTEMS INC /DE/  
Form 10-Q  
May 02, 2014

UNITED STATES																			
SECURITIES AND EXCHANGE COMMISSION																			
Washington, D.C. 20549																			
FORM 10-Q																			
<b>(Mark One)</b>																			
x	<b>QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934</b>																		
For the quarterly period ended March 31, 2014																			
OR																			
	<b>TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934</b>																		
For the transition period from to																			
Commission file number 001-14157																			
TELEPHONE AND DATA SYSTEMS, INC.																			
(Exact name of Registrant as specified in its charter)																			
Delaware										36-2669023									
(State or other jurisdiction of incorporation or organization)										(IRS Employer Identification No.)									
<b><u>30 North LaSalle Street, Suite 4000, Chicago, Illinois 60602</u></b>																			
(Address of principal executive offices) (Zip code)																			
Registrant's telephone number, including area code: (312) 630-1900																			
<b>Indicate by check mark</b>																		<b>Yes</b>	<b>No</b>
• 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	

• 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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).																	x		
• whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.																			
Large accelerated filer				x	Accelerated filer					Non-accelerated filer					Smaller reporting company				
• whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).																		x	
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.																			
<b>Class</b>										<b>Outstanding at March 31, 2014</b>									
Common Shares, \$0.01 par value										101,573,846 Shares									
Series A Common Shares, \$0.01 par value										7,175,948 Shares									

Telephone and Data Systems, Inc.			
Quarterly Report on Form 10-Q			
For the Quarterly Period Ended March 31, 2014			
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<b>Part I. Financial Information</b>								
<b>Item 1. Financial Statements</b>								
<b>Telephone and Data Systems, Inc.</b>								
<b><u>Consolidated Statement of Operations</u></b>								
<b><u>(Unaudited)</u></b>								
				<b>Three Months Ended</b>				
				<b>March 31,</b>				
<b>(Dollars and shares in thousands, except per share amounts)</b>				<b>2014</b>			<b>2013</b>	
<b>Operating revenues</b>								
	Service			\$	1,080,242		\$	1,198,902
	Equipment and product sales				115,720			109,671
		Total operating revenues			1,195,962			1,308,573
<b>Operating expenses</b>								
	Cost of services (excluding Depreciation, amortization and accretion reported below)				275,958			299,127
	Cost of equipment and products				306,647			260,765
	Selling, general and administrative				463,669			486,903
	Depreciation, amortization and accretion				224,919			242,077
	(Gain) loss on asset disposals, net				2,430			5,616
	(Gain) loss on sale of business and other exit costs, net				(6,900)			6,931
	(Gain) loss on license sales and exchanges				(91,446)			-
		Total operating expenses			1,175,277			1,301,419
<b>Operating income</b>					20,685			7,154
<b>Investment and other income (expense)</b>								
	Equity in earnings of unconsolidated entities				37,327			27,089
	Interest and dividend income				2,486			1,578
	Interest expense				(28,707)			(24,498)
	Other, net				160			(154)
		Total investment and other income			11,266			4,015
<b>Income before income taxes</b>					31,951			11,169
	Income tax expense				11,657			4,180
<b>Net income</b>					20,294			6,989

Less: Net income attributable to noncontrolling interests, net of tax		2,040			5,570
<b>Net income attributable to TDS shareholders</b>		18,254			1,419
TDS Preferred dividend requirement		(12)			(12)
<b>Net income available to common shareholders</b>	\$	18,242		\$	1,407
<b>Basic weighted average shares outstanding</b>		108,988			108,255
<b>Basic earnings per share attributable to TDS shareholders</b>	\$	0.17		\$	0.01
<b>Diluted weighted average shares outstanding</b>		109,672			108,693
<b>Diluted earnings per share attributable to TDS shareholders</b>	\$	0.16		\$	0.01
<b>Dividends per share to TDS shareholders</b>	\$	0.1340		\$	0.1275
The accompanying notes are an integral part of these consolidated financial statements.					

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Telephone and Data Systems, Inc.									
<u>Consolidated Statement of Comprehensive Income</u>									
<u>(Unaudited)</u>									
					Three Months Ended				
					March 31,				
(Dollars in thousands)					2014			2013	
Net income					\$	20,294		\$	6,989
Net change in accumulated other comprehensive income (loss)									
	Change in foreign currency translation adjustment					(4)			15
	Change related to retirement plan								
		Amounts included in net periodic benefit cost for the period							
			Amortization of prior service cost			(911)			(902)
			Amortization of unrecognized net loss			322			602
						(589)			(300)
			Change in deferred income taxes			224			114
		Change related to retirement plan, net of tax				(365)			(186)
	Net change in accumulated other comprehensive income (loss)					(369)			(171)
Comprehensive income						19,925			6,818
	Less: Comprehensive income attributable to noncontrolling interest					2,040			5,570
Comprehensive income attributable to TDS shareholders					\$	17,885		\$	1,248
The accompanying notes are an integral part of these consolidated financial statements.									

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<b><u>Telephone and Data Systems, Inc.</u></b>					
<b><u>Consolidated Statement of Cash Flows</u></b>					
<b><u>(Unaudited)</u></b>					
				<b>Three Months Ended</b>	
				<b>March 31,</b>	
<b>(Dollars in thousands)</b>				<b>2014</b>	<b>2013</b>
<b>Cash flows from operating activities</b>					
	Net income		\$	20,294	\$ 6,989
	Add (deduct) adjustments to reconcile net income to net cash flows from operating activities				
		Depreciation, amortization and accretion		224,919	242,077
		Bad debts expense		21,559	17,874
		Stock-based compensation expense		6,759	7,585
		Deferred income taxes, net		(14,510)	3,009
		Equity in earnings of unconsolidated entities		(37,327)	(27,089)
		Distributions from unconsolidated entities		12,820	8,089
		(Gain) loss on asset disposals, net		2,430	5,616
		(Gain) loss on sale of business and other exit costs, net		(6,900)	6,931
		(Gain) loss on license sales and exchanges		(91,446)	-
		Noncash interest expense		506	497
		Other operating activities		47	256
	<b>Changes in assets and liabilities from operations</b>				
		Accounts receivable		92,949	34,038
		Inventory		19,656	16,860
		Accounts payable		(53,403)	(3,203)
		Customer deposits and deferred revenues		(1,447)	7,904
		Accrued taxes		(1,634)	5,309
		Accrued interest		9,136	9,279
		Other assets and liabilities		(99,471)	(95,669)
				104,937	246,352
<b>Cash flows from investing activities</b>					
	Cash used for additions to property, plant and equipment			(150,890)	(176,318)
	Cash paid for acquisitions and licenses			(8,254)	(14,150)
	Cash received from divestitures			103,042	-
	Cash received for investments			10,000	-
	Other investing activities			1,623	6,364



						(44,479)			(184,104)
<b>Cash flows from financing activities</b>									
	Repayment of long-term debt					(392)			(328)
	TDS Common Shares reissued for benefit plans, net of tax payments					(50)			140
	U.S. Cellular Common Shares reissued for benefit plans, net of tax payments					316			123
	Repurchase of TDS Common Shares					(3,342)			-
	Repurchase of U.S. Cellular Common Shares					(2,000)			(18,425)
	Dividends paid to TDS shareholders					(14,582)			(13,792)
	Distributions to noncontrolling interests					(346)			(2,396)
	Other financing activities					2,834			(1,351)
						(17,562)			(36,029)
<b>Net increase in cash and cash equivalents</b>						42,896			26,219
<b>Cash and cash equivalents</b>									
	Beginning of period					830,014			740,481
	End of period				\$	872,910		\$	766,700
The accompanying notes are an integral part of these consolidated financial statements.									

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Telephone and Data Systems, Inc.					
<u>Consolidated Balance Sheet — Assets</u>					
<u>(Unaudited)</u>					
(Dollars in thousands)			March 31,		December 31,
			2014		2013
<b>Current assets</b>					
	Cash and cash equivalents		\$ 872,910	\$	830,014
	Short-term investments		40,056		50,104
	Accounts receivable				
	Due from customers and agents, less allowances of \$56,112 and \$63,690, respectively		424,451		551,611
	Other, less allowances of \$2,165 and \$1,914, respectively		190,558		179,503
	Inventory, net		224,904		244,560
	Net deferred income tax asset		106,077		106,077
	Prepaid expenses		89,344		87,920
	Income taxes receivable		5,679		2,397
	Other current assets		35,154		35,151
			1,989,133		2,087,337
<b>Assets held for sale</b>			-		16,027
<b>Investments</b>					
	Licenses		1,448,598		1,423,779
	Goodwill		836,843		836,843
	Franchise rights		123,668		123,668
	Other intangible assets, net of accumulated amortization of \$117,767 and \$112,752, respectively		66,439		71,454
	Investments in unconsolidated entities		326,279		301,772
	Other investments		611		641
			2,802,438		2,758,157
<b>Property, plant and equipment</b>					
	In service and under construction		11,253,631		11,239,804
	Less: Accumulated depreciation		7,474,498		7,361,660
			3,779,133		3,878,144
<b>Other assets and deferred charges</b>			178,599		164,482

<b>Total assets</b>				\$	8,749,303		\$	8,904,147
The accompanying notes are an integral part of these consolidated financial statements.								

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Telephone and Data Systems, Inc.					
<u>Consolidated Balance Sheet — Liabilities and Equity</u>					
<u>(Unaudited)</u>					
				March 31,	December 31,
(Dollars and shares in thousands)				2014	2013
<b>Current liabilities</b>					
	Current portion of long-term debt		\$	1,415	\$ 1,646
	Accounts payable			414,015	496,069
	Customer deposits and deferred revenues			287,999	289,445
	Accrued interest			15,757	6,673
	Accrued taxes			72,761	70,518
	Accrued compensation			65,486	115,031
	Other current liabilities			167,746	212,374
				1,025,179	1,191,756
<b>Deferred liabilities and credits</b>					
	Net deferred income tax liability			847,850	862,975
	Other deferred liabilities and credits			477,305	458,709
<b>Long-term debt</b>				1,720,031	1,720,074
<b>Commitments and contingencies</b>				-	-
<b>Noncontrolling interests with redemption features</b>				543	536
<b>Equity</b>					
	TDS shareholders' equity				
	Series A Common and Common Shares				
	Authorized 290,000 shares (25,000 Series A Common and 265,000 Common Shares)				
	Issued 132,721 shares (7,176 Series A Common and 125,545 Common Shares) and 132,711 shares (7,166 Series A Common and 125,545 Common Shares), respectively				
	Outstanding 108,750 shares (7,176 Series A Common and 101,574 Common Shares) and 108,757 shares (7,166 Series A Common and 101,591 Common Shares), respectively				
				1,327	1,327

		Par Value (\$.01 per share) of \$1,327 (\$72 Series A Common and \$1,255 Common Shares)					
		Capital in excess of par value		2,313,682			2,308,807
		Treasury shares at cost:					
		23,971 and 23,954 Common Shares, respectively		(722,658)			(721,354)
		Accumulated other comprehensive loss		(938)			(569)
		Retained earnings		2,533,298			2,529,626
		Total TDS shareholders' equity		4,124,711			4,117,837
		Preferred shares		824			824
		Noncontrolling interests		552,860			551,436
		Total equity		4,678,395			4,670,097
		<b>Total liabilities and equity</b>	\$	8,749,303		\$	8,904,147
The accompanying notes are an integral part of these consolidated financial statements.							

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Telephone and Data Systems, Inc.										
<u>Consolidated Statement of Changes in Equity</u>										
<u>(Unaudited)</u>										
TDS Shareholders										
(Dollars and in thousands)	Series A Common Shares	Capital in Excess of Par Value	Treasury Common Shares	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total TDS Shareholders' Equity	Preferred Shares	Non controlling Interests	Total Equity	
December 31, 2013	\$ 1,327	\$ 2,308,807	\$ (721,354)	\$ (569)	\$ 2,529,626	\$ 4,117,837	\$ 824	\$ 551,436	\$ 4,670,097	
Add (Deduct)										
Net income attributable to TDS shareholders	-	-	-	-	18,254	18,254	-	-	18,254	
Net income attributable to noncontrolling interests										
classified as equity	-	-	-	-	-	-	-	2,011	2,011	
Change in foreign currency	-	-	-	(4)	-	(4)	-	-	(4)	

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Telephone and Data Systems, Inc.											
<u>Consolidated Statement of Changes in Equity</u>											
<u>(Unaudited)</u>											
TDS Shareholders											
(Dollars and in thousands)	Series A Common Shares	Capital in Excess of Par Value	Treasury Common Shares	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total TDS Shareholders' Equity	Preferred Shares	Non controlling Interests	Total Equity		
December 31, 2012	\$ 1,327	\$ 2,304,122	\$ (750,099)	\$ (8,132)	\$ 2,464,318	\$ 4,011,536	\$ 825	\$ 643,966	\$ 4,656,327		
Add (Deduct)											
Net income attributable to TDS shareholders	-	-	-	-	1,419	1,419	-	-	1,419		
Net income attributable to noncontrolling interests											
classified as equity	-	-	-	-	-	-	-	5,597	5,597		
Change in foreign currency	-	-	-	15	-	15	-	-	15		



Stock-based compensation awards	-	2,395	-	-	-	2,395	-	-	2,395
Tax windfall (shortfall) from stock awards	-	(532)	-	-	-	(532)	-	-	(532)
Distributions to noncontrolling interests	-	-	-	-	-	-	-	(2,396)	(2,396)
Adjust investment in subsidiaries for noncontrolling interest purchases	-	(10,295)	-	-	-	(10,295)	-	5,299	(4,996)
<b>March 31, 2013</b>	<b>\$ 1,327</b>	<b>\$ 2,302,785</b>	<b>\$ (747,831)</b>	<b>\$ (8,303)</b>	<b>\$ 2,449,720</b>	<b>\$ 3,997,698</b>	<b>\$ 825</b>	<b>\$ 632,457</b>	<b>\$ 4,630,980</b>
The accompanying notes are an integral part of these consolidated financial statements.									

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**Telephone and Data Systems, Inc.**

**Notes to Consolidated Financial Statements**

**1. Basis of Presentation**

The accounting policies of Telephone and Data Systems, Inc. (“TDS”) conform to accounting principles generally accepted in the United States of America (“GAAP”) as set forth in the Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”). The consolidated financial statements include the accounts of TDS and its majority-owned subsidiaries, including TDS’ 84%-owned wireless telephone subsidiary, United States Cellular Corporation (“U.S. Cellular”) and TDS’ wholly-owned subsidiary, TDS Telecommunications Corporation (“TDS Telecom”). In addition, the consolidated financial statements include certain entities in which TDS has a variable interest that require consolidation under GAAP. All material intercompany accounts and transactions have been eliminated.

The consolidated financial statements included herein have been prepared by TDS, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. However, TDS believes that the disclosures included herein are adequate to make the information presented not misleading. These consolidated financial statements should be read in conjunction with the consolidated financial statements and the notes thereto included in TDS’ Annual Report on Form 10-K (“Form 10-K”) for the year ended December 31, 2013.

TDS’ business segments reflected in this Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2014 are U.S. Cellular, TDS Telecom’s Wireline, Cable and Hosted and Managed Services (“HMS”) operations, and the Non-Reportable Segment which includes TDS’ majority-owned printing and distribution company, Suttle-Straus, Inc. (“Suttle-Straus”) and TDS’ wholly-owned wireless telephone subsidiary, Airadigm Communications, Inc. (“Airadigm”). Periods presented for comparative purposes have been re-presented to conform to this segment presentation. All of TDS’ segments operate only in the United States, except for HMS, which includes an insignificant foreign operation. See Note 11 — Business Segment Information for summary financial information on each business segment.

The accompanying unaudited consolidated financial statements contain all adjustments (consisting of only normal recurring items, unless otherwise disclosed) necessary for a fair statement of the financial position as of March 31, 2014 and December 31, 2013, and the results of operations, changes in comprehensive income, cash flows and equity for the three months ended March 31, 2014 and 2013. These results are not necessarily indicative of the results to be expected for the full year.

#### Recently Issued Accounting Pronouncements

On April 10, 2014, the FASB issued Accounting Standards Update 2014-08, *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity* ("ASU 2014-08"). ASU 2014-08 changes the requirements and disclosures for reporting discontinued operations. TDS is required to adopt the provisions of ASU 2014-08 effective January 1, 2015, although early adoption is permitted. The adoption of ASU 2014-08 is not expected to have a significant impact on TDS' financial position or results of operations.

#### Reclassifications

Certain prior year amounts have been reclassified to conform to the 2014 financial statement presentation. These reclassifications did not affect consolidated net income attributable to TDS shareholders, cash flows, assets, liabilities or equity for the years presented.

In 2014, TDS began displaying separately Equipment and product sales and Cost of equipment and products. As a result of recent HMS acquisitions, these amounts are now more significant to TDS and, accordingly, are shown as separate captions under Operating revenues and Operating expenses, respectively, on the Consolidated Statement of Operations. Amounts in 2013 have been reclassified to conform to the 2014 presentation.

Table of ContentsAmounts Collected from Customers and Remitted to Governmental Authorities

If a tax is assessed upon the customer and TDS merely acts as an agent in collecting the tax on behalf of the imposing governmental authority, then amounts collected from customers and remitted to governmental authorities are recorded on a net basis within a tax liability account in the Consolidated Balance Sheet. If the tax is assessed upon TDS, then amounts collected from customers as recovery of the tax are recorded in Service revenues and amounts remitted to governmental authorities are recorded in Selling, general and administrative expenses in the Consolidated Statement of Operations. The amounts recorded gross in revenues that are billed to customers and remitted to governmental authorities totaled \$31.0 million and \$36.1 million for the three months ended March 31, 2014, and 2013, respectively.

**2. Fair Value Measurements**

As of March 31, 2014 and December 31, 2013, TDS did not have any financial or nonfinancial assets or liabilities that were required to be recorded at fair value in its Consolidated Balance Sheet in accordance with GAAP. However, TDS has applied the provisions of fair value accounting for purposes of computing the fair value of financial instruments for disclosure purposes as displayed below.

			Level within the Fair Value Hierarchy	March 31, 2014						December 31, 2013								
				Book Value			Fair Value			Book Value			Fair Value					
(Dollars in thousands)																		
Cash and cash equivalents			1	\$	872,910			\$	872,910			\$	830,014			\$	830,014	
Short-term investments																		
	U.S. Treasury Notes		1		40,056				40,056				50,104				50,104	
Long-term debt																		
	Retail		1		1,178,250				1,170,617				1,178,250				1,048,010	
	Institutional and other		2		537,408				536,843				537,454				512,635	

Short-term investments are designated as held-to-maturity investments and recorded at amortized cost in the Consolidated Balance Sheet. Long-term debt excludes capital lease obligations and the current portion of Long-term debt.

The fair values of Cash and cash equivalents and Short-term investments approximate their book values due to the short-term nature of these financial instruments. The fair value of "Retail" Long-term debt was estimated using market prices for TDS' 7.0% Senior Notes, 6.875% Senior Notes, 6.625% Senior Notes and 5.875% Senior Notes, and U.S. Cellular's 6.95% Senior Notes. TDS' institutional debt includes U.S. Cellular's 6.7% Senior Notes which are traded over the counter. TDS estimated the fair value of its institutional and other debt through a discounted cash flow analysis using the interest rates or estimated yield to maturity for each borrowing, which ranged from 0.00% to 6.91% at March 31, 2014.

### **3. Income Taxes**

TDS' overall effective tax rate on Income before income taxes for the three months ended March 31, 2014 and 2013 was 36.5% and 37.4%, respectively. The effective tax rate for the three months ended March 31, 2014 was lower than the rate for the three months ended March 31, 2013 primarily as a result of tax benefits from state law changes in 2014.

### **4. Earnings Per Share**

Basic earnings per share attributable to TDS shareholders is computed by dividing Net income available to common shareholders of TDS by the weighted average number of common shares outstanding during the period. Diluted earnings per share attributable to TDS shareholders is computed by dividing Net income available to common shareholders of TDS by the weighted average number of common shares outstanding during the period adjusted to include the effects of potentially dilutive securities. Potentially dilutive securities primarily include incremental shares issuable upon exercise of outstanding stock options and the vesting of restricted stock units.

The amounts used in computing earnings per common share and the effects of potentially dilutive securities on the weighted average number of common shares were as follows:

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					Three Months Ended				
					March 31,				
					2014			2013	
(Dollars and shares in thousands, except per share amounts)									
Basic earnings per share attributable to TDS shareholders:									
	Net income available to common shareholders of								
	TDS used in basic earnings per share				\$	18,242		\$	1,407
Adjustments to compute diluted earnings:									
	Noncontrolling interest adjustment					(165)			(37)
	Net income attributable to common shareholders of								
	TDS used in diluted earnings per share				\$	18,077		\$	1,370
Weighted average number of shares used in basic earnings per share:									
		Common Shares				101,821			101,095
		Series A Common Shares				7,167			7,160
			Total			108,988			108,255
Effects of dilutive securities:									
	Stock options					303			112
	Restricted stock units					381			326
Weighted average number of shares used in diluted earnings per share						109,672			108,693
Basic earnings per share attributable to TDS shareholders					\$	0.17		\$	0.01
Diluted earnings per share attributable to TDS shareholders					\$	0.16		\$	0.01

Certain Common Shares issuable upon the exercise of stock options, vesting of restricted stock units or conversion of preferred shares were not included in average diluted shares outstanding for the calculation of Diluted earnings per share attributable to TDS shareholders because their effects were antidilutive. The number of such Common Shares excluded, if any, is shown in the table below.

		<b>Three Months Ended</b>		
		<b>March 31,</b>		
		<b>2014</b>		<b>2013</b>
<b>(Shares in thousands)</b>				
Stock options		6,915		6,672



Preferred shares	57		61
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On June 25, 2013, U.S. Cellular paid a special cash dividend of \$5.75 per share, for an aggregate amount of \$482.3 million, to all holders of U.S. Cellular Common Shares and Series A Common Shares as of June 11, 2013. Outstanding U.S. Cellular stock options and restricted stock unit awards were equitably adjusted for the special cash dividend. The impact of such adjustments on the earnings per share calculation was reflected for all periods presented.

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**5. Acquisitions, Divestitures and Exchanges**

Divestiture Transaction

On November 6, 2012, U.S. Cellular entered into a Purchase and Sale Agreement with subsidiaries of Sprint Corp., fka Sprint Nextel Corporation (“Sprint”). Pursuant to the Purchase and Sale Agreement, on May 16, 2013, U.S. Cellular transferred customers and certain PCS license spectrum to Sprint in U.S. Cellular’s Chicago, central Illinois, St. Louis and certain Indiana/Michigan/Ohio markets (“Divestiture Markets”) in consideration for \$480 million in cash. The Purchase and Sale Agreement also contemplated certain other agreements, together with the Purchase and Sale Agreement collectively referred to as the “Divestiture Transaction.”

Pursuant to the Purchase and Sale Agreement, U.S. Cellular and Sprint also entered into certain other agreements, including customer and network transition services agreements, which require U.S. Cellular to provide customer, billing and network services to Sprint for a period of up to 24 months after the May 16, 2013 closing date. Sprint will reimburse U.S. Cellular for providing such services at an amount equal to U.S. Cellular’s estimated costs, including applicable overhead allocations. These services were substantially complete as of March 31, 2014. In addition, these agreements require Sprint to reimburse U.S. Cellular up to \$200 million (the “Sprint Cost Reimbursement”) for certain network decommissioning costs, network site lease rent and termination costs, network access termination costs, and employee termination benefits for specified engineering employees. It is estimated that up to \$175 million of the Sprint Cost Reimbursement will be recorded in (Gain) loss on sale of business and other exit costs, net and up to \$25 million of the Sprint Cost Reimbursement will be recorded in Cost of services in the Consolidated Statement of Operations. For the three months ended March 31, 2014, \$11.3 million of the Sprint Cost Reimbursement had been received and recorded in Cash received from divestitures in the Consolidated Statement of Cash Flows.

Financial impacts of the Divestiture Transaction are classified in the Consolidated Statement of Operations within Operating income. The table below describes the amounts TDS has recognized and expects to recognize in the Consolidated Statement of Operations between the date the Purchase and Sale Agreement was signed and the end of the transition services period.

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[illegible]

accretion, net of salvage values														
<b>(Increase) decrease in Operating income</b>				\$ (102,927)		\$ (104,927)		\$ (72,880)		\$ 6,031		\$ 45,136		

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Statement of Operations for the three months ended March 31, 2014.

On February 14, 2014, U.S. Cellular completed an exchange whereby U.S. Cellular received one E block PCS spectrum license covering Milwaukee, WI in exchange for one D block PCS spectrum license covering Milwaukee, WI. The exchange of licenses provided U.S. Cellular with spectrum to meet anticipated future capacity and coverage requirements. No cash, customers, network assets, other assets or liabilities were included in the exchange. As a result of this transaction, TDS recognized a gain of \$15.7 million, representing the difference between the \$15.9 million fair value of the license surrendered, calculated using a market approach valuation method, and the \$0.2 million carrying value of the license surrendered. This gain was recorded in (Gain) loss on license sales and exchanges in the Consolidated Statement of Operations for the three months ended March 31, 2014.

## **6. Intangible Assets**

There were no significant changes to Goodwill, Franchise rights or Other intangible assets during the periods presented.

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<b>Licenses</b>									
			<b>U.S. Cellular</b>		<b>Wireline</b>		<b>Non-Reportable Segment</b>		<b>Total</b>
<b>(Dollars in thousands)</b>									
Balance December 31, 2013		\$	1,405,759	\$	2,800	\$	15,220	\$	1,423,779
	Acquisitions		9,100		-		-		9,100
	Exchanges, net		15,719		-		-		15,719
Balance March 31, 2014		\$	1,430,578	\$	2,800	\$	15,220	\$	1,448,598
Balance December 31, 2012		\$	1,462,019	\$	2,800	\$	15,220	\$	1,480,039
	Acquisitions		14,150		-		-		14,150
Balance March 31, 2013		\$	1,476,169	\$	2,800	\$	15,220	\$	1,494,189

**7. Investments in Unconsolidated Entities**

Investments in unconsolidated entities consist of amounts invested in wireless and wireline entities in which TDS holds a noncontrolling interest. These investments are accounted for using either the equity or cost method.

	The following table, which is based on information provided in part by third parties, summarizes the combined results of operations of TDS' equity method investments.				
		<b>Three Months Ended March 31,</b>			
		<b>2014</b>		<b>2013</b>	
<b>(Dollars in thousands)</b>					
Revenues		\$	1,625,765	\$	1,475,620
Operating expenses			1,142,073		1,038,991
Operating income			483,692		436,629
Other income, net			1,835		510
Net income		\$	485,527	\$	437,139

NY1 & NY2 Deconsolidation

U.S. Cellular holds a 60.00% interest in St. Lawrence Seaway RSA Cellular Partnership (“NY1”) and a 57.14% interest in New York RSA 2 Cellular Partnership (“NY2”) (together with NY1, the “Partnerships”). The remaining interests in the Partnerships are held by Cellco Partnership d/b/a Verizon Wireless (“Verizon Wireless”). Prior to April 3, 2013, because U.S. Cellular owned a greater than 50% interest in each of these Partnerships and based on U.S. Cellular’s rights under the Partnership Agreements, TDS consolidated the financial results of these Partnerships in accordance with GAAP.

On April 3, 2013, U.S. Cellular entered into an agreement with Verizon Wireless relating to the Partnerships. The agreement amends the Partnership Agreements in several ways which provide Verizon Wireless with substantive participating rights that allow Verizon Wireless to make decisions that are in the ordinary course of business of the Partnerships and which are significant to directing and executing the activities of the business. Accordingly, as required by GAAP, TDS deconsolidated the Partnerships effective as of April 3, 2013 and thereafter reported them as equity method investments in its consolidated financial statements (“NY1 & NY2 Deconsolidation”). After the NY1 & NY2 Deconsolidation, TDS retained the same ownership percentages in the Partnerships and continues to report the same percentages of income from the Partnerships, which are recorded in Equity in earnings of unconsolidated entities in the Consolidated Statement of Operations.

#### **8. Variable Interest Entities (VIEs)**

TDS consolidates variable interest entities in which it has a controlling financial interest and is the primary beneficiary. A controlling financial interest will have both of the following characteristics: (a) the power to direct the VIE activities that most significantly impact economic performance and (b) the obligation to absorb VIE losses and the right to receive benefits that are significant to the VIE. TDS reviews these criteria initially at the time it enters into agreements and subsequently when reconsideration events occur.

#### Consolidated VIEs



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As of March 31, 2014, TDS holds a variable interest in and consolidates the following VIEs under GAAP:

- Aquinas Wireless L.P. (“Aquinas Wireless”); and
- King Street Wireless L.P. (“King Street Wireless”) and King Street Wireless, Inc., the general partner of King Street Wireless.

The power to direct the activities that most significantly impact the economic performance of Aquinas Wireless and King Street Wireless (collectively, the “limited partnerships”) is shared. Specifically, the general partner of these VIEs has the exclusive right to manage, operate and control the limited partnerships and make all decisions to carry on the business of the partnerships; however, the general partner of each partnership needs consent of the limited partner, a TDS subsidiary, to sell or lease certain licenses, to make certain large expenditures, admit other partners or liquidate the limited partnerships. Although the power to direct the activities of the VIEs is shared, TDS has a disproportionate level of exposure to the variability associated with the economic performance of the VIEs, indicating that TDS is the primary beneficiary of the VIEs in accordance with GAAP. Accordingly, these VIEs are consolidated.

The following table presents the classification of the consolidated VIEs’ assets and liabilities in TDS’ Consolidated Balance Sheet.

		March 31,		December 31,	
		2014		2013	
<b>(Dollars in thousands)</b>					
<b>Assets</b>					
	Cash and cash equivalents	\$	2,325	\$	2,076
	Other current assets		1,126		1,184
	Licenses		310,475		310,475
	Property, plant and equipment, net		16,940		18,600
	Other assets and deferred charges		511		511
	Total assets	\$	331,377	\$	332,846
<b>Liabilities</b>					
	Current liabilities	\$	135	\$	46
	Deferred liabilities and credits		2,122		3,139
	Total liabilities	\$	2,257	\$	3,185

Other Related Matters

Aquinas Wireless and King Street Wireless were formed to participate in Federal Communications Commission (“FCC”) auctions of wireless spectrum and to fund, establish, and provide wireless service with respect to any FCC licenses won in the auctions. As such, these entities have risks similar to those described in the “Risk Factors” in TDS’ Form 10-K for the year ended December 31, 2013.

TDS may agree to make additional capital contributions and/or advances to Aquinas Wireless and King Street Wireless and/or to their general partners to provide additional funding for the development of licenses granted in various auctions. TDS may finance such amounts with a combination of cash on hand, borrowings under its revolving credit agreement and/or long-term debt. There is no assurance that TDS will be able to obtain additional financing on commercially reasonable terms or at all to provide such financial support.

There were no capital contributions or advances made to Aquinas Wireless or King Street Wireless or their general partners in the three months ended March 31, 2014 and 2013.

U.S. Cellular currently provides 4G LTE service in conjunction with King Street Wireless. Aquinas Wireless is still in the process of developing long-term business plans.

## **9. Noncontrolling Interests**

The following schedule discloses the effects of Net income (loss) attributable to TDS shareholders and changes in TDS’ ownership interest in U.S. Cellular on TDS’ equity:

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				<b>Three Months Ended</b>			
				<b>March 31,</b>			
				<b>2014</b>		<b>2013</b>	
<b>(Dollars in thousands)</b>							
Net income attributable to TDS shareholders				\$	18,254	\$	1,419
	Transfer (to) from the noncontrolling interests						
	Change in TDS' Capital in excess of par value from						
	U.S. Cellular's issuance of U.S. Cellular shares				(1,010)		(1,012)
	Change in TDS' Capital in excess of par value from						
	U.S. Cellular's repurchase of U.S. Cellular shares				74		3,470
	Net transfers (to) from noncontrolling interests				(936)		2,458
	Change from net income attributable to TDS and						
	transfers (to) from noncontrolling interests			\$	17,318	\$	3,877

Mandatorily Redeemable Noncontrolling Interests in Finite-Lived Subsidiaries

TDS' consolidated financial statements include certain noncontrolling interests that meet the GAAP definition of mandatorily redeemable financial instruments. These mandatorily redeemable noncontrolling interests represent interests held by third parties in consolidated partnerships and limited liability companies ("LLCs"), where the terms of the underlying partnership or LLC agreement provide for a defined termination date at which time the assets of the subsidiary are to be sold, the liabilities are to be extinguished and the remaining net proceeds are to be distributed to the noncontrolling interest holders and TDS in accordance with the respective partnership and LLC agreements. The termination dates of these mandatorily redeemable noncontrolling interests range from 2085 to 2107.

The estimated aggregate amount that would be due and payable to settle all of these noncontrolling interests ("settlement value"), assuming an orderly liquidation of the finite-lived consolidated partnerships and LLCs on March 31, 2014, net of estimated liquidation costs, is \$10.5 million. This amount excludes redemption amounts recorded in Noncontrolling interests with redemption features in the Consolidated Balance Sheet. The estimate of settlement value was based on certain factors and assumptions which are subjective in nature. Changes in those factors and assumptions could result in a materially larger or smaller settlement amount. TDS currently has no plans or intentions relating to the liquidation of any of the related partnerships or LLCs prior to their scheduled termination dates. The corresponding carrying value of the mandatorily redeemable noncontrolling interests in finite-lived consolidated partnerships and LLCs at March 31, 2014 was \$7.2 million, and is included in Noncontrolling interests in the Consolidated Balance Sheet. The excess of the aggregate settlement value over the aggregate carrying value of these mandatorily redeemable noncontrolling interests is due primarily to the unrecognized appreciation of the noncontrolling interest holders' share of the underlying net assets in the consolidated partnerships and LLCs. Neither the noncontrolling interest holders' share, nor TDS' share, of the appreciation of the underlying net assets of these

subsidiaries is reflected in the consolidated financial statements.

## **10. Common Share Repurchases**

On August 2, 2013, the Board of Directors of TDS authorized a \$250 million stock repurchase program for the purchase of TDS Common Shares from time to time pursuant to open market purchases, block transactions, private purchases or otherwise, depending on market conditions. This authorization does not have an expiration date.

On November 17, 2009, the Board of Directors of U.S. Cellular authorized the repurchase of up to 1,300,000 Common Shares on an annual basis beginning in 2009 and continuing each year thereafter, on a cumulative basis. These purchases will be made pursuant to open market purchases, block purchases, private purchases, or otherwise, depending on market prices and other conditions. This authorization does not have an expiration date.

Share repurchases made under these authorizations were as follows:

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		Number of Shares	Average Cost			
Three Months Ended March 31,			Per Share		Amount	
(Dollar amounts and shares in thousands)						
2014						
	TDS Common Shares	158	\$	24.34	\$	3,843
	U.S. Cellular Common Shares	59	\$	39.13	\$	2,300
2013						
	TDS Common Shares	-	\$	-	\$	-
	U.S. Cellular Common Shares	496	\$	37.16	\$	18,425

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**11. Business Segment Information**

U.S. Cellular and TDS Telecom are billed for all services they receive from TDS, consisting primarily of information processing, accounting and finance, and general management services. Such billings are based on expenses specifically identified to U.S. Cellular and TDS Telecom and on allocations of common expenses. Management believes the method used to allocate common expenses is reasonable and that all expenses and costs applicable to U.S. Cellular and TDS Telecom are reflected in the accompanying business segment information on a basis that is representative of what they would have been if U.S. Cellular and TDS Telecom operated on a stand-alone basis.

Financial data for TDS' reportable segments for the three month periods ended, or as of March 31, 2014 and 2013, is as follows. See Note 1 — Basis of Presentation for additional information.

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				TDS Telecom													
Three Months Ended or as of March 31, 2014		U.S. Cellular		Wireline		Cable		HMS		TDS Telecom Eliminations		TDS Telecom Total		Non-Reportable Segment		Corporate, Eliminations and Other Reconciling Items	
(Dollars in thousands)																	
Operating revenues																	
	Service	\$	853,613	\$	176,933	\$	22,503	\$	27,376	\$	(681)	\$	226,131	\$	4,513	\$	(4,015)
	Equipment and product sales		72,198		553		-		35,732		-		36,285		7,237		-
	Total operating revenues		925,811		177,486		22,503		63,108		(681)		262,416		11,750		(4,015)
Cost of services (excluding Depreciation, amortization and accretion reported below)			180,607		64,400		10,955		16,946		(645)		91,656		4,250		(555)
Cost of equipment and products			270,474		483		-		30,467		-		30,950		5,223		-
Selling, general and administrative			395,564		46,520		6,378		14,835		(36)		67,697		3,746		(3,338)
Depreciation, amortization and accretion			167,753		42,736		4,361		6,678		-		53,775		1,802		1,589
(Gain) loss on asset disposals, net			1,934		245		65		34		-		344		143		9
(Gain) loss on sale of business and other exit			(6,900)		-		-		-		-		-		-		-

costs, net																				
(Gain) loss on license sales and exchanges		(91,446)		-		-		-		-		-		-		-		-		-
<b>Operating income</b>		7,825		23,102		744		(5,852)		-		17,994		(3,414)		(1,720)				
Equity in earnings of unconsolidated entities		37,075		-		-		-		-		-		-		-		252		
Interest and dividend income		884		685		1		20		-		706		-		896				
Interest expense		(14,862)		664		5		(421)		-		248		(1,069)		(13,024)				
Other, net		86		(54)		-		134		-		80		(5)		(1)				
<b>Income before income taxes</b>		31,008		24,397		750		(6,119)		-		19,028		(4,488)		(13,597)				
<b>Add back:</b>																				
Depreciation, amortization and accretion		167,753		42,736		4,361		6,678		-		53,775		1,802		1,589				
(Gain) loss on sale of business and other exit costs, net		(6,900)		-		-		-		-		-		-		-				
(Gain) loss on license sales and exchanges		(91,446)		-		-		-		-		-		-		-				
Interest expense		14,862		(664)		(5)		421		-		(248)		1,069		13,024				
<b>Adjusted income before income taxes</b>		\$ 115,277		\$ 66,469		\$ 5,106		\$ 980		\$ -		\$ 72,555		\$ (1,617)		\$ 1,016				
Investments in unconsolidated entities		\$ 289,842		\$ 3,807		\$ -		\$ -		\$ -		\$ 3,807		\$ -		\$ 32,630				
Total assets		\$ 6,338,334		\$ 1,426,408		\$ 280,891		\$ 313,521		\$ -		\$ 2,020,820		\$ 54,796		\$ 335,353				
Capital expenditures		\$ 89,581		\$ 22,898		\$ 6,219		\$ 2,751		\$ -		\$ 31,868		\$ 95		\$ 1,054				





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TDS Telecom									
Three Months Ended or as of March 31, 2013	U.S. Cellular	Wireline	HMS	TDS Telecom Eliminations	TDS Telecom Total	Non-Reportable Segment	Corporate, Eliminations and Other Reconciling Items	Total	
(Dollars in thousands)									
Operating revenues									
Service	\$ 996,349	\$ 180,678	\$ 22,000	\$ (78)	\$ 202,600	\$ 4,633	\$ (4,680)	\$ 1,198,902	
Equipment and product sales	85,397	897	13,564	-	14,461	9,813	-	109,671	
Total operating revenues	1,081,746	181,575	35,564	(78)	217,061	14,446	(4,680)	1,308,573	
Cost of services (excluding Depreciation, amortization and accretion reported below)	216,299	66,439	13,602	(78)	79,963	3,221	(356)	299,127	
Cost of equipment and products	241,691	1,010	11,212	-	12,222	6,852	-	260,765	
Selling, general and administrative	420,080	57,380	9,921	-	67,301	3,761	(4,239)	486,903	
Depreciation, amortization and accretion	189,845	44,023	5,468	-	49,491	1,509	1,232	242,077	
(Gain) loss on asset disposals, net	5,434	163	30	-	193	1	(12)	5,616	
(Gain) loss on sale of business and other exit	6,931	-	-	-	-	-	-	6,931	

costs, net																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																																				
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Adjusted income before income taxes is a segment measure reported to the chief operating decision maker for purposes of making decisions about allocating resources to the segments and assessing their performance. Adjusted income before income taxes is defined as Income (loss) before income taxes, adjusted for the items set forth in the reconciliation above. Adjusted income before income taxes excludes these items in order to show operating results on a more comparable basis from period to period. In addition, TDS may also exclude other items from adjusted income before income taxes if such items help reflect operating results on a more comparable basis. TDS does not intend to imply that any of such amounts that are excluded are non-recurring, infrequent or unusual; such amounts may occur in the future. TDS believes Adjusted income before income taxes is a useful measure of TDS' operating results before

significant recurring non-cash charges, discrete gains and losses and financing charges (Interest expense).

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**12. Supplemental Cash Flow Disclosures**

Under the American Recovery and Reinvestment Act of 2009 (“the Recovery Act”), TDS Telecom was awarded \$105.1 million in federal grants and will provide \$30.9 million of its own funds to complete 44 projects to provide broadband access in unserved areas. TDS Telecom received \$3.7 million and \$19.9 million in grants during the three months ended March 31, 2014 and 2013, respectively. TDS Telecom has received cumulative grants of \$67.3 million as of March 31, 2014. These funds reduced the carrying amount of the assets to which they relate. TDS Telecom had recorded \$22.7 million and \$23.6 million in grants receivable at March 31, 2014 and December 31, 2013, respectively. These amounts were included as a component of Accounts receivable, Other, in the Consolidated Balance Sheet.

U.S. Cellular and several of its wholly-owned subsidiaries participated in FCC Auction 901 and were winning bidders in eligible areas within 10 states and will receive up to \$40.1 million in one-time support from the Mobility Fund. These funds will reduce the carrying amount of the assets to which they relate or will offset operating expenses. U.S. Cellular has received \$13.4 million in support funds as of March 31, 2014, of which \$9.4 million is included as a component of Other assets and deferred charges in the Consolidated Balance Sheet and \$4.0 million reduced the carrying amount of the assets to which they relate, which are included in Property, plant and equipment in the Consolidated Balance Sheet.

**13. Subsequent Event**

On May 1, 2014, TDS entered into an agreement to acquire substantially all of the assets of a group of companies operating as BendBroadband, headquartered in Bend, Oregon for \$261 million in cash, subject to working capital and other adjustments. BendBroadband is a full-service communications company, offering an extensive range of broadband, fiber connectivity, cable television and telephone services for commercial and residential customers in Central Oregon. The agreement also includes a Tier III data center providing colocation and managed services and a cable advertising and broadcast business. At December 31, 2013, BendBroadband passed approximately 79,000 homes and businesses, with approximately 36,000 video subscribers, 41,000 high-speed broadband subscribers and 22,000 digital voice subscribers. BendBroadband generated annual revenues of \$70 million in 2013. The transaction is subject to governmental regulatory approvals, compliance with the Hart-Scott-Rodino Act and other conditions. Subject to approvals, the transaction is expected to close in the third quarter of 2014.

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

Telephone and Data Systems, Inc. ("TDS") is a diversified telecommunications company providing high-quality telecommunications services to approximately 4.7 million wireless customers and 1.1 million wireline and cable connections at March 31, 2014. TDS conducts substantially all of its wireless operations through its 84% owned subsidiary, United States Cellular Corporation ("U.S. Cellular"). TDS provides wireline services, cable services and Hosted and Managed Services ("HMS"), through its wholly-owned subsidiary, TDS Telecommunications Corporation ("TDS Telecom").

The following discussion and analysis should be read in conjunction with TDS' interim consolidated financial statements and notes included in Item 1 above, and with the description of TDS' business, its audited consolidated financial statements and Management's Discussion and Analysis of Financial Condition and Results of Operations included in TDS' Annual Report on Form 10-K ("Form 10-K") for the year ended December 31, 2013.

**OVERVIEW**

The following is a summary of certain selected information contained in the comprehensive Management's Discussion and Analysis of Financial Condition and Results of Operations that follows. The overview does not contain all of the information that may be important. You should carefully read the entire Management's Discussion and Analysis of Financial Condition and Results of Operations and not rely solely on the overview.

The following provides historical and forward-looking information and analysis about TDS' existing business segments. In addition, TDS' consolidated operations include corporate operations, corporate investments and the Non-Reportable Segment, which includes TDS' majority-owned printing and distribution company, Suttle-Straus, Inc. ("Suttle-Straus") and TDS' wholly-owned wireless telephone subsidiary, Airadigm Communications, Inc. ("Airadigm"), and may in the future include other possible activities or businesses that are not included within the operating results of U.S. Cellular or TDS Telecom. Accordingly, the combined operating results do not currently represent, and in the future will not represent, the only components of the consolidated operating results of TDS, which will continue to reflect such other operations, investments, segments, activities or businesses.

**U.S. Cellular**

In its consolidated operating markets, U.S. Cellular serves approximately 4.7 million customers in 23 states. As of March 31, 2014, U.S. Cellular's average penetration rate in its consolidated operating markets was 14.8%.

U.S. Cellular operates on a customer satisfaction strategy, striving to meet or exceed customer needs by providing a comprehensive range of wireless products and services, excellent customer support, and a high-quality network.

Financial and operating highlights in the three months ended March 31, 2014 included the following:

- In March 2014, U.S. Cellular sold the majority of its St. Louis area non-operating market license for \$92.3 million. As a result of this sale, a gain of \$75.8 million was recorded in (Gain) loss on license sales and exchanges in the Consolidated Statement of Operations.
- In February 2014, U.S. Cellular completed a license exchange in Milwaukee. As a result of this transaction, a gain of \$15.7 million was recorded in (Gain) loss on license sales and exchanges in the Consolidated Statement of Operations.
- Total consolidated customers were 4,684,000 at March 31, 2014, including 4,530,000 retail customers (97% of total).

The following operating information is presented for Core Markets. As used here, Core Markets is defined as all consolidated markets in which U.S. Cellular currently conducts business and, therefore, excludes the Divestiture Markets and the NY1 & NY2 Partnerships. Core Markets as defined also includes any other income or expenses due to U.S. Cellular's direct or indirect ownership interests in other spectrum in the Divestiture Markets which was not included in the Divestiture Transaction and other retained assets from the Divestiture Markets. See Note 5 — Acquisitions, Divestitures and Exchanges and Note 7 — Investments in Unconsolidated Entities in the Notes to Consolidated Financial Statements for additional information.

- Retail customer net losses were 80,000 in 2014 compared to net losses of 2,000 in 2013. In the postpaid category, there were net losses of 93,000 in 2014, compared to net losses of 33,000 in 2013. Postpaid defections increased due to billing system conversion issues and aggressive promotions by other carriers. Prepaid net additions were 13,000 in 2014 compared to net additions of 31,000 in 2013. The decline resulted from lower net additions in the national retail channel.
- Postpaid customers comprised approximately 92% of U.S. Cellular's retail customers as of March 31, 2014. The postpaid churn rate was 2.3% in 2014 compared to 1.6% in 2013. Billing system conversion issues and aggressive competitive offerings contributed to the increase in postpaid churn. The prepaid churn rate was 6.9% in 2014 compared to 5.6% in 2013.





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- Billed average revenue per user (“ARPU”) increased to \$53.93 in 2014 from \$50.93 in 2013 reflecting an increase in postpaid ARPU due to increases in smartphone adoption and corresponding revenues from data products and services. Service revenue ARPU increased to \$60.19 in 2014 from \$57.14 in 2013 due primarily to an increase in postpaid ARPU, offset by decreases in inbound roaming revenue and prepaid ARPU.
- Postpaid customers on smartphone service plans increased to 53% as of March 31, 2014 compared to 43% as of March 31, 2013. In addition, smartphones represented 73% of all devices sold in 2014 compared to 62% in 2013.

The following financial information is presented for U.S. Cellular consolidated results:

- Retail service revenues of \$764.8 million decreased \$119.2 million, or 13%, in 2014 due to a decrease of 1,036,000 in the average number of customers (including approximately 750,000 due to the reductions caused by the Divestiture Transaction and NY1 & NY2 Deconsolidation) partially offset by an increase in billed ARPU.
- Total additions to Property, plant and equipment were \$89.6 million, including expenditures to deploy fourth generation Long-term Evolution (“4G LTE”) equipment, construct cell sites, increase capacity in existing cell sites and switches, outfit new and remodel existing retail stores, and enhance billing and other customer management related systems and platforms. Total cell sites in service decreased 23% year-over-year to 6,165 primarily as a result of the NY1 & NY2 Deconsolidation and the deactivation of certain cell sites in the Divestiture Markets.
- Operating income increased \$6.4 million, to \$7.8 million in 2014. Excluding the (gain) loss on license sales and exchanges, operating income decreased due to lower service revenues and higher equipment subsidies exceeding reductions in operating expenses.

U.S. Cellular anticipates that its future results may be affected by the following factors:

- Effects of industry competition on service and equipment pricing;
- U.S. Cellular completed the migration of its customers to a new Billing and Operational Support System (“B/OSS”) in the third quarter of 2013. Intermittent system outages and delayed system response times negatively

impacted customer service and sales operations at certain times. System enhancements continue to be implemented to address these issues, and customer service and sales operations response times have improved. However, any future operational problems associated with the new billing system could have adverse effects on U.S. Cellular's business (in areas such as overall customer satisfaction, customer attrition, uncollectible accounts receivable, gross customer additions, or operating expenses). All of these factors could have a material adverse effect on U.S. Cellular's results of operations or cash flows;

- Impacts of selling Apple iPhone products;
- Impacts of selling devices under retail installment contracts;
- Relative ability to attract and retain customers in a competitive marketplace in a cost effective manner;
- Expanded distribution of products and services in third-party national retailers;
- Potential increases in prepaid customers, who generally generate lower ARPU and higher churn, as a percentage of U.S. Cellular's customer base in response to changes in customer preferences and industry dynamics;
- The nature and rate of growth in the wireless industry, requiring U.S. Cellular to grow revenues primarily from selling additional products and services to its existing customers, increasing the number of multi-device users among its existing customers, increasing data products and services and attracting wireless customers switching from other wireless carriers;
- Continued growth in revenues and costs related to data products and services and declines in revenues from voice services;
- Rapid growth in the demand for new data devices and services which may result in increased cost of equipment sold and other operating expenses and the need for additional investment in network capacity and enhancements;
- Further consolidation among carriers in the wireless industry, which could result in increased competition for customers and/or cause roaming revenues to decline;



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- Uncertainty related to various rulemaking proceedings underway at the Federal Communications Commission (“FCC”);
- The ability to negotiate satisfactory 4G LTE data roaming agreements with other wireless operators.

See “Results of Operations—U.S. Cellular.”

## **TDS Telecom**

The Wireline and Cable segments seek to be the preferred telecommunications solutions providers in their chosen markets serving both residential and commercial customers by developing and delivering high-quality products through a superior network that meet or exceed customers’ needs and to outperform the competition by maintaining superior customer service. TDS Telecom provides broadband, voice, and video services to residential customers through value-added bundling of products. The commercial focus is to provide advanced IP-based voice and data services to small to medium sized businesses. The HMS segment provides colocation, dedicated hosting, hosted application management, cloud computing services and planning, engineering, procurement, installation, sales and management of Information Technology (“IT”) infrastructure hardware solutions.

On October 4, 2013, TDS acquired 100% of the outstanding shares of MSN Communications, Inc. (“MSN”) for \$43.6 million in cash. The operations of MSN are included in the HMS segment. On August 1, 2013, TDS Telecom acquired substantially all of the assets of Baja Broadband, LLC (“Baja”) for \$264.1 million in cash. The operations of Baja comprise the Cable segment. These acquisitions impact the comparability of TDS Telecom’s operating results.

On May 1, 2014, TDS entered into an agreement to acquire substantially all of the assets of a group of companies operating as BendBroadband, headquartered in Bend, Oregon for \$261 million in cash, subject to working capital and other adjustments. BendBroadband is a full-service communications company, offering an extensive range of broadband, fiber connectivity, cable television and telephone services for commercial and residential customers in Central Oregon. The agreement also includes a Tier III data center providing colocation and managed services and a cable advertising and broadcast business. At December 31, 2013, BendBroadband passed approximately 79,000 homes and businesses, with approximately 36,000 video subscribers, 41,000 high-speed broadband subscribers and 22,000 digital voice subscribers. BendBroadband generated annual revenues of \$70 million in 2013. The transaction is subject to governmental regulatory approvals, compliance with the Hart-Scott-Rodino Act and other conditions. Subject to approvals, the transaction is expected to close in the third quarter of 2014.

TDS Telecom's financial results for the three months ended March 31, 2014 included the following:

- Operating revenues increased \$45.4 million or 21% to \$262.4 million in 2014. The increase was due primarily to \$47.1 million from acquisitions of Baja and MSN, partially offset by a \$4.1 million decrease in Wireline Wholesale revenues.
- Operating expenses increased \$35.3 million or 17% to \$244.4 million in 2014 due primarily to \$46.5 million from acquisitions, partially offset by a \$14.6 million decrease in Wireline expenses.

TDS anticipates that TDS Telecom's future results will be affected by the following factors:

- Continued increases in competition from wireless and other wireline providers, cable providers, and technologies such as Voice over Internet Protocol ("VoIP"), DOCSIS 3.0 and fourth-generation ("4G") mobile technology;
- Continued increases in consumer data usage and demand for high-speed data services;
- Continued declines in Wireline voice connections;
- Continued focus on customer retention programs, including discounting for "triple-play" bundles including voice, broadband and video or satellite video;
- The expansion of Internet Protocol television ("IPTV") into additional market areas;
- Continued growth in hosted and managed services which may result in the need for additional investment in data centers;
- Continued focus on cost-reduction initiatives through product and service cost improvements and process efficiencies;

- The Federal government's disbursement of Broadband Stimulus Funds to bring broadband to rural customers;

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- The National Broadband Plan and other rulemaking by the FCC, including uncertainty related to future funding from the Universal Service Fund (“USF”), broadband requirements, intercarrier compensation and changes in access reform;
- Impacts of the Baja and MSN transactions, including, but not limited to, the ability to successfully integrate and operate these businesses and the financial impacts of such transactions;
- Impacts of the BendBroadband transaction, including, but not limited to, the ability to obtain regulatory approval, successfully complete the transaction, integrate and operate the businesses of BendBroadband, and the financial impacts of such transaction, including the effects on TDS’ capital resources and liquidity as a result of the use of \$261 million in cash for the purchase price; and
- Potential acquisitions or divestitures by TDS and/or TDS Telecom of wireline, cable, HMS or other businesses.

See “Results of Operations—TDS Telecom.”

## **Pro Forma Financial Information**

Refer to TDS’ Form 8-K filed on May 3, 2013 for pro forma financial information related to the Divestiture Transaction and the NY1 & NY2 Deconsolidation for the three months ended March 31, 2013, as if the transactions had occurred at the beginning of the period.

## **REGULATORY DEVELOPMENTS**

### **FCC Interoperability Order**

On October 25, 2013, the FCC adopted a Report and Order and Order of Proposed Modification confirming a voluntary industry agreement on interoperability in the Lower 700 MHz spectrum band. The FCC's Report and Order laid out a roadmap for the voluntary commitments of AT&T and DISH Network Corporation ("DISH") to become fully binding. The FCC implemented the AT&T commitments in an Order adopted in the first quarter of 2014 that modified AT&T’s Lower 700 MHz licenses. Pursuant to these commitments, AT&T will begin incorporating changes in its network and devices that will foster interoperability across all paired spectrum blocks in the Lower 700 MHz

Band and support LTE roaming on AT&T networks for carriers with compatible Band 12 devices, consistent with the FCC's rules on roaming. AT&T will be implementing the foregoing changes in phases starting with network software enhancement taking place possibly through the third quarter of 2015 with the AT&T Band 12 device roll-out to follow. In addition, the FCC has adopted changes in its technical rules for certain unpaired spectrum licensed to AT&T and DISH in the Lower 700 MHz band to enhance prospects for Lower 700 MHz interoperability. AT&T's network and devices currently interoperate across only two of the three paired blocks in the Lower 700 MHz band. U.S. Cellular's LTE deployment, carried out in conjunction with its partner, King Street Wireless, utilizes spectrum in all three of these blocks and, consequently, was not interoperable with the AT&T configuration. U.S. Cellular believes that the FCC action will broaden the ecosystem of devices available to U.S. Cellular's customers over time.



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Three Months Ended March 31, 2014 Compared to Three Months Ended March 31, 2013											
RESULTS OF OPERATIONS — CONSOLIDATED											
Three Months Ended March 31,				2014		2013			Change	Percentage Change	
(Dollars in thousands, except per share amounts)											
Operating revenues											
	U.S. Cellular			\$	925,811	\$	1,081,746	\$	(155,935)	(14)	%
	TDS Telecom				262,416		217,061		45,355	21	%
	All other (1)				7,735		9,766		(2,031)	(21)	%
		Total operating revenues			1,195,962		1,308,573		(112,611)	(9)	%
Operating expenses											
	U.S. Cellular				917,986		1,080,280		(162,294)	(15)	%
	TDS Telecom				244,422		209,170		35,252	17	%
	All other (1)				12,869		11,969		900	8	%
		Total operating expenses			1,175,277		1,301,419		(126,142)	(10)	%
Operating income (loss)											
	U.S. Cellular				7,825		1,466		6,359	>100	%
	TDS Telecom				17,994		7,891		10,103	>100	%
	All other (1)				(5,134)		(2,203)		(2,931)	>(100)	%
		Total operating income			20,685		7,154		13,531	>100	%
Other income and (expenses)											
	Equity in earnings of unconsolidated entities				37,327		27,089		10,238	38	%
	Interest and dividend income				2,486		1,578		908	58	%
	Interest expense				(28,707)		(24,498)		(4,209)	(17)	%
	Other, net				160		(154)		314	>100	%
		Total other income (expenses)			11,266		4,015		7,251	>100	%
Income before income taxes					31,951		11,169		20,782	>100	%
	Income tax expense				11,657		4,180		7,477	>100	%
Net income					20,294		6,989		13,305	>100	%
	Less: Net income attributable to noncontrolling interests, net of tax				2,040		5,570		(3,530)	(63)	%
					18,254		1,419		16,835	>100	%

Net income attributable to TDS shareholders														
	Preferred dividend requirement					(12)		(12)			-		-	
Net income available to common shareholders					\$	18,242		\$	1,407		\$	16,835		>100%
Basic earnings per share attributable														
to TDS shareholders					\$	0.17		\$	0.01		\$	0.16		>100%
Diluted earnings per share attributable														
to TDS shareholders					\$	0.16		\$	0.01		\$	0.15		>100%
(1)	Consists of Non-Reportable Segment, corporate operations and intercompany eliminations between U.S. Cellular, TDS Telecom, the Non-Reportable Segment and corporate operations.													

### Operating revenues and expenses

See “Results of Operations — U.S. Cellular” and “Results of Operations — TDS Telecom” below for factors that affected consolidated Operating revenues and expenses.

### Equity in earnings of unconsolidated entities

TDS’ investment in the Los Angeles SMSA Limited Partnership (“LA Partnership”) contributed \$21.2 million and \$20.6 million to Equity in earnings of unconsolidated entities in 2014 and 2013, respectively.

On April 3, 2013, TDS deconsolidated the NY1 & NY2 Partnerships and began reporting them as equity method investments in its consolidated financial statements as of that date. See Note 7 — Investments in Unconsolidated Entities in Notes to Consolidated Financial Statements for additional information. In 2014, TDS’ investment in the NY1 & NY2 Partnerships contributed \$8.0 million.

Table of Contents**Interest expense**

The increase in interest expense was due primarily to a decrease in capitalized interest related to network and systems projects. Interest cost capitalized was \$1.8 million and \$5.7 million for 2014 and 2013, respectively.

**Income tax expense**

See Note 3 — Income Taxes in the Notes to Consolidated Financial Statements for a discussion of the overall effective tax rate on Income before income taxes.

**Net income (loss) attributable to noncontrolling interests, net of tax**

Net income (loss) attributable to noncontrolling interests, net of tax includes the noncontrolling public shareholders' share of U.S. Cellular's net income (loss) and the noncontrolling shareholders' or partners' share of certain TDS or U.S. Cellular subsidiaries' net income (loss).

				<b>Three Months Ended</b>			
				<b>March 31,</b>			
				<b>2014</b>		<b>2013</b>	
<b>(Dollars in thousands)</b>							
Net income (loss) attributable to noncontrolling interests, net of tax							
	U.S. Cellular noncontrolling public shareholders'	\$	3,084		\$	770	
	Noncontrolling shareholders' or partners' (1)		(1,044)			4,800	
		\$	2,040		\$	5,570	
(1)	The decrease from 2013 to 2014 is due primarily to the elimination of the noncontrolling interest as a result of the NY1 & NY2 Deconsolidation on April 3, 2013.						

Table of Contents**RESULTS OF OPERATIONS — U.S. CELLULAR**

TDS provides wireless telephone service through U.S. Cellular, an 84%-owned subsidiary. U.S. Cellular owns, manages and invests in wireless markets throughout the United States.

**Summary Operating Data for U.S. Cellular Consolidated Markets**

Following is a table of summarized operating data for U.S. Cellular's Consolidated Markets. Consolidated Markets herein refers to markets which U.S. Cellular currently consolidates, or previously consolidated in the periods presented, and is not adjusted in prior periods for subsequent divestitures or deconsolidations. Unless otherwise noted, figures reported in Results of Operations are representative of consolidated results.

As of or for Three Months Ended March 31,			2014		2013	
Retail Customers						
	Postpaid					
		Total at end of period		4,174,000		5,060,000
		Gross additions		197,000		191,000
		Net additions (losses)		(93,000)		(74,000)
		ARPU(1)	\$	57.59	\$	54.85
		Churn rate(2)		2.3%		1.7%
		Smartphone penetration(3)(4)		53.1%		43.5%
	Prepaid					
		Total at end of period		356,000		446,000
		Gross additions		85,000		104,000
		Net additions (losses)		13,000		23,000
		ARPU(1)	\$	32.22	\$	33.31
		Churn rate(2)		6.9%		6.2%
Total customers at end of period				4,684,000		5,736,000
Billed ARPU(1)			\$	53.93	\$	51.13
Service revenue ARPU(1)			\$	60.19	\$	57.63
Smartphones sold as a percent of total devices sold				73.0%		61.7%
Total Population						
	Consolidated markets(5)			54,817,000		93,943,000
	Consolidated operating markets(5)			31,729,000		47,440,000
Market penetration at end of period						
	Consolidated markets(6)			8.5%		6.1%
	Consolidated operating markets(6)			14.8%		12.1%

<b>Capital expenditures (000s)</b>	\$	89,581		\$	118,410
<b>Total cell sites in service</b>		6,165			8,027
<b>Owned towers</b>		4,448			4,411

Summary Operating Data for U.S. Cellular Core Markets									
Following is a table of summarized operating data for U.S. Cellular's Core Markets. For comparability, Core Markets as presented here excludes the results of the Divestiture Markets and NY1 and NY2 Partnerships as of or for the three months ended March 31, 2013.									
As of or for Three Months Ended March 31,			2014				2013		
Retail Customers									
	Postpaid								
		Total at end of period		4,174,000				4,463,000	
		Gross additions		197,000				176,000	
		Net additions (losses)		(93,000)				(33,000)	
		ARPU(1)	\$	57.59			\$	54.21	
		Churn rate(2)		2.3 %				1.6 %	
		Smartphone penetration(3)(4)		53.1 %				43.0 %	
	Prepaid								
		Total at end of period		356,000				373,000	
		Gross additions		85,000				91,000	
		Net additions (losses)		13,000				31,000	
		ARPU(1)	\$	32.22			\$	32.92	
		Churn rate(2)		6.9 %				5.6 %	
Total customers at end of period				4,684,000				5,005,000	
Billed ARPU(1)			\$	53.93			\$	50.93	
Service revenue ARPU(1)			\$	60.19			\$	57.14	
Smartphones sold as a percent of total devices sold				73.0 %				62.1 %	
Total Population									
	Consolidated markets(5)			54,817,000				84,025,000	
	Consolidated operating markets(5)			31,729,000				31,822,000	
Market penetration at end of period									
	Consolidated markets(6)			8.5 %				6.0 %	
	Consolidated operating markets(6)			14.8 %				15.7 %	
Capital expenditures (000s)			\$	89,581			\$	107,907	
Total cell sites in service				6,165				6,113	
Owned towers				3,883				3,846	

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- (1) ARPU metrics are calculated by dividing a revenue base by an average number of customers by the number of months in the period. These revenue bases and customer populations are shown below:
- a. Postpaid ARPU consists of total postpaid service revenues and postpaid customers.
  - b. Prepaid ARPU consists of total prepaid service revenues and prepaid customers.
  - c. Billed ARPU consists of total postpaid, prepaid and reseller service revenues and postpaid, prepaid and reseller customers.
  - d. Service revenue ARPU consists of total retail service revenues, inbound roaming and other service revenues and postpaid, prepaid and reseller customers.
- (2) Churn metrics represent the percentage of the postpaid or prepaid customers that disconnect service each month. These metrics represent the average monthly postpaid or prepaid churn rate for each respective period.
- (3) Smartphones represent wireless devices which run on an Android, Apple, BlackBerry or Windows Mobile operating system, excluding tablets.
- (4) Smartphone penetration is calculated by dividing postpaid smartphone customers by total postpaid customers.
- (5) Used only to calculate market penetration of consolidated markets and consolidated operating markets, respectively. See footnote (6) below.
- (6) Market penetration is calculated by dividing the number of wireless customers at the end of the period by the total population of consolidated markets and consolidated operating markets, respectively, as estimated by Claritas.

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Components of Operating Income									
Three Months Ended March 31, (Dollars in thousands)			2014		2013		Change		Percentage Change
Retail service		\$	764,801	\$	883,991	\$	(119,190)	(13)	%
Inbound roaming			50,126		65,874		(15,748)	(24)	%
Other			38,686		46,484		(7,798)	(17)	%
Service revenues			853,613		996,349		(142,736)	(14)	%
Equipment sales			72,198		85,397		(13,199)	(15)	%
Total operating revenues			925,811		1,081,746		(155,935)	(14)	%
System operations (excluding Depreciation, amortization and accretion reported below)			180,607		216,299		(35,692)	(17)	%
Cost of equipment sold			270,474		241,691		28,783	12	%
Selling, general and administrative			395,564		420,080		(24,516)	(6)	%
Depreciation, amortization and accretion			167,753		189,845		(22,092)	(12)	%
(Gain) loss on asset disposals, net			1,934		5,434		(3,500)	(64)	%
(Gain) loss on sale of business and other exit costs, net			(6,900)		6,931		(13,831)	>(100)	%
(Gain) loss on license sales and exchanges			(91,446)		-		(91,446)	N/M	
Total operating expenses			917,986		1,080,280		(162,294)	(15)	%
Operating income		\$	7,825	\$	1,466	\$	6,359	>100	%

**Operating Revenues***Service revenues*

Service revenues consist primarily of: (i) charges for access, airtime, roaming, recovery of regulatory costs and value added services, including data products and services, provided to U.S. Cellular's retail customers and to end users through third party resellers ("retail service"); (ii) charges to other wireless carriers whose customers use U.S. Cellular's wireless systems when roaming; and (iii) amounts received from the Federal Universal Service Fund ("USF").

***Retail service revenues***

Retail service revenues decreased by \$119.2 million, or 13%, in 2014 to \$764.8 million due to a decrease in U.S. Cellular's average customer base (including the reductions caused by the Divestiture Transaction and NY1 & NY2 Deconsolidation) partially offset by an increase in billed ARPU.

Billed ARPU increased to \$53.93 in 2014 from \$51.13 in 2013. This overall increase is due primarily to an increase in postpaid ARPU to \$57.59 in 2014 from \$54.85 in 2013, reflecting increases in smartphone adoption and corresponding revenues from data products and services.

U.S. Cellular expects continued pressure on revenues in the foreseeable future due to industry competition for customers and related effects on pricing of service plan offerings offset to some degree by continued adoption of smartphones and data usage. In addition, beginning in the second quarter of 2014, U.S. Cellular expanded its offerings involving equipment installment contracts. To the extent customers adopt these plans, U.S. Cellular expects it to reduce retail service revenue and ARPU and increase equipment revenue.

***Inbound roaming revenues***

Inbound roaming revenues decreased by \$15.7 million, or 24%, in 2014 to \$50.1 million. The decrease was due primarily to the impacts of the Divestiture Transaction and NY1 & NY2 Deconsolidation.

***Other revenues***

Other revenues decreased by \$7.8 million, or 17%, in 2014 compared to 2013, due primarily to decreases in eligible telecommunications carriers ("ETC") support.

Pursuant to the FCC's Reform Order ("Reform Order"), U.S. Cellular's current ETC support is being phased down at the rate of 20% per year beginning July 1, 2012. If the Phase II Mobility Fund is not operational by July 2014, the phase down will halt at that time and U.S. Cellular will continue to receive 60% of its baseline support until the Phase II Mobility Fund is operational. At this time,



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U.S. Cellular cannot predict the net effect of the FCC's changes to the USF high cost support program in the Reform Order. Accordingly, U.S. Cellular cannot predict whether such changes will have a material adverse effect on U.S. Cellular's business, financial condition or results of operations.

### ***Equipment sales revenues***

Equipment sales revenues include revenues from sales of wireless devices and related accessories to both new and existing customers, as well as revenues from sales of devices and accessories to agents. All Equipment sales revenues are recorded net of rebates.

U.S. Cellular offers a competitive line of quality wireless devices to both new and existing customers. U.S. Cellular's customer acquisition and retention efforts include offering new wireless devices to customers at discounted prices; in addition, customers on currently offered rate plans receive loyalty reward points that may be used to purchase a new wireless device or accelerate the timing of a customer's eligibility for a wireless device upgrade at promotional pricing. Beginning in the second quarter of 2014, U.S. Cellular expanded its offerings involving equipment installment contracts. To the extent customers adopt these plans, U.S. Cellular expects it to reduce retail service revenue and ARPU and increase equipment revenue. U.S. Cellular also continues to sell wireless devices to agents including national retailers; this practice enables U.S. Cellular to provide better control over the quality of wireless devices sold to its customers, establish roaming preferences and earn quantity discounts from wireless device manufacturers which are passed along to agents and other retailers.

Equipment sales revenues decreased \$13.2 million, or 15%, in 2014 to \$72.2 million. The decrease was due primarily to the effects of the Divestiture Transaction and the NY1 & NY2 Deconsolidation and fewer device sales in the Core Markets, primarily feature phones. The decrease also reflected a reduction in average revenue per device sold due to industry price competition.

### **Operating Expenses**

#### ***System operations expenses (excluding Depreciation, amortization and accretion)***

System operations expenses (excluding Depreciation, amortization, and accretion) include charges from telecommunications service providers for U.S. Cellular's customers' use of their facilities, costs related to local interconnection to the wireline network, charges for cell site rent and maintenance of U.S. Cellular's network, long-distance charges, outbound roaming expenses and payments to third party data product and platform developers.

System operations expenses decreased \$35.7 million, or 17%, to \$180.6 million. Key components of the net changes in System operations expense were as follows:

- Customer usage expenses decreased by \$17.7 million, or 25%, driven by impacts of the Divestiture Transaction and NY1 & NY2 Deconsolidation and decreases in certain data costs due to 4G LTE migration and lower fees for platform and content providers.
- Maintenance, utility and cell site expenses decreased \$12.2 million, or 12%, driven primarily by impacts of the Divestiture Transaction and NY1 & NY2 Deconsolidation and lower headcount.
- Expenses incurred when U.S. Cellular's customers used other carriers' networks while roaming decreased \$5.9 million, or 13%, due primarily to the Divestiture Transaction and NY1 & NY2 Deconsolidation. Such expenses also decreased in the Core Markets due to lower voice volume, offset by an increase in data roaming usage.

U.S. Cellular expects system operations expenses to increase in the future to support the continued growth in cell sites and other network facilities as it continues to add capacity, enhance quality and deploy new technologies as well as to support increases in total customer usage, particularly data usage. However, these increases are expected to be offset to some extent by cost savings generated by shifting data traffic to the 4G LTE network from the 3G network.

#### ***Cost of equipment sold***

Cost of equipment sold increased by \$28.8 million, or 12%, in 2014 to \$270.5 million. The increase was driven by a 37% increase in the average cost per device sold, which more than offset the impact of selling fewer devices. Average cost per device sold increased due to general customer preference for higher-priced 4G LTE smartphones. Smartphones sold as a percentage of total devices sold were 73.0% and 61.7% in 2014 and 2013, respectively. The total number of devices sold decreased by 16%, primarily due to the Divestiture Transaction.

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U.S. Cellular's loss on equipment, defined as equipment sales revenues less cost of equipment sold, was \$198.3 million and \$156.3 million for 2014 and 2013, respectively. U.S. Cellular expects loss on equipment to continue to be a significant cost in the foreseeable future as wireless carriers continue to use device availability and pricing as a means of competitive differentiation. In addition, U.S. Cellular expects increasing sales of data centric wireless devices to result in higher equipment subsidies over time; these devices generally have higher purchase costs which cannot be recovered through proportionately higher selling prices to customers under the standard contract/subsidy model the industry has operated with for many years. However, U.S. Cellular is beginning to offer new equipment pricing constructs such as installment plans which U.S. Cellular expects will mitigate loss on equipment to some degree.

### *Selling, general and administrative expenses*

Selling, general and administrative expenses include salaries, commissions and expenses of field sales and retail personnel and facilities; telesales department salaries and expenses; agent commissions and related expenses; corporate marketing and merchandise management; and advertising expenses. Selling, general and administrative expenses also include bad debts expense, costs of operating customer care centers and corporate expenses.

Key components of the \$24.5 million, or 6%, decrease to \$395.6 million were as follows:

- Selling and marketing expense decreased by \$5.5 million, or 3%, due primarily to the Divestiture Transaction and NY1 & NY2 Deconsolidation, offset by increases in commissions and advertising expenses.
- General and administrative expense decreased by \$19.0 million, or 8%, due primarily to the Divestiture Transaction and NY1 & NY2 Deconsolidation, offset by an increase in bad debts expense.

### *Depreciation, amortization and accretion*

Depreciation, amortization and accretion decreased \$22.1 million, or 12%, in 2014 to \$167.8 million due primarily to the higher amount of accelerated depreciation, amortization and accretion in the Divestiture Markets that occurred in 2013. The impact of the acceleration was \$13.1 million in 2014 compared to \$38.1 million in 2013. The accelerated depreciation, amortization and accretion in the Divestiture Markets was completed in the first quarter of 2014.

***(Gain) loss on asset disposals, net***

(Gain) loss on asset disposals, net was a loss in both 2014 and 2013 due primarily to the write-off and disposals of certain network assets.

***(Gain) loss on sale of business and other exit costs, net***

The net gain in 2014 and the net loss in 2013 resulted from the Divestiture Transaction. See Note 5 — Acquisitions, Divestitures and Exchanges in the Notes to Consolidated Financial Statements for additional information.

***(Gain) loss on license sales and exchanges***

The net gain in 2014 resulted from the sale of the St. Louis area non-operating market license and the license exchange in Milwaukee. See Note 5 — Acquisitions, Divestitures and Exchanges in the Notes to Consolidated Financial Statements for additional information.

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**RESULTS OF OPERATIONS — TDS TELECOM**

TDS Telecom provides broadband, video and voice telecommunications services and hosted and managed services in three reportable segments: Wireline, Cable and HMS. TDS Telecom's Wireline and Cable operations served 1,112,800 customer connections at March 31, 2014. TDS Telecom also provides hosted and managed services ("HMS") under the OneNeck IT Solutions ("OneNeck") brand, which provides colocation, dedicated hosting, hosted application management, cloud computing services and planning, engineering, procurement, installation, sales and management of Information Technology ("IT") infrastructure hardware solutions.

On August 1, 2013, TDS Telecom acquired substantially all of the assets of Baja. The operations of Baja are included in the Cable segment since the date of acquisition. On October 4, 2013, TDS acquired 100% of the outstanding shares of MSN. The operations of MSN are included in the HMS segment since the date of acquisition. These acquisitions impact the comparability of TDS Telecom's operating results.

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The following table summarizes customer connections for TDS Telecom’s Wireline and Cable operations:																
As of March 31,					2014			2013			Change					
<u>Wireline</u>																
	Residential connections															
		Voice (1)					348,700				368,600				(19,900)	
		Broadband (2)					229,000				229,500				(500)	
		IPTV (3)					15,900				9,000				6,900	
			Wireline residential connections				593,600				607,100				(13,500)	
	Commercial connections															
		Voice (1)					212,200				235,700				(23,500)	
		Broadband (2)					26,600				28,800				(2,200)	
		managedIP (4)					131,000				103,400				27,600	
			Wireline commercial connections				369,800				367,900				1,900	
	Total Wireline connections						963,400				975,000				(11,600)	
	Total residential revenue per connection (5)					\$	40.79			\$	39.99			\$	0.80	
<u>Cable</u>																
	Cable connections															
		Video (6)					68,700									
		Broadband (7)					63,000									
		Voice (7)					17,700									
			Cable connections				149,400									
	Total residential revenue per connection (5)					\$	57.37									
(1)	The individual circuit connecting customers to TDS Telecom’s central office facilities.															
(2)	The number of customers provided high-capacity data circuits via various technologies, including DSL and dedicated internet circuit technologies.															
(3)	The number of customers provided video services using IP networking technology.															
(4)	The number of telephone handsets, data lines and IP trunks providing communications using IP networking technology.															

(5)	Total residential revenue divided by the average number of total residential connections.														
(6)	Generally, a home or business receiving video programming counts as one video connection. In counting bulk residential or commercial connections, such as an apartment building or a hotel, connections are counted based on the number of units/rooms within the building receiving service.														
(7)	Broadband and voice connections reflect billable number of lines into a building for high speed data and voice services, respectively.														

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<b>TDS Telecom</b>															
<b>Components of Operating Income</b>															
<b>Three Months Ended March 31,</b>															
<b>(Dollars in thousands)</b>															
Operating revenues															
	Wireline			\$	177,486	\$	181,575	\$	(4,089)		(2)	%			
	Cable				22,503		-		22,503		N/M				
	HMS				63,108		35,564		27,544		77	%			
	Intra-company elimination				(681)		(78)		(603)		>(100)	%			
	TDS Telecom operating revenues				262,416		217,061		45,355		21	%			
Operating expenses															
	Wireline				154,384		169,015		(14,631)		(9)	%			
	Cable				21,759		-		21,759		N/M				
	HMS				68,960		40,233		28,727		71	%			
	Intra-company elimination				(681)		(78)		(603)		>(100)	%			
	TDS Telecom operating expenses				244,422		209,170		35,252		17	%			
	TDS Telecom operating income			\$	17,994	\$	7,891	\$	10,103		>100	%			

N/M - Not meaningful

<b>Wireline Operations</b>															
<b>Components of Operating Income</b>															
<b>Three Months Ended March 31,</b>															
<b>(Dollars in thousands)</b>															
Service revenues															
	Residential			\$	72,505	\$	73,004	\$	(499)		(1)	%			
	Commercial				57,980		57,125		855		1	%			
	Wholesale				46,448		50,549		(4,101)		(8)	%			
	Total service revenues				176,933		180,678		(3,745)		(2)	%			
Equipment sales															
					553		897		(344)		(38)	%			



			Total operating revenues			177,486			181,575			(4,089)		(2)	%
			Cost of services (excluding												
			Depreciation, amortization and												
			accretion reported below)			64,400			66,439			(2,039)		(3)	%
			Cost of equipment sold			483			1,010			(527)		(52)	%
			Selling, general and administrative			46,520			57,380			(10,860)		(19)	%
			Depreciation, amortization and accretion			42,736			44,023			(1,287)		(3)	%
			(Gain) loss on asset disposals, net			245			163			82		50	%
			Total operating expenses			154,384			169,015			(14,631)		(9)	%
			Total operating												
			income			\$ 23,102			\$ 12,560			\$ 10,542		84	%

## Operating Revenues

**Residential revenues** consist of voice, data and video services to TDS Telecom's Wireline residential customer base.

Residential revenues decreased \$0.5 million or 1% to \$72.5 million in 2014. Legacy voice connections declined by 6% decreasing revenues by \$2.2 million, while IPTV connections grew 76% increasing revenues \$1.2 million. A 2% increase in average revenue per residential connection driven by growth in customers selecting higher tier IPTV packages and the growth of customers opting for faster broadband speeds increased revenues \$1.0 million.

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**Commercial revenues** consist of data and voice services and sales and installation of IP-based telecommunication systems to TDS Telecom's Wireline commercial customer base.

Commercial revenues increased \$0.9 million or 1% to \$58.0 million in 2014. A 1% increase in average revenue per commercial connection, primarily driven by higher managedIP rates, increased revenues \$0.7 million. TDS managedIP connections grew 28% as customers converted from legacy voice and data products.

**Wholesale revenues** represent compensation from other carriers for utilizing TDS Telecom's network infrastructure and regulatory recoveries.

Wholesale revenues decreased \$4.1 million or 8% to \$46.4 million. Revenues received through inter-state and intra-state regulatory recovery mechanisms decreased \$2.0 million. Wholesale revenues declined \$0.8 million due to a 12% reduction in intra-state minutes-of-use. Revenues received for Network access also decreased \$0.6 million in 2014 as a result of changes in support mechanisms and in intercarrier compensation resulting from the Reform Order released by the FCC in November 2011.

## **Operating Expenses**

### ***Cost of services (excluding Depreciation, amortization and accretion)***

Cost of services decreased \$2.0 million or 3% to \$64.4 million in 2014. Employee expenses decreased by \$1.9 million while reductions in costs of providing long distance services and promotional giveaways reduced expense \$1.4 million. Charges related to the growth in IPTV increased cost of services \$0.9 million.

### ***Selling, general and administrative expenses***

Selling, general and administrative expenses decreased \$10.9 million or 19% to \$46.5 million in 2014 due primarily to decreases in employee expenses of \$5.9 million and consulting and IT maintenance charges of \$2.3 million.

### ***Depreciation, amortization and accretion***

Depreciation, amortization and accretion expense decreased \$1.3 million or 3% to \$42.7 million in 2014 primarily due to depreciation being fully recognized on some assets.

<b>Cable Operations</b>						
<b>Components of Operating Income</b>						
<b>Three Months Ended March 31,</b>					<b>2014</b>	
(Dollars in thousands)						
Service revenues						
	Residential			\$		18,253
	Commercial					4,250
			Total operating revenues			22,503
Cost of services (excluding Depreciation, amortization and accretion reported below)						10,955
Selling, general and administrative						6,378
Depreciation, amortization and accretion						4,361
(Gain) loss on asset disposals, net						65
			Total operating expenses			21,759
			Total operating income (loss)	\$		744

## Operating Revenues

**Residential revenues** consist of video, broadband and voice services to TDS Telecom's Cable residential customer base.

Cable had 106,500 residential customer connections which generated revenues of \$18.3 million in the quarter.

**Commercial revenues** consist of video, broadband and voice services to TDS Telecom's Cable commercial customer base.

Cable had 42,900 commercial customer connections which generated Commercial revenues of \$4.3 million in 2014.



Table of Contents**Operating Expenses***Cost of services (excluding Depreciation, amortization and accretion)*

Cost of services (excluding Depreciation, amortization and accretion) of \$11.0 million were incurred in 2014 for programming costs and expenses related to the delivery and support of services.

*Selling, general and administrative expenses*

Selling, general and administrative expenses of \$6.4 million were incurred primarily for product management and marketing of services in 2014.

*Depreciation, amortization and accretion expense*

Depreciation, amortization and accretion expense was \$4.4 million. Amortization of the acquired customer list and trade name contributed \$1.4 million to the expense in 2014.

<b>HMS Operations</b>													
<b>Components of Operating Income (Loss)</b>													
<b>Three Months Ended March 31,</b>					<b>2014</b>		<b>2013</b>		<b>Change</b>		<b>Percentage</b>		
(Dollars in thousands)											<b>Change</b>		
Service revenues				\$	27,376	\$	22,000	\$	5,376		24	%	
Equipment sales					35,732		13,564		22,168		>100	%	
Total operating revenues					63,108		35,564		27,544		77	%	
Cost of services (excluding					16,946		13,602		3,344		25	%	
Depreciation, amortization and accretion													

reported below)									
Cost of equipment sold			30,467		11,212		19,255	>100	%
Selling, general and administrative			14,835		9,921		4,914	50	%
Depreciation, amortization and accretion			6,678		5,468		1,210	22	%
(Gain) loss on asset disposals, net			34		30		4	13	%
Total operating expenses			68,960		40,233		28,727	71	%
Total operating income (loss)		\$	(5,852)		\$	(4,669)		\$	(1,183) %

## Operating Revenues

*Service revenues* consist primarily of colocation, cloud computing and hosted managed services, application management, and installation and management of IT infrastructure hardware solutions.

Service revenues increased \$5.4 million or 24% to \$27.4 million in 2014. The acquisition of MSN in October of 2013 contributed \$3.6 million of this increase with the remaining increase primarily due to growth in colocation, dedicated hosting, hosted application management and cloud computing services of \$1.6 million or 9%.

*Equipment sales revenues* include revenues from sales of IT infrastructure hardware solutions.

Equipment sales revenues increased \$22.2 million to \$35.7 million in 2014. The acquisition of MSN contributed \$21.0 million of this increase.

## Operating Expenses

### *Cost of services (excluding Depreciation, amortization and accretion)*

Cost of services increased \$3.3 million to \$16.9 million in 2014 due primarily to \$2.8 million from the acquisition of MSN.

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***Cost of equipment sold***

Cost of equipment sold increased \$19.3 million to \$30.5 million in 2014. The acquisition of MSN contributed \$17.8 million of this increase.

***Selling, general and administrative expense***

Selling, general and administrative expense increased \$4.9 million to \$14.8 million in 2014 due primarily to \$3.4 million from the acquisition of MSN.

***Depreciation, amortization and accretion expense***

Depreciation, amortization and accretion expense increased \$1.2 million to \$6.7 million due to \$0.6 million of customer list amortization from the MSN acquisition and depreciation on capital additions.

**RECENT ACCOUNTING PRONOUNCEMENTS**

Recent accounting pronouncements are not expected to have a significant effect on TDS' financial condition or results of operations. See Note 1 — Basis of Presentation in the Notes to Consolidated Financial Statements for additional information.

**FINANCIAL RESOURCES**

TDS operates a capital- and marketing-intensive business. TDS utilizes cash on hand, cash from operating activities, cash proceeds from divestitures and disposition of investments, short-term credit facilities and long-term debt financing to fund its acquisitions (including 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, capital expenditures and other factors. The table below and the following discussion in this Financial Resources section summarize TDS' cash flow activities for the three months ended March 31, 2014 and 2013.

		2014	2013
<b>(Dollars in thousands)</b>			
Cash flows from (used in):			
Operating activities	\$	104,937	\$ 246,352
Investing activities		(44,479)	(184,104)
Financing activities		(17,562)	(36,029)
Net increase in cash and cash equivalents	\$	42,896	\$ 26,219

### Cash Flows from Operating Activities

Cash flows from operating activities were \$104.9 million in 2014 and \$246.4 million in 2013, including net income tax payments of \$25.9 million and \$1.0 million, respectively. This decrease was due primarily to lower earnings excluding gains recognized on sale of business and license sales and exchanges. Also contributing to this decrease were changes in Accounts payable balances driven primarily by payment timing differences related to operating expenses and device purchases. The above decreases in Cash flows from operating activities were partially offset by changes in Accounts receivable balances as the high receivables at December 31, 2013 resulting from the conversion to a new U.S. Cellular billing system have begun to decline towards more normal levels.

### Cash Flows from Investing Activities

TDS makes substantial investments to acquire wireless licenses and properties and to construct and upgrade 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 TDS' networks.

Capital expenditures (i.e., additions to property, plant and equipment and system development expenditures) totaled \$122.6 million in 2014 and \$150.1 million in 2013. Cash used for additions to property, plant and equipment is reported in the Consolidated Statement of Cash Flows and excludes amounts accrued in Accounts receivable and Accounts payable for capital expenditures at March 31, 2014 and includes amounts received and/or paid in the current period that were accrued at December 31, 2013. Cash used for additions to property, plant and equipment totaled \$150.9 million in 2014 and \$176.3 million in 2013. See "Capital Expenditures" in Liquidity and Capital Resources below for additional information on capital expenditures.

Cash payments for acquisitions of U.S. Cellular licenses were \$9.1 million and \$14.2 million in 2014 and 2013, respectively.





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Cash received from divestitures in 2014 was as follows. No cash was received from divestitures in 2013.			
<b>Cash Received from Divestitures</b>		<b>2014</b>	
<b>(Dollars in thousands)</b>			
U.S. Cellular licenses	\$		91,789
U.S. Cellular businesses			11,253
<b>Total</b>	\$		103,042

See Note 5 — Acquisitions, Divestitures and Exchanges in the Notes to Consolidated Financial Statements for additional information related to these divestitures.

In 2014, TDS realized proceeds of \$10.0 million related to the maturities of certain of its investments in U.S. Treasury Notes.

**Cash Flows from Financing Activities**

Cash flows from financing activities include proceeds from and repayments of short-term and long-term debt, dividends to shareholders, distributions to noncontrolling interests, cash used to repurchase Common Shares and cash proceeds from reissuance of Common Shares pursuant to stock-based compensation plans.

In 2014, TDS repurchased Common Shares for \$3.3 million. TDS did not repurchase any Common Shares in 2013. Payments for repurchases of U.S. Cellular Common Shares required \$2.0 million and \$18.4 million in 2014 and 2013, respectively. See Note 10 — Common Share Repurchases in the Notes to Consolidated Financial Statements for additional information related to these transactions.

**Free Cash Flow**

The following table presents Free cash flow. Free cash flow is defined as Cash flows from operating activities less Cash used for additions to property, plant and equipment. Free cash flow is a non-GAAP financial measure which TDS believes may be useful to investors and other users of its financial information in evaluating the amount of cash generated by business operations, after Cash used for additions to property, plant and equipment.

<b>Three Months Ended March 31,</b>				<b>2014</b>			<b>2013</b>
<b>(Dollars in thousands)</b>							
Cash flows from operating activities			\$	104,937		\$	246,352
Cash used for additions to property, plant and equipment				(150,890)			(176,318)
Free cash flow			\$	(45,953)		\$	70,034
See Cash Flows from Operating Activities and Cash Flows from Investing Activities for additional information related to the components of Free cash flow.							

## LIQUIDITY AND CAPITAL RESOURCES

TDS believes that existing cash and investment balances, funds available under its revolving credit facilities and expected cash flows from operating and investing activities provide substantial liquidity and financial flexibility for TDS to meet its normal financing needs for the foreseeable future. In addition, TDS and its subsidiaries may access public and private capital markets to help meet their financing needs.

TDS cannot provide assurances that circumstances that could have a material adverse effect on its liquidity or capital resources will not occur. Economic conditions, changes in financial markets, TDS financial performance and/or prospects or other factors could restrict TDS' liquidity and availability of financing on terms and prices acceptable to TDS, which could require TDS to reduce its capital expenditure, acquisition or share repurchase programs. Such reductions could have a material adverse effect on TDS' business, financial condition or results of operations.

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The following table summarizes TDS' and U.S. Cellular's cash and investments as of March 31, 2014.					
<b>(Dollars in thousands)</b>	<b>TDS</b>			<b>U.S. Cellular (1)</b>	
Cash and cash equivalents	\$	872,910		\$	398,541
Short-term investments	\$	40,056		\$	40,056
(1)	Also included as a component of the TDS column.				

**Cash and Cash Equivalents**

Cash and cash equivalents include cash and short-term, highly liquid investments with original maturities of three months or less. The primary objective of TDS' Cash and cash equivalents investment activities is to preserve principal. At March 31, 2014, the majority of TDS' Cash and cash equivalents was held in bank deposit accounts and in money market funds that invest exclusively in U.S. Treasury Notes or in repurchase agreements fully collateralized by such obligations. TDS 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.

**Short-term Investments**

Short-term investments consist of U.S. Treasury Notes which are designated as held-to-maturity investments and are recorded at amortized cost in the Consolidated Balance Sheet. For these investments, TDS' objective is to earn a higher rate of return on funds that are not anticipated to be required to meet liquidity needs in the near term, while maintaining a low level of investment risk. See Note 2 — Fair Value Measurements in the Notes to Consolidated Financial Statements for additional information on Short-term investments.

**Revolving Credit Facilities**

TDS and U.S. Cellular have revolving credit facilities available for general corporate purposes.

In connection with U.S. Cellular's revolving credit facility, TDS and U.S. Cellular entered into a subordination agreement dated December 17, 2010 together with the administrative agent for the lenders under U.S. Cellular's

revolving credit facility. At March 31, 2014, no U.S. Cellular debt was subordinated pursuant to this subordination agreement.

In April 2014, two of the nationally recognized credit rating agencies downgraded the TDS and U.S. Cellular corporate and senior debt credit ratings. After these downgrades, two of the nationally recognized credit rating agencies rated TDS and U.S. Cellular at investment grade. One of the nationally recognized credit rating agencies rated TDS and U.S. Cellular at sub-investment grade.

TDS' and U.S. Cellular's interest cost on their revolving credit facilities may be subject to increase if their current credit ratings from nationally recognized credit rating agencies are lowered, and may be subject to decrease if the ratings are raised. The April 2014 downgrades will not affect the interest cost on the revolving credit facility. The credit facilities would not cease to be available nor would the maturity date accelerate solely as a result of a downgrade in TDS' or U.S. Cellular's credit rating. However, a further downgrade in TDS' or U.S. Cellular's credit rating could adversely affect their ability to renew the credit facilities or obtain access to other credit facilities in the future.

The following table summarizes the terms of such revolving credit facilities as of March 31, 2014:					
(Dollars in millions)		TDS		U.S. Cellular	
Maximum borrowing capacity	\$	400.0		\$	300.0
Letters of credit outstanding	\$	0.3		\$	17.6
Amount borrowed	\$	-		\$	-
Amount available for use	\$	399.7		\$	282.4
Agreement date		December 2010			December 2010
Maturity date		December 2017			December 2017

The continued availability of the revolving credit facilities requires TDS and U.S. Cellular to comply with certain negative and affirmative covenants, maintain certain financial ratios and make representations regarding certain matters at the time of each borrowing. TDS and U.S. Cellular believe that they were in compliance as of March 31, 2014 with all of the financial covenants and requirements set forth in their revolving credit facilities. TDS also has certain other non-material credit facilities from time to time.

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**Long-Term Financing**

There were no material changes to Long-Term Financing as disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations included in TDS' Form 10-K for the year ended December 31, 2013.

TDS and its subsidiaries' long-term debt indentures do not contain any provisions resulting in acceleration of the maturities of outstanding debt in the event of a change in TDS' credit rating. However, a downgrade in TDS' credit rating could adversely affect its ability to obtain long-term debt financing in the future. TDS believes that it and its subsidiaries were in compliance as of March 31, 2014 with all financial covenants and other requirements set forth in its long-term debt indentures. TDS and U.S. Cellular have not failed to make nor do they expect to fail to make any scheduled payment of principal or interest under such indentures.

The long-term debt principal payments due for the remainder of 2014 and the next four years represent less than 1% of the total long-term debt obligation at March 31, 2014. Refer to Market Risk — Long-Term Debt in TDS' Form 10-K for the year ended December 31, 2013 for additional information regarding required principal payments and the weighted average interest rates related to TDS' Long-term debt.

**Capital Expenditures**

U.S. Cellular's capital expenditures for 2014 are expected to be approximately \$640 million. These expenditures are expected to be for the following general purposes:

- Expand and enhance network coverage in its service areas, including providing additional capacity to accommodate increased network usage, principally data usage, by current customers;
- Continue to deploy 4G LTE technology in certain markets;
- Expand and enhance the retail store network; and
- Develop and enhance office systems.

TDS Telecom's capital expenditures for 2014 are expected to be approximately \$200 million. These expenditures are expected to be for the following general purposes:

- Maintain and enhance existing infrastructure at Wireline, HMS and Cable;
- Fiber expansion in Wireline markets to support IPTV and super high speed data;
- Success-based spending to sustain managedIP, IPTV, HMS and Cable growth; and
- Expansion of HMS data center facilities.

TDS plans to finance its capital expenditures program for 2014 using primarily Cash flows from operating activities and, as necessary, existing cash balances and short-term investments.

### **Acquisitions, Divestitures and Exchanges**

TDS assesses its business interests on an ongoing basis with a goal of improving the competitiveness of its operations and maximizing its long-term return on investment. As part of this strategy, TDS reviews attractive opportunities to acquire additional wireless operating markets and wireless spectrum; and telecommunications, cable, HMS or other possible businesses. In addition, TDS may seek to divest outright or include in exchanges for other interests those interests that are not strategic to its long-term success. As a result, TDS may be engaged from time to time in negotiations relating to the acquisition, divestiture or exchange of companies, properties, wireless spectrum and other possible businesses. In general, TDS may not disclose such transactions until there is a definitive agreement. See Note 5 — Acquisitions, Divestitures and Exchanges in the Notes to Consolidated Financial Statements for additional information related to significant transactions.

### **Variable Interest Entities**

TDS consolidates certain entities because they are “variable interest entities” under accounting principles generally accepted in the United States of America (“GAAP”). See Note 8 — Variable Interest Entities (VIEs) in the Notes to Consolidated Financial Statements for additional information related to these variable interest entities. TDS 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 Programs**

In the past year, TDS and U.S. Cellular have repurchased and expect to continue to repurchase their Common Shares, in each case subject to any available repurchase program. For additional information related to the current TDS and U.S. Cellular repurchase authorizations and repurchases made during 2014 and 2013, see Note 10 — Common Share Repurchases in the Notes to Consolidated Financial Statements and Part II, Item 2. 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, 2013 and March 31, 2014 to the Contractual and Other Obligations disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations included in TDS' Form 10-K for the year ended December 31, 2013.

**Off-Balance Sheet Arrangements**

TDS 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, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

**APPLICATION OF CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

TDS prepares its consolidated financial statements in accordance with GAAP. TDS' significant accounting policies are discussed in detail in Note 1 — Summary of Significant Accounting Policies and Recent Accounting Pronouncements in the Notes to Consolidated Financial Statements and TDS' Application of Critical Accounting Policies and Estimates is discussed in detail in Management's Discussion and Analysis of Financial Condition and Results of Operations, both of which are included in TDS' Form 10-K for the year ended December 31, 2013. There were no material changes to TDS' application of critical accounting policies and estimates during the three months ended March 31, 2014.





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**PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995**

**SAFE HARBOR CAUTIONARY STATEMENT**

This Form 10-Q, including exhibits, contains statements that are not based on historical facts and represent forward-looking statements, as this term is defined in the Private Securities Litigation Reform Act of 1995. All statements, other than statements of historical facts, that address activities, events or developments that TDS intends, expects, projects, believes, estimates, plans or anticipates will or may occur in the future are forward-looking statements. The words “believes,” “anticipates,” “estimates,” “expects,” “plans,” “intends,” “projects” and similar expressions intended to identify these forward-looking statements, but are not the exclusive means of identifying them. 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. Such risks, uncertainties and other factors include those set forth below, as more fully described under “Risk Factors” in TDS’ Form 10-K for the year ended December 31, 2013. However, such factors are not necessarily all of the important factors that could cause actual results, performance or achievements to differ materially from those expressed in, or implied by, the forward-looking statements contained in this document. Other unknown or unpredictable factors also could have material adverse effects on future results, performance or achievements. TDS undertakes no obligation to update publicly any forward-looking statements whether as a result of new information, future events or otherwise. You should carefully consider the Risk Factors in TDS’ Form 10-K for the year ended December 31, 2013, the following factors and other information contained in, or incorporated by reference into, this Form 10-Q to understand the material risks relating to TDS’ business.

- *Intense competition in the markets in which TDS operates could adversely affect TDS’ revenues or increase its costs to compete.*
- *A failure by TDS to successfully execute its business strategy (including planned acquisitions, divestitures and exchanges) or allocate resources or capital could have an adverse effect on TDS’ business, financial condition or results of operations.*
- *A failure by TDS’ service offerings to meet customer expectations, including any continuing issues relating to the conversion to the new Billing and Operational Support System (“B/OSS”) in the third quarter of 2013, could limit TDS’ ability to attract and retain customers and could have an adverse effect on TDS’ business, financial condition or results of operations.*
- *TDS’ system infrastructure may not be capable of supporting changes in technologies and services expected by customers, which could result in lost customers and revenues.*

- *Changes in roaming practices or other factors could cause TDS' roaming revenues to decline from current levels and/or impact TDS' ability to service its customers in geographic areas where TDS does not have its own network, which would have an adverse effect on TDS' business, financial condition or results of operations.*
- *A failure by TDS to obtain access to adequate radio spectrum to meet current or anticipated future needs and/or to accurately predict future needs for radio spectrum could have an adverse effect on TDS' business, financial condition or results of operations.*
- *To the extent conducted by the Federal Communications Commission ("FCC"), TDS is likely to participate in FCC auctions of additional spectrum in the future as an applicant or as a noncontrolling partner in another auction applicant and, during certain periods, will be subject to the FCC's anti-collusion rules, which could have an adverse effect on TDS.*
- *Changes in the regulatory environment or a failure by TDS to timely or fully comply with any applicable regulatory requirements could adversely affect TDS' business, financial condition or results of operations.*
- *Changes in Universal Service Fund ("USF") funding and/or intercarrier compensation could have an adverse impact on TDS' business, financial condition or results of operations.*
- *An inability to attract and/or retain highly competent management, technical, sales and other personnel could have an adverse effect on TDS' business, financial condition or results of operations.*
- *TDS' assets are concentrated primarily in the U.S. telecommunications industry. As a result, its results of operations may fluctuate based on factors related primarily to conditions in this industry.*
- *TDS' lower scale relative to larger competitors could adversely affect its business, financial condition or results of operations.*
- *Changes in various business factors could have an adverse effect on TDS' business, financial condition or results of operations.*

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- *Advances or changes in technology could render certain technologies used by TDS obsolete, could put TDS at a competitive disadvantage, could reduce TDS' revenues or could increase its costs of doing business.*
- *Complexities associated with deploying new technologies present substantial risk.*
- *TDS is subject to numerous surcharges and fees from federal, state and local governments, and the applicability and the amount of these fees are subject to great uncertainty.*
- *Performance under device purchase agreements could have a material adverse impact on TDS' business, financial condition or results of operations.*
- *Changes in TDS' enterprise value, changes in the market supply or demand for wireless licenses, wireline or cable markets or IT service providers, adverse developments in the businesses or the industries in which TDS is involved and/or other factors could require TDS to recognize impairments in the carrying value of its licenses, goodwill, franchise rights and/or physical assets.*
- *Costs, integration problems or other factors associated with acquisitions, divestitures or exchanges of properties or licenses and/or expansion of TDS' businesses could have an adverse effect on TDS' business, financial condition or results of operations.*
- *A significant portion of TDS' wireless revenues is derived from customers who buy services through independent agents who market TDS' services on a commission basis and third-party national retailers. If TDS' relationships with these agents or third-party national retailers are seriously harmed, its business, financial condition or results of operations could be adversely affected.*
- *TDS' investments in unproven technologies may not produce the benefits that TDS expects.*
- *A failure by TDS to complete significant network construction and systems implementation activities as part of its plans to improve the quality, coverage, capabilities and capacity of its networks and support systems could have an adverse effect on its operations.*

- *Financial difficulties (including bankruptcy proceedings) or other operational difficulties of TDS' key suppliers, termination or impairment of TDS' relationships with such suppliers, or a failure by TDS to manage its supply chain effectively could result in delays or termination of TDS' receipt of required equipment or services, or could result in excess quantities of required equipment or services, any of which could adversely affect TDS' business, financial condition or results of operations.*
- *TDS has significant investments in entities that it does not control. Losses in the value of such investments could have an adverse effect on TDS' financial condition or results of operations.*
- *A failure by TDS to maintain flexible and capable telecommunication networks or information technology, or a material disruption thereof, including breaches of network or information technology security, could have an adverse effect on TDS' business, financial condition or results of operations.*
- *Wars, conflicts, hostilities and/or terrorist attacks or equipment failures, power outages, natural disasters or other events could have an adverse effect on TDS' business, financial condition or results of operations.*
- *The market price of TDS' Common Shares is subject to fluctuations due to a variety of factors.*
- *Identification of errors in financial information or disclosures could require amendments to or restatements of financial information or disclosures included in this or prior filings with the Securities and Exchange Commission ("SEC"). Such amendments or restatements and related matters, including resulting delays in filing periodic reports with the SEC, could have an adverse effect on TDS' business, financial condition or results of operations.*
- *The existence of material weaknesses in the effectiveness of internal control over financial reporting could result in inaccurate financial statements or other disclosures or failure to prevent fraud, which could have an adverse effect on TDS' business, financial condition or results of operations.*

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- *Changes in facts or circumstances, including new or additional information that affects the calculation of potential liabilities for contingent obligations under guarantees, indemnities, claims, litigation or otherwise, could require TDS to record charges in excess of amounts accrued in the financial statements, if any, which could have an adverse effect on TDS' business, financial condition or results of operations.*
- *Disruption in credit or other financial markets, a deterioration of U.S. or global economic conditions or other events could, among other things, impede TDS' access to or increase the cost of financing its operating and investment activities and/or result in reduced revenues and lower operating income and cash flows, which would have an adverse effect on TDS' business, financial condition or results of operations.*
- *Uncertainty of TDS' ability to access capital, deterioration in the capital markets, other changes in market conditions, changes in TDS' credit ratings or other factors could limit or restrict the availability of financing on terms and prices acceptable to TDS, which could require TDS to reduce its construction, development or acquisition programs.*
- *Settlements, judgments, restraints on its current or future manner of doing business and/or legal costs resulting from pending and future litigation could have an adverse effect on TDS' business, financial condition or results of operations.*
- *The possible development of adverse precedent in litigation or conclusions in professional studies to the effect that radio frequency emissions from wireless devices and/or cell sites cause harmful health consequences, including cancer or tumors, or may interfere with various electronic medical devices such as pacemakers, could have an adverse effect on TDS' wireless business, financial condition or results of operations.*
- *Claims of infringement of intellectual property and proprietary rights of others, primarily involving patent infringement claims, could prevent TDS from using necessary technology to provide products or services or subject TDS to expensive intellectual property litigation or monetary penalties, which could have an adverse effect on TDS' business, financial condition or results of operations.*
- *Certain matters, such as control by the TDS Voting Trust and provisions in the TDS Restated Certificate of Incorporation, may serve to discourage or make more difficult a change in control of TDS.*
- *Any of the foregoing events or other events could cause revenues, earnings, capital expenditures and/or any other financial or statistical information to vary from TDS' forward-looking estimates by a material amount.*



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

**MARKET RISK**

Refer to the disclosure under Market Risk in TDS' Form 10-K for the year ended December 31, 2013 for additional information, including information regarding required principal payments and the weighted average interest rates related to TDS' Long-term debt. There have been no material changes to such information since December 31, 2013.

See Note 2 — Fair Value Measurements in the Notes to Consolidated Financial Statements for additional information related to the fair value of TDS' Long-term debt as of March 31, 2014.



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**Item 4. Controls and Procedures**

Evaluation of Disclosure Controls and Procedures

TDS maintains disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) that are designed to ensure that information required to be disclosed in its reports filed or submitted under the Exchange Act is processed, recorded, summarized and reported within the time periods specified in the Securities and Exchange Commission’s (“SEC”) rules and forms, and that such information is accumulated and communicated to TDS’ management, including its principal executive officer and principal financial officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

As required by SEC Rule 13a-15(b), TDS carried out an evaluation, under the supervision and with the participation of management, including its principal executive officer and principal financial officer, of the effectiveness of the design and operation of TDS’ disclosure controls and procedures as of the end of the period covered by this Quarterly Report. Based on this evaluation, TDS’ principal executive officer and principal financial officer concluded that TDS’ disclosure controls and procedures were effective as of March 31, 2014, at the reasonable assurance level.

Changes in Internal Control Over Financial Reporting

Internal controls over financial reporting are updated as necessary to accommodate modifications to our business processes and accounting procedures. There have been no changes in TDS’ internal control over financial reporting during the quarter ended March 31, 2014 that have materially affected, or are reasonably likely to materially affect TDS’ internal control over financial reporting.

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**Part II. Other Information**

**Item 1. Legal Proceedings.**

Refer to the disclosure under Legal Proceedings in TDS' Form 10-K for the year ended December 31, 2013. There have been no material changes to such information since December 31, 2013.

**Item 1A. Risk Factors.**

In addition to the information set forth in this Form 10-Q, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in TDS' Annual Report on Form 10-K for the year ended December 31, 2013, which could materially affect TDS' business, financial condition or future results. The risks described in this Form 10-Q and the Form 10-K for the year ended December 31, 2013, may not be the only risks that could affect TDS. Additional unidentified or unrecognized risks and uncertainties could materially adversely affect TDS' business, financial condition and/or operating results. Subject to the foregoing, TDS has not identified for disclosure any material changes to the risk factors as previously disclosed in TDS' Annual Report on Form 10-K for the year ended December 31, 2013.

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

On August 2, 2013, the Board of Directors of TDS authorized a \$250 million stock repurchase program for TDS Common Shares. Depending on market conditions, such shares may be repurchased in compliance with Rule 10b-18 of the Securities Exchange Act of 1934, as amended ("Exchange Act"), pursuant to Rule 10b5-1 under the Exchange Act, or pursuant to accelerated share repurchase arrangements, prepaid share repurchases, private transactions or as otherwise authorized. This authorization does not have an expiration date.

The following table provides certain information with respect to all purchases made by or on behalf of TDS, and any open market purchases made by any "affiliated purchaser" (as defined by the SEC) of TDS, of TDS Common Shares during the quarter covered by this Form 10-Q.

Period	Total Number of	Average Price	Total Number of Shares	Maximum Dollar Value of Shares that
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		Shares Purchased	Paid per Share	Purchased as Part of Publicly Announced Plans or Programs	May Yet Be Purchased Under the Plans or Programs
January 1 – 31, 2014		-	\$ -	-	\$ 240,307,656
February 1 – 28, 2014		-	-	-	240,307,656
March 1 – 31, 2014		157,891	24.34	157,891	236,464,320
	Total for or as of the end of the quarter ended March 31, 2014	157,891	\$ 24.34	157,891	\$ 236,464,320

The following is additional information with respect to the Common Share authorization:

- i. The date the program was announced was August 2, 2013 by Form 8-K.
- ii. The amount approved was up to \$250 million in aggregate purchase price of TDS Common Shares.
- iii. The program does not have an expiration date.
- iv. The authorization did not expire during the first quarter of 2014.
- v. TDS did not determine to terminate the foregoing Common Share repurchase program, or cease making further purchases thereunder, during the first quarter of 2014.

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**Item 5. Other Information.**

The following information is being provided to update prior disclosures made pursuant to the requirements of Form 8-K, Item 2.03 — Creation of a Direct Financial Obligation or an Obligation Under an Off-Balance Sheet Arrangement of a Registrant.

Neither TDS nor U.S. Cellular borrowed or repaid any amounts under their revolving credit facilities in the first quarter of 2014 and had no borrowings outstanding under their revolving credit facilities as of March 31, 2014.

A description of TDS' revolving credit facility is included under Item 1.01 in TDS' Current Report on Form 8-K dated December 17, 2010 and is incorporated by reference herein.

A description of U.S. Cellular's revolving credit facility is included under Item 1.01 in U.S. Cellular's Current Report on Form 8-K dated December 17, 2010 and is incorporated by reference herein.

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**Item 6. Exhibits.**

Exhibit 10.1 — Form of U.S. Cellular Long-Term Incentive Plan Restricted Stock Unit Award Agreement for Kenneth R. Meyers, is hereby incorporated by reference to Exhibit 10.1 to U.S. Cellular's Quarterly Report on Form 10-Q for the quarter ended March 31, 2014.

Exhibit 10.2 — Form of U.S. Cellular's Long-Term Incentive Plan Stock Option Award Agreement for Kenneth R. Meyers, is hereby incorporated by reference to Exhibit 10.2 to U.S. Cellular's Quarterly Report on Form 10-Q for the quarter ended March 31, 2014.

Exhibit 10.3 — Amendment Number One to TDS' 2011 Long-Term Incentive Plan is hereby incorporated by reference to Exhibit A to the TDS Notice of Annual Meeting of Shareholders and Proxy Statement dated April 18, 2014.

Exhibit 11 — Statement regarding computation of per share earnings is included herein as Note 4 — Earnings Per Share in the Notes to Consolidated Financial Statements.

Exhibit 12 — Statement regarding computation of ratio of earnings to fixed charges.

Exhibit 31.1 — Principal executive officer certification pursuant to Rule 13a-14 of the Securities Exchange Act of 1934.

Exhibit 31.2 — Principal financial officer certification pursuant to Rule 13a-14 of the Securities Exchange Act of 1934.

Exhibit 32.1 — Principal executive officer certification pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code.

Exhibit 32.2 — Principal financial officer certification pursuant to Section 1350 of Chapter 63 of Title 18 of the United States Code.

Exhibit 101.INS — XBRL Instance Document

Exhibit 101.SCH — XBRL Taxonomy Extension Schema Document

Exhibit 101.PRE — XBRL Taxonomy Presentation Linkbase Document

Exhibit 101.CAL — XBRL Taxonomy Calculation Linkbase Document

Exhibit 101.LAB — XBRL Taxonomy Label Linkbase Document

Exhibit 101.DEF — XBRL Taxonomy Extension Definition Linkbase Document

The foregoing exhibits include only the exhibits that relate specifically to this Form 10-Q or that supplement the exhibits identified in TDS' Form 10-K for the year ended December 31, 2013. Reference is made to TDS' Form 10-K for the year ended December 31, 2013 for a complete list of exhibits, which are incorporated herein except to the extent supplemented or superseded above.

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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.

		TELEPHONE AND DATA SYSTEMS, INC.	
		(Registrant)	
Date:	May 2, 2014	/s/ LeRoy T. Carlson, Jr.	
		LeRoy T. Carlson, Jr.,  President and Chief Executive Officer  (principal executive officer)	
Date:	May 2, 2014	/s/ Douglas D. Shuma	
		Douglas D. Shuma,  Senior Vice President and Controller  (principal financial officer and principal accounting officer)	

