UNITED STATES CELLULAR CORP
Form 10-Q
November 06, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2007 OR

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

For the transition period from to

Commission File Number 1-9712

UNITED STATES CELLULAR CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**62-1147325**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

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

(Address of principal executive offices) (Zip Code)

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

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

Yes x No o

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

Large accelerated filer x Accelerated filer o Accelerated filer o

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

Yes o No x

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

Class	Outstanding at September 30, 2007
Common Shares, $1 par value	54,707,492 Shares

Series A Common Shares, $1 par value	33,005,877 Shares

UNITED STATES CELLULAR CORPORATION

QUARTERLY REPORT ON FORM 10-Q

FOR THE PERIOD ENDED SEPTEMBER 30, 2007

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PART I. FINANCIAL INFORMATION

ITEM I. FINANCIAL STATEMENTS

UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

UNAUDITED

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
	(Dollars in thousands, except per share amounts)			
OPERATING REVENUES				
Service	$ 954,540	$ 821,820	$ 2,721,341	$ 2,382,747
Equipment sales	61,294	66,703	200,813	188,289
Total Operating Revenues	1,015,834	888,523	2,922,154	2,571,036
OPERATING EXPENSES				
System operations (excluding Depreciation, amortization and accretion shown separately below)	185,479	165,107	529,172	468,980
Cost of equipment sold	164,662	140,757	470,356	417,489
Selling, general and administrative (including charges from affiliates of $31.4 million and $28.2 million for the three months ended September 30, 2007 and 2006, respectively, and $90.1 million and $77.8 million for the nine months ended September 30, 2007 and 2006, respectively)	414,978	358,392	1,141,803	1,028,865
Depreciation, amortization and accretion	149,776	146,940	447,889	429,451
Total Operating Expenses	914,895	811,196	2,589,220	2,344,785
OPERATING INCOME	100,939	77,327	332,934	226,251
INVESTMENT AND OTHER INCOME (EXPENSE)				
Equity in earnings of unconsolidated entities	23,782	23,483	69,860	64,923
Interest and dividend income	3,395	601	8,598	10,996
Fair value adjustment of derivative instruments		(21,285)	(5,388)	(17,392)
Gain on sale of investments			131,686	
Interest expense	(19,625)	(23,974)	(64,634)	(70,189)
Other, net	179	(225)	(315)	(163)
Total Investment and Other Income (Expense)	7,731	(21,400)	139,807	(11,825)
INCOME BEFORE INCOME TAXES AND MINORITY INTEREST	108,670	55,927	472,741	214,426
Income tax expense	41,154	15,510	176,542	77,903

INCOME BEFORE MINORITY INTEREST		67,516		40,417		296,199		136,523
Minority share of income		(3,961)		(4,542)		(10,672)		(11,138)
NET INCOME	$	63,555	$	35,875	$	285,527	$	125,385
BASIC WEIGHTED AVERAGE SHARES OUTSTANDING (000s)		87,757		87,281		87,743		87,258
BASIC EARNINGS PER SHARE	$	0.72	$	0.41	$	3.25	$	1.44
DILUTED WEIGHTED AVERAGE SHARES OUTSTANDING (000s)		88,589		88,092		88,680		88,071
DILUTED EARNINGS PER SHARE	$	0.72	$	0.41	$	3.22	$	1.42

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

UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

UNAUDITED

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006
	(Dollars in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 285,527	$ 125,385
Add (deduct) adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and accretion	447,889	429,451
Bad debts expense	46,539	43,787
Stock-based compensation expense	11,383	16,134
Deferred income taxes, net	(10,756)	(30,714)
Equity in earnings of unconsolidated entities	(69,860)	(64,923)
Distributions from unconsolidated entities	47,595	39,374
Minority share of income	10,672	11,138
Unrealized fair value adjustment for derivative instruments	5,388	17,392
Gain on sale of assets	(5,000)	
Gain on sale of investments	(131,686)	
Noncash interest expense	1,333	1,335
Other operating activities		244
Changes in assets and liabilities from operations:		
Change in accounts receivable	(72,684)	(74,401)
Change in inventory	4,224	16,084
Change in accounts payable - trade	2,873	(41,396)
Change in accounts payable - affiliate	(4,393)	3,826
Change in customer deposits and deferred revenues	20,413	7,813
Change in accrued taxes	27,928	9,145
Change in accrued interest	8,595	9,226
Change in other assets and liabilities	(8,560)	(19,262)
	617,420	499,638
CASH FLOWS (USED IN) INVESTING ACTIVITIES		
Additions to property, plant and equipment	(377,399)	(421,378)
Proceeds from sale of investments	4,301	
Proceeds from return of investment		28,650
Cash received from divestitures	4,277	
Cash paid for acquisitions	(18,283)	(98,581)
Other investing activities	(1,346)	(3,256)
	(388,450)	(494,565)
CASH FLOWS FROM/(USED IN) FINANCING ACTIVITIES		
Issuance of notes payable	25,000	390,000
Repayment of notes payable	(60,000)	(375,000)
Common shares reissued	16,474	3,856
Common shares repurchased	(65,202)	
Capital (distributions) to minority partners	(7,508)	(14,371)

Excess tax benefit from exercise of stock awards		11,374		349
		(79,862)		4,834
NET INCREASE IN CASH AND CASH EQUIVALENTS		149,108		9,907
CASH AND CASH EQUIVALENTS				
Beginning of period		32,912		29,003
End of period	$	182,020	$	38,910

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

UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

ASSETS

UNAUDITED

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
CURRENT ASSETS		
Cash and cash equivalents	$ 182,020	$ 32,912
Accounts receivable		
Customers, less allowance of $12,581 and $12,027, respectively	329,547	305,475
Roaming	39,941	30,396
Other, less allowance of $427 and $989, respectively	60,196	71,567
Marketable equity securities	16,133	249,039
Inventory	113,078	117,189
Prepaid expenses	46,634	34,955
Net deferred tax assets	1,328	
Other current assets	12,229	13,385
	801,106	854,918
INVESTMENTS		
Licenses	1,500,092	1,494,327
Goodwill	491,316	485,452
Customer lists, net of accumulated amortization of $78,425 and $68,110, respectively	17,442	26,196
Marketable equity securities		4,873
Investments in unconsolidated entities	176,557	150,325
Notes and interest receivable long-term	4,452	4,541
	2,189,859	2,165,714
PROPERTY, PLANT AND EQUIPMENT		
In service and under construction	5,414,358	5,120,994
Less accumulated depreciation	2,844,527	2,492,146
	2,569,831	2,628,848
OTHER ASSETS AND DEFERRED CHARGES	28,658	31,136
TOTAL ASSETS	$ 5,589,454	$ 5,680,616

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

UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

LIABILITIES AND SHAREHOLDERS EQUITY

UNAUDITED

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
CURRENT LIABILITIES		
Notes payable	$	$ 35,000
Prepaid forward contracts		159,856
Accounts payable		
Affiliate	9,175	13,568
Trade	244,176	241,303
Customer deposits and deferred revenues	143,923	123,344
Accrued taxes	46,641	26,913
Derivative liability		88,840
Net deferred income tax liability		26,326
Accrued compensation	50,801	47,842
Other current liabilities	103,338	93,718
	598,054	856,710
DEFERRED LIABILITIES AND CREDITS		
Net deferred income tax liability	555,075	601,535
Asset retirement obligation	123,466	127,639
Other deferred liabilities and credits	81,059	62,914
	759,600	792,088
LONG-TERM DEBT		
Long-term debt	1,002,180	1,001,839
COMMITMENTS AND CONTINGENCIES		
MINORITY INTEREST	41,898	36,700
COMMON SHAREHOLDERS EQUITY		
Common Shares, par value $1 per share; authorized 140,000,000 shares; issued 55,045,685 shares	55,046	55,046
Series A Common Shares, par value $1 per share; authorized 50,000,000 shares; issued and outstanding 33,005,877 shares	33,006	33,006
Additional paid-in capital	1,319,038	1,290,829
Treasury Shares, at cost, 338,193 and 329,934 Common Shares, respectively	(28,601)	(14,462)
Accumulated other comprehensive income	10,009	80,382
Retained earnings	1,799,224	1,548,478
	3,187,722	2,993,279
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$ 5,589,454	$ 5,680,616

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

UNITED STATES CELLULAR CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accounting policies of United States Cellular Corporation (U.S. Cellular) conform to accounting principles generally accepted in the United States of America (U.S. GAAP). The consolidated financial statements include the accounts of U.S. Cellular, its majority-owned subsidiaries since acquisition, general partnerships in which U.S. Cellular has a majority partnership interest and any entity in which U.S. Cellular has a variable interest that requires U.S. Cellular to recognize a majority of the entity s expected gains or losses. All material intercompany accounts and transactions have been eliminated. Certain prior year amounts have been reclassified to conform to the 2007 presentation.

The consolidated financial statements included herein have been prepared by U.S. Cellular, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. However, U.S. Cellular believes that the disclosures included herein are adequate to make the information presented not misleading. It is suggested that these consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in U.S. Cellular s Annual Report on Form 10-K for the year ended December 31, 2006 (Form 10-K).

The accompanying unaudited consolidated financial statements contain all adjustments (consisting of only normal recurring items unless otherwise disclosed) necessary to present fairly the financial position as of September 30, 2007 and December 31, 2006, the results of operations for the three and nine months ended September 30, 2007 and 2006, and the cash flows for the nine months ended September 30, 2007 and 2006. The results of operations for the three and nine months ended September 30, 2007 are not necessarily indicative of the results to be expected for the full year.

2. Summary of Significant Accounting Policies

Pension Plan

U.S. Cellular participates in a qualified noncontributory defined contribution pension plan sponsored by Telephone and Data Systems, Inc. (TDS), U.S. Cellular s parent organization. The plan provides pension benefits for the employees of U.S. Cellular and its subsidiaries. Under this plan, pension benefits and costs are calculated separately for each participant and are funded currently. Pension costs were $2.6 million and $6.8 million for the three and nine months ended September 30, 2007, respectively, and $2.1 million and $6.5 million for the three and nine months ended September 30, 2006, respectively.

Amounts Collected from Customers and Remitted to Governmental Authorities

U.S. Cellular records amounts collected from customers and remitted to governmental authorities net within a tax liability account if the tax is assessed upon the customer and U.S. Cellular merely acts as an agent in collecting the tax on behalf of the imposing governmental authority. If the tax is assessed upon U.S. Cellular, 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 on the Consolidated Statements of Operations. The amounts recorded gross in revenues that are billed to customers and remitted to governmental authorities totaled $35.3 million and $96.1 million for the three and nine months ended September 30, 2007, respectively, and $21.3 million and $60.6 million for the three and nine months ended September 30, 2006, respectively.

Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value as used in numerous accounting pronouncements, establishes a framework for measuring fair value in U.S. GAAP, and expands disclosures related to the use of fair value measures in financial statements. SFAS 157 does not expand the use of fair value measurements in financial statements, but standardizes its definition and guidance in U.S. GAAP. SFAS 157 emphasizes that fair value is a market-based measurement and not an entity-specific measurement, based on an exchange transaction in which the entity sells an asset or transfers a liability (exit price). SFAS 157 establishes a fair value hierarchy, from observable market data as the highest level to an entity s own fair value assumptions as the lowest level. SFAS 157 is effective for U.S. Cellular s 2008 financial statements. U.S. Cellular is currently reviewing the requirements of SFAS 157 and has not determined the impact, if any, on its financial position or results of operations.

In September 2006, the FASB ratified Emerging Issues Task Force Issue No. 06-1, *Accounting for Consideration Given by a Service Provider to Manufacturers or Resellers of Equipment Necessary for an End-Customer to Receive Service from the Service Provider* (EITF 06-1). This guidance requires the application of EITF 01-9, *Accounting for Consideration Given by a Vendor to a Customer* (EITF 01-9), when consideration is given to a reseller or manufacturer for benefit to the service provider s end customer. EITF 01-9 requires that the consideration given be recorded as a liability at the time of the sale of the equipment and also provides guidance for the classification of the expense. EITF 06-1 is effective for U.S. Cellular s 2008 financial statements. U.S. Cellular is currently reviewing the requirements of EITF 06-1 and has not yet determined the impact, if any, on its financial position or results of operations.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities, Including an Amendment of FASB Statement No. 115* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value at specified election dates. Unrealized gains and losses on items for which the fair value option has been elected shall be reported in earnings at each subsequent reporting date. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for U.S. Cellular s 2008 financial statements. U.S. Cellular is currently reviewing the requirements of SFAS 159 and has not yet determined the impact, if any, on its financial position or results of operations.

3. Acquisitions, Divestitures and Exchanges

U.S. Cellular assesses its existing wireless interests on an ongoing basis with a goal of improving the competitiveness of its operations and maximizing its long-term return on investment. As part of this strategy, U.S. Cellular reviews attractive opportunities to acquire additional operating markets and wireless spectrum. In addition, U.S. Cellular may seek to divest outright or include in exchanges for other interests those markets and interests that are not strategic to its long-term success.

On February 1, 2007, U.S. Cellular purchased 100% of the membership interests of Iowa 15 Wireless, LLC (Iowa 15) and obtained the 25 megahertz Federal Communications Commission (FCC) cellular license to provide wireless service in Iowa Rural Service Area (RSA) 15 for approximately $18.2 million in cash. This acquisition increased investments in licenses, goodwill and customer lists by $7.9 million, $5.9 million and $1.6 million, respectively. The goodwill of $5.9 million is deductible for income tax purposes.

U.S. Cellular is a limited partner in Barat Wireless, L.P. (Barat Wireless), an entity which participated in the auction of wireless spectrum designated by the FCC as Auction 66. Barat Wireless was qualified to receive a 25% discount available to very small businesses which were defined as having annual gross revenues of less than $15 million. At the conclusion of the auction on September 18, 2006, Barat Wireless was the high bidder with respect to 17 licenses and had bid $127.1 million, net of its discount. On April 30, 2007, the FCC granted Barat Wireless applications with respect to the 17 licenses for which it was the winning bidder.

Barat Wireless is in the process of developing its long-term business and financing plans. As of September 30, 2007, U.S. Cellular had made capital contributions and advances to Barat Wireless and/or its general partner of $127.2 million, which are included in Licenses in the Consolidated Balance Sheets. Barat Wireless used the funding to pay the FCC an initial deposit of $79.9 million on July 14, 2006 to allow it to participate in Auction 66. On October 18, 2006, Barat Wireless paid the balance due at the conclusion of the auction for the licenses with respect to which Barat Wireless was the high bidder; such amount totaled $47.2 million. For financial statement purposes, U.S. Cellular consolidates Barat Wireless and Barat Wireless, Inc., the general partner of Barat Wireless, pursuant to the guidelines of FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities*, an interpretation of ARB No. 51, (FIN 46(R)), as U.S. Cellular anticipates benefiting from or absorbing a majority of Barat Wireless expected gains or losses. Pending finalization of Barat Wireless permanent financing plan, and upon request by Barat Wireless, U.S. Cellular may agree to make additional capital contributions and advances to Barat Wireless and/or its general partner.

In October 2006, Midwest Wireless Communications, L.L.C. (Midwest Wireless) was sold to ALLTEL Corporation. In connection with the sale, U.S. Cellular became entitled to receive approximately $106.0 million in cash with respect to its interest in Midwest Wireless. Of this amount, $95.1 million was distributed upon closing and $10.9 million was held in escrow to secure certain true-up, indemnification and other possible adjustments; the funds held in escrow were to be distributed in installments over a period of four to fifteen months following the closing. During the first nine months of 2007, U.S. Cellular received $4.3 million of funds that were distributed from the aforementioned escrow. At September 30, 2007, the amount which U.S. Cellular might be entitled to receive from the escrow in future periods was $6.6 million, excluding accrued interest income.

In April 2006, U.S. Cellular purchased the remaining ownership interest in a Tennessee wireless market, in which it had previously owned a 16.7% interest, for approximately $18.8 million in cash. This acquisition increased investments in licenses, goodwill and customer lists by $5.5 million, $4.0 million and $2.0 million, respectively. The $4.0 million of goodwill is not deductible for income tax purposes.

U.S. Cellular is a limited partner in Carroll Wireless L.P. (Carroll Wireless), an entity which participated in the auction of wireless spectrum designated by the FCC as Auction 58. Carroll Wireless was qualified to bid on closed licenses that were available only to companies included under the FCC definition of entrepreneurs, which are small businesses that have a limited amount of assets and revenues. In addition, Carroll Wireless bid on open licenses that were not subject to restriction. With respect to these licenses, however, Carroll Wireless was qualified to receive a 25% discount available to very small businesses which were defined as having average annual gross revenues of less than $15 million. Carroll Wireless was a successful bidder for 17 license areas in Auction 58, which ended on February 15, 2005. The aggregate amount paid to the FCC for the 17 licenses was $129.9 million, net of the discounts to which Carroll Wireless was entitled. These 17 license areas cover portions of 12 states and are in markets which are either adjacent to or overlap current U.S. Cellular licensed areas. On January 6, 2006, the FCC granted Carroll Wireless applications with respect to 16 of the 17 licenses for which it had been the successful bidder and dismissed one application, relating to Walla Walla, Washington. Following the completion of Auction 58, the FCC determined that a portion of the Walla Walla license was already licensed to another party and should not have been included in Auction 58. Accordingly, in 2006, Carroll Wireless received a full refund of the $0.2 million previously paid to the FCC with respect to the Walla Walla license.

Carroll Wireless is in the process of developing its long-term business and financing plans. As of September 30, 2007, U.S. Cellular had made capital contributions and advances to Carroll Wireless and/or its general partner of approximately $129.9 million; $129.7 million of this amount is included in Licenses in the Consolidated Balance Sheets. For financial statement purposes, U.S. Cellular consolidates Carroll Wireless and Carroll PCS, Inc., the general partner of Carroll Wireless, pursuant to the guidelines of FIN 46(R), as U.S. Cellular anticipates benefiting from or absorbing a majority of Carroll Wireless expected gains or losses. Pending finalization of Carroll Wireless permanent financing plan, and upon request by Carroll Wireless, U.S. Cellular may make additional capital contributions and advances to Carroll Wireless and/or its general partner. U.S. Cellular has approved additional funding of $1.4 million of which $0.1 million was provided to Carroll Wireless as of September 30, 2007.

4. Gain on Sale of Assets

In December 2006, U.S. Cellular entered into an agreement to sell $226.0 million face amount of accounts receivable written off in previous periods; the proceeds from the sale were $5.9 million. The agreement transferred all rights, title, and interest in the account balances, along with the right to collect all amounts due, to the buyer. The sale was subject to a 180-day period in which the buyer was entitled to request a refund for unenforceable accounts. The transaction was recognized as a sale during the fourth quarter of 2006 in accordance with the provisions of FASB Statement of Financial Accounting Standards No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities,* with the gain deferred until expiration of the recourse period. During the second quarter of 2007, U.S. Cellular recognized a gain of $5.0 million, net of refunds for unenforceable accounts. The gain is included in Selling, general and administrative expenses on the Consolidated Statements of Operations. All expenses related to the transaction were recognized in the period incurred.

5. Fair Value Adjustments of Derivative Instruments

Fair value adjustments of derivative instruments, all of which matured in May 2007, resulted in a loss of $5.4 million in the nine months ended September 30, 2007, and a loss of $21.3 million and $17.4 million in the three and nine months ended September 30, 2006, respectively. Because all forward contracts were settled in May 2007, U.S. Cellular did not have any fair value adjustment of derivative instruments in the three months ended September 30, 2007. Fair value adjustments of derivative instruments for the period reflect the change in the fair value of the bifurcated embedded collars within the forward contracts related to the Vodafone marketable equity securities not designated as a hedge. See Note 11 Marketable Equity Securities and Forward Contracts and Note 15 Long-Term Debt and Forward Contracts for additional information related to the forward contracts.

6. Income Taxes

The overall effective tax rate on income before income taxes and minority interest for the three and nine months ended September 30, 2007 was 37.9% and 37.3%, respectively, and 27.7% and 36.3% for the three and nine months ended September 30, 2006, respectively. The effective tax rates for the 2007 periods are higher than 2006 primarily due to the favorable resolution of state audits in 2006.

Effective January 1, 2007, U.S. Cellular adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). In accordance with FIN 48, U.S. Cellular recognized a cumulative-effect adjustment of $1.3 million, increasing its liability for unrecognized tax benefits, interest, and penalties and reducing the January 1, 2007 balance of Retained earnings.

At January 1, 2007, U.S. Cellular had $25.8 million in unrecognized tax benefits, which, if recognized, would reduce income tax expense by $12.6 million, net of the federal benefit from state income taxes. Included in the balance of unrecognized tax benefits at January 1, 2007, is an immaterial amount related to tax positions for which it is possible that the total amounts could change during the next twelve months. At September 30, 2007 U.S. Cellular had $30.1 million in unrecognized tax benefits, which, if recognized, would reduce income tax expense by $15.4 million, net of the federal benefit from state income taxes.

U.S. Cellular recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. This amount totaled $1.4 million and $3.6 million for the three and nine months ended September 30, 2007, respectively. Accrued interest and penalties were $6.2 million and $9.8 million as of January 1, 2007 and September 30, 2007, respectively.

U.S. Cellular is included in a consolidated federal income tax return with other members of the TDS consolidated group. TDS and U.S. Cellular are parties to a Tax Allocation Agreement which provides that U.S. Cellular and its subsidiaries be included with the TDS affiliated group in a consolidated federal income tax return and in state income or franchise tax returns in certain situations. For financial statement purposes, U.S. Cellular and its subsidiaries calculate their income, income taxes and credits as if they comprised a separate affiliated group. Under the Tax Allocation Agreement, U.S. Cellular remits its applicable income tax payments to TDS. U.S. Cellular had a tax payable balance to TDS of $5.0 million as of September 30, 2007 and $3.7 million as of December 31, 2006.

As discussed above, U.S. Cellular is included in TDS consolidated federal income tax return; U.S. Cellular also files various state and local income tax returns. With few exceptions, U.S. Cellular is no longer subject to federal, state and local income tax examinations by tax authorities for years prior to 2002. TDS consolidated federal income tax returns for the years 2002 - 2005, which include U.S. Cellular, are currently under examination by the Internal Revenue Service. U.S. Cellular and its subsidiaries are also under examination by various state taxing authorities.

7. Earnings per Share

Basic earnings per share is computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed by dividing net income by the weighted average common shares adjusted to include the effect of potentially dilutive securities.

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

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	**2006**	**2007**	**2006**
	(Dollars and shares in thousands, except earnings per share)			
Net income	$ 63,555	$ 35,875	$ 285,527	$ 125,385
Weighted average number of common shares used in basic earnings per share	87,757	87,281	87,743	87,258
Effect of stock options (1)	500	692	622	668
Effect of Restricted Stock Units	199	119	182	145
Effect of assuming shares delivered upon settlement of Accelerated Share Repurchase (2)	133		133	
Weighted average number of common shares used in diluted earnings per share	88,589	88,092	88,680	88,071
Basic Earnings per Share	$ 0.72	$ 0.41	$ 3.25	$ 1.44
Diluted Earnings per Share	$ 0.72	$ 0.41	$ 3.22	$ 1.42

(1) Stock options convertible into 4,000 and 10,000 Common Shares in the three and nine months ended September 30, 2007, respectively, and 200,000 and 765,000 Common Shares in the three and nine months ended September 30, 2006, respectively, were not included in computing Diluted Earnings per Share because their effects were antidilutive.

(2) See Note 18 - Common Share Repurchase Program below for a discussion of U.S. Cellular s purchase of 838,000 of its Common Shares from an investment banking firm in private transactions pursuant to accelerated share repurchase agreements.

8. Supplemental Cash Flow Disclosures Non-Cash Financing Activities; Gain on Sale of Marketable Equity Securities

During the second quarter of 2007, U.S. Cellular delivered 8,815,475 American Depositary Receipts (ADRs) of Vodafone Group, Plc (Vodafone) with a fair market value of $254.1 million to settle the $159.9 million principal amount of prepaid forward contracts and $94.2 million of related derivative liability.

Upon settlement of the prepaid forward contracts and related derivative liability, U.S. Cellular disposed of its remaining 149,223 Vodafone ADRs. U.S. Cellular recorded a gain of $131.7 million in the second quarter of 2007 on the settlement of the prepaid forward contracts and the related derivative liability and the disposition of remaining Vodafone ADRs.

See Note 11 Marketable Equity Securities and Forward Contracts and Note 15 Long-Term Debt and Forward Contracts for additional information related to the Vodafone ADRs and prepaid forward contracts.

In the nine months ended September 30, 2007, U.S. Cellular withheld 544,000 Common Shares aggregating $43.5 million for the payment of the exercise price and income taxes from employees who exercised stock options or who received vested stock awards.

9. Licenses and Goodwill

U.S. Cellular has substantial amounts of licenses and goodwill as a result of the acquisition of wireless markets. The changes in licenses and goodwill for the nine months ended September 30, 2007 and 2006 were as follows:

		September 30, 2007		September 30, 2006
		(Dollars in thousands)		
Licenses				
Balance, beginning of period	$	1,494,327	$	1,362,263
Acquisitions		7,901		5,534
Impairment		(2,136)		
Other (1)				79,772
Balance, end of period	$	1,500,092	$	1,447,569

(1) Includes $79.9 million representing deposits made to the FCC for Barat Wireless licenses with respect to which Barat Wireless was the high bidder in Auction 66.

		September 30, 2007		September 30, 2006
		(Dollars in thousands)		
Goodwill				
Balance, beginning of period	$	485,452	$	481,235
Acquisitions		5,864		3,932
Other adjustments				318
Balance, end of period	$	491,316	$	485,485

See Note 3 Acquisitions, Divestitures and Exchanges for additional information related to transactions which affected licenses and goodwill.

Licenses and goodwill must be reviewed for impairment annually or more frequently if events or changes in circumstances indicate that the asset might be impaired. U.S. Cellular performs the annual impairment review on licenses and goodwill during the second quarter of its fiscal year. Accordingly, the annual impairment tests for licenses and goodwill for 2007 and 2006 were performed in the second quarter of 2007 and 2006. Such impairment tests indicated that there was an impairment of licenses totaling $2.1 million in 2007; the loss is included in Depreciation, amortization and accretion on the Consolidated Statements of Operations. There was no impairment of licenses in 2006, and no impairment of goodwill in either 2007 or 2006.

U.S. Cellular s license impairments in 2007 were related to two of its six units of accounting in which operations have not yet begun. The carrying values of licenses associated with these six units of accounting are tested separately from those associated with U.S. Cellular s operating licenses. Fair values for such units of accounting were determined by reference to values established by auctions and other market transactions involving licenses comparable to those included in each specific unit of accounting.

10. Customer Lists

Customer lists, which are intangible assets resulting from acquisitions of wireless markets, are amortized based on average customer retention periods using the double declining balance method in the first year, switching to straight-line over the remaining estimated life. The changes in the customer lists for the nine months ended September 30, 2007 and 2006 were as follows:

	September 30, 2007	September 30, 2006
	(Dollars in thousands)	
Customer Lists		
Balance, beginning of period	$ 26,196	$ 47,649
Acquisitions	1,560	2,042
Impairment	(1,947)	
Amortization	(8,367)	(17,643)
Balance, end of period	$ 17,442	$ 32,048

U.S. Cellular performs an annual impairment test of customer list balances in the third quarter of its fiscal year. During the third quarter of 2007, such test indicated that the carrying value of certain customer list balances exceeded their estimated fair values and an impairment loss of $1.9 million was recorded; the loss is included in Depreciation, amortization and accretion on the Consolidated Statements of Operations. Fair values were determined based upon a present value analysis of expected future cash flows. There was no impairment of customer lists in 2006.

Based on the customer list balance as of September 30, 2007, amortization expense for the fourth quarter of 2007 and for the years 2008-2012 is expected to be $2.1 million, $7.1 million, $4.7 million, $3.2 million, $0.3 million and $0.1 million, respectively.

11. Marketable Equity Securities and Forward Contracts

U.S. Cellular holds marketable equity securities that are publicly traded and can have volatile movements in share prices. Any increase or decrease in the fair value of the underlying marketable securities is reflected in Accumulated other comprehensive income on the balance sheet rather than as a non-operating gain or loss in the Consolidated Statements of Operations. U.S. Cellular does not make direct investments in publicly traded companies and all of these interests were acquired as a result of sales, trades or reorganizations of other assets.

Information regarding U.S. Cellular s marketable equity securities is summarized below.

	September 30, 2007	December 31, 2006
	(Dollars in thousands)	
Marketable Equity Securities Current Assets		
Vodafone Group Plc 8,964,698 American Depositary Receipts in 2006	$	$ 249,039
Rural Cellular Corporation 370,882 Common Shares in 2007	16,133	
Total Marketable Equity Securities Current	16,133	249,039
Marketable Equity Securities Investments		
Rural Cellular Corporation 370,882 Common Shares in 2006		4,873
Total aggregate fair value	16,133	253,912
Accounting cost basis	334	131,512
Gross unrealized holding gains	15,799	122,400
Deferred income tax liability	(5,790)	(44,855)
Net unrealized holding gains	10,009	77,545
Derivative instruments, net of tax		2,837
Accumulated other comprehensive income	$ 10,009	$ 80,382

The investment in Vodafone resulted from certain dispositions of non-strategic wireless investments to, or settlements with, AirTouch Communications, Inc. (AirTouch), in exchange for stock of AirTouch, which was then acquired by Vodafone whereby U.S. Cellular received ADRs representing Vodafone stock.

U.S. Cellular entered into a number of forward contracts related to the Vodafone ADRs that it held. The economic hedge risk management objective of the forward contracts was to hedge the value of the securities from losses due to decreases in the market prices of the securities while retaining a share of gains from increases in the market prices of such securities. The downside risk was hedged at or above the accounting cost basis of the securities.

The forward contracts related to the Vodafone ADRs matured in May 2007. U.S. Cellular delivered Vodafone ADRs in settlement of the forward contracts and disposed of all remaining Vodafone ADRs in connection therewith. As a result, U.S. Cellular no longer owns any Vodafone ADRs and no longer has any liability or other obligations under the related forward contracts. U.S. Cellular recorded a pre-tax gain of $131.7 million on the settlement of the forward contracts and the disposition of the remaining Vodafone ADRs.

See Note 15 Long-term Debt and Forward Contracts for additional information related to U.S. Cellular s forward contracts.

U.S. Cellular owns 370,882 Common Shares of Rural Cellular Corporation (RCCC). On July 30, 2007, RCCC announced that Verizon Wireless has agreed to purchase the outstanding shares of RCCC for $45 per share in cash. The acquisition is expected to close in the first half of 2008. If the transaction closes, U.S. Cellular will receive approximately $16.7 million in cash, recognize a $16.4 million pre-tax gain and cease to own any interest in RCCC.

12. Unconsolidated Entities

Investments in unconsolidated entities consist of amounts invested in wireless entities in which U.S. Cellular holds a minority interest. These investments are accounted for using either the equity or cost method.

U.S. Cellular s significant investments in unconsolidated entities include the following:

	September 30, 2007	September 30, 2006
Los Angeles SMSA Limited Partnership	5.5%	5.5%
Midwest Wireless Communications, L.L.C. (1)		14.2%
North Carolina RSA 1 Partnership	50.0%	50.0%
Oklahoma City SMSA Limited Partnership	14.6%	14.6%

(1) In addition, U.S. Cellular owns a 49% interest in an entity which owned an interest of approximately 2.9% in Midwest Wireless Holdings, L.L.C., the parent company of Midwest Wireless Communications, L.L.C. The entity s investment in Midwest Wireless Holdings L.L.C. was disposed of in the fourth quarter of 2006.

Based primarily on data furnished to U.S. Cellular by third parties, the following table summarizes the combined results of operations of U.S. Cellular s equity method investments:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
	(Dollars in thousands)			
Results of Operations				