TELEPHONE & DATA SYSTEMS INC /DE/
Form 10-Q
May 01, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2015

OR

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

For the transition period from to

Commission file number 001-14157

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.)

30 North LaSalle Street, Suite 4000, Chicago, Illinois 60602

(Address of principal executive offices) (Zip code)

Registrant’s telephone number, including area code: (312) 630-1900

Indicate by check mark	**Yes**	**No**
• 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.

Class	**Outstanding at March 31, 2015**
Common Shares, $0.01 par value	100,853,104 Shares
Series A Common Shares, $0.01 par value	7,188,071 Shares

Telephone and Data Systems, Inc.

Quarterly Report on Form 10-Q
For the Quarterly Period Ended March 31, 2015

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Part I. Financial Information

Item 1. Financial Statements

Telephone and Data Systems, Inc.

Consolidated Statement of Operations

(Unaudited)

	Three Months Ended March 31, 2015	2014
(Dollars and shares in thousands, except per share amounts)	**2015**	**2014**
Operating revenues		
Service	$ 1,073,091	$ 1,080,242
Equipment and product sales	178,502	115,720
Total operating revenues	1,251,593	1,195,962
Operating expenses		
Cost of services (excluding Depreciation, amortization and accretion reported below)	293,647	275,958
Cost of equipment and products	271,981	306,647
Selling, general and administrative	438,040	463,669
Depreciation, amortization and accretion	206,575	224,919
(Gain) loss on asset disposals, net	5,377	2,430
(Gain) loss on sale of business and other exit costs, net	(123,783)	(6,900)
(Gain) loss on license sales and exchanges, net	(122,873)	(91,446)
Total operating expenses	968,964	1,175,277
Operating income	282,629	20,685
Investment and other income (expense)		
Equity in earnings of unconsolidated entities	34,641	37,327
Interest and dividend income	8,385	2,486
Interest expense	(33,830)	(28,707)
Other, net	(4)	160
Total investment and other income (expense)	9,192	11,266
Income before income taxes	291,821	31,951
Income tax expense	116,020	11,657
Net income	175,801	20,294
Less: Net income attributable to noncontrolling interests, net of tax	30,061	2,040

Net income attributable to TDS shareholders		145,740			18,254
TDS Preferred dividend requirement		(12)			(12)
Net income available to common shareholders	$	145,728		$	18,242
Basic weighted average shares outstanding		108,169			108,988
Basic earnings per share attributable to TDS shareholders	$	1.35		$	0.17
Diluted weighted average shares outstanding		108,946			109,672
Diluted earnings per share attributable to TDS shareholders	$	1.33		$	0.16
Dividends per share to TDS shareholders	$	0.141		$	0.134
The accompanying notes are an integral part of these consolidated financial statements.					

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Telephone and Data Systems, Inc.

Consolidated Statement of Comprehensive Income

(Unaudited)

	Three Months Ended March 31,	
(Dollars in thousands)	**2015**	**2014**
Net income	$ 175,801	$ 20,294
Net change in accumulated other comprehensive income		
Change in foreign currency translation adjustment	36	(4)
Change related to retirement plan		
Amounts included in net periodic benefit cost for the period		
Amortization of prior service cost	(852)	(911)
Amortization of unrecognized net loss	64	322
	(788)	(589)
Change in deferred income taxes	312	224
Change related to retirement plan, net of tax	(476)	(365)
Net change in accumulated other comprehensive income	(440)	(369)
Comprehensive income	175,361	19,925
Less: Comprehensive income attributable to noncontrolling interest	30,061	2,040
Comprehensive income attributable to TDS shareholders	$ 145,300	$ 17,885

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

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Telephone and Data Systems, Inc.

Consolidated Statement of Cash Flows

(Unaudited)

	Three Months Ended March 31,	
(Dollars in thousands)	**2015**	**2014**
Cash flows from operating activities		
Net income	$ 175,801	$ 20,294
Add (deduct) adjustments to reconcile net income to cash flows from operating activities		
Depreciation, amortization and accretion	206,575	224,919
Bad debts expense	29,849	21,559
Stock-based compensation expense	8,096	6,759
Deferred income taxes, net	(47,466)	(14,510)
Equity in earnings of unconsolidated entities	(34,641)	(37,327)
Distributions from unconsolidated entities	12,988	12,820
(Gain) loss on asset disposals, net	5,377	2,430
(Gain) loss on sale of business and other exit costs, net	(123,783)	(6,900)
(Gain) loss on license sales and exchanges, net	(122,873)	(91,446)
Noncash interest expense	670	506
Other operating activities	-	47
Changes in assets and liabilities from operations		
Accounts receivable	21,240	90,555
Equipment installment plans receivable	(36,498)	2,394
Inventory	95,395	19,656
Accounts payable	(13,592)	(53,403)
Customer deposits and deferred revenues	13,319	(1,447)
Accrued taxes	251,510	(1,634)
Accrued interest	9,460	9,136
Other assets and liabilities	(96,121)	(99,471)
	355,306	104,937
Cash flows from investing activities		
Cash used for additions to property, plant and equipment	(166,461)	(150,890)
Cash paid for acquisitions and licenses	(280,710)	(8,254)
Cash received from divestitures and exchanges	274,131	103,042
Cash received for investments	-	10,000
Other investing activities	2,765	1,623

		(170,275)	(44,479)
Cash flows from financing activities			
Repayment of long-term debt		(247)	(392)
TDS Common Shares reissued for benefit plans, net of tax payments		213	(50)
U.S. Cellular Common Shares reissued for benefit plans, net of tax payments		487	316
Repurchase of TDS Common Shares		-	(3,342)
Repurchase of U.S. Cellular Common Shares		(2,302)	(2,000)
Dividends paid to TDS shareholders		(15,232)	(14,582)
Payment of debt issuance costs		(3,018)	-
Distributions to noncontrolling interests		(225)	(346)
Other financing activities		(1,488)	2,834
		(21,812)	(17,562)
Net increase in cash and cash equivalents		163,219	42,896
Cash and cash equivalents			
Beginning of period		471,901	830,014
End of period	$	635,120	$ 872,910

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

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Telephone and Data Systems, Inc.

Consolidated Balance Sheet — Assets

(Unaudited)

(Dollars in thousands)	March 31, 2015	December 31, 2014
Current assets		
Cash and cash equivalents	$ 635,120	$ 471,901
Accounts receivable		
Due from customers and agents, less allowances of $42,737 and $41,431, respectively	549,146	548,537
Other, less allowances of $1,124 and $1,141, respectively	109,742	135,144
Inventory, net	178,313	273,707
Net deferred income tax asset	92,791	107,686
Prepaid expenses	97,707	86,506
Income taxes receivable	853	113,708
Other current assets	29,132	29,766
	1,692,804	1,766,955
Assets held for sale	29,771	103,343
Investments		
Licenses	1,837,238	1,453,574
Goodwill	771,674	771,352
Franchise rights	244,300	244,300
Other intangible assets, net of accumulated amortization of $138,614 and $133,823, respectively	59,708	64,499
Investments in unconsolidated entities	343,382	321,729
Other investments	485	508
	3,256,787	2,855,962
Property, plant and equipment		
In service and under construction	11,189,882	11,194,044
Less: Accumulated depreciation	7,443,048	7,347,919
	3,746,834	3,846,125
Other assets and deferred charges	270,042	334,554

Total assets	$ 8,996,238		$ 8,906,939

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

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Telephone and Data Systems, Inc.

Consolidated Balance Sheet — Liabilities and Equity

(Unaudited)

(Dollars and shares in thousands)	March 31, 2015	December 31, 2014
Current liabilities		
Current portion of long-term debt	$ 805	$ 808
Accounts payable	312,091	387,125
Customer deposits and deferred revenues	338,076	324,318
Accrued interest	17,376	7,919
Accrued taxes	174,043	46,734
Accrued compensation	68,838	114,549
Other current liabilities	145,871	181,803
	1,057,100	1,063,256
Liabilities held for sale	406	21,643
Deferred liabilities and credits		
Net deferred income tax liability	878,809	941,519
Other deferred liabilities and credits	441,745	430,774
Long-term debt	1,993,457	1,993,586
Commitments and contingencies	-	-
Noncontrolling interests with redemption features	6,619	1,150
Equity		
TDS shareholders' equity		
Series A Common and Common Shares		
Authorized 290,000 shares (25,000 Series A Common and 265,000 Common Shares)		
Issued 132,758 shares (7,188 Series A Common and 125,570 Common Shares) and 132,749 shares (7,179 Series A Common and 125,570 Common Shares), respectively		
Outstanding 108,041 shares (7,188 Series A Common and 100,853 Common Shares) and 107,899 shares (7,179 Series A Common and 100,720 Common Shares), respectively		
	1,327	1,327

Par Value ($.01 per share) $1,327 ($72 Series A Common and $1,255 Common Shares)				
Capital in excess of par value		2,344,274		2,336,511
Treasury shares at cost:				
24,717 and 24,850 Common Shares, respectively		(745,590)		(748,199)
Accumulated other comprehensive income		6,012		6,452
Retained earnings		2,460,323		2,330,187
Total TDS shareholders' equity		4,066,346		3,926,278
Preferred shares		824		824
Noncontrolling interests		550,932		527,909
Total equity		4,618,102		4,455,011
Total liabilities and equity	$	8,996,238	$	8,906,939
The accompanying notes are an integral part of these consolidated financial statements.				

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Telephone and Data Systems, Inc.

Consolidated Statement of Changes in Equity

(Unaudited)

	TDS Shareholders								
(Dollars in thousands)	Series A Common and Common Shares	Capital in Excess of Par Value	Treasury Common Shares	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total TDS Shareholders' Equity	Preferred Shares	Noncontrolling Interests	Total Equity
December 31, 2014	**$ 1,327**	**$ 2,336,511**	**$ (748,199)**	**$ 6,452**	**$ 2,330,187**	**$ 3,926,278**	**$ 824**	**$ 527,909**	**$ 4,455,011**
Add (Deduct)									
Net income attributable to TDS shareholders	-	-	-	-	145,740	145,740	-	-	145,740
Net income attributable to noncontrolling interests classified as equity	-	-	-	-	-	-	-	24,444	24,444
Change in foreign currency	-	-	-	36	-	36	-	-	36

translation adjustment									
Change related to retirement plan	-	-	-	(476)	-	(476)	-	-	(476)
TDS Common and Series A Common Share dividends	-	-	-	-	(15,220)	(15,220)	-	-	(15,220)
TDS Preferred dividend requirement	-	-	-	-	(12)	(12)	-	-	(12)
Dividend reinvestment plan	-	642	1,757	-	-	2,399	-	-	2,399
Incentive and compensation plans	-	(79)	852	-	(372)	401	-	-	401
Adjust investment in subsidiaries for repurchases, issuances and other compensation plans	-	4,734	-	-	-	4,734	-	(1,344)	3,390

Stock-based compensation awards	-	2,468	-	-	-	2,468	-	-	2,468
Tax windfall (shortfall) from stock awards	-	(2)	-	-	-	(2)	-	-	(2)
Distributions to noncontrolling interests	-	-	-	-	-	-	-	(77)	(77)
March 31, 2015	**$ 1,327**	**$ 2,344,274**	**$ (745,590)**	**$ 6,012**	**$ 2,460,323**	**$ 4,066,346**	**$ 824**	**$ 550,932**	**$ 4,618,102**

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

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Telephone and Data Systems, Inc.

Consolidated Statement of Changes in Equity

(Unaudited)

	TDS Shareholders								
(Dollars in thousands)	Series A Common and Common Shares	Capital in Excess of Par Value	Treasury Common Shares	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total TDS Shareholders' Equity	Preferred Shares	Noncontrolling 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)

translation adjustment									
Change related to retirement plan	-	-	-	(365)	-	(365)	-	-	(365)
TDS Common and Series A Common Share dividends	-	-	-	-	(14,570)	(14,570)	-	-	(14,570)
TDS Preferred dividend requirement	-	-	-	-	(12)	(12)	-	-	(12)
Repurchase of Common Shares	-	-	(3,843)	-	-	(3,843)		-	(3,843)
Dividend reinvestment plan	-	800	1,874	-	-	2,674	-	-	2,674
Incentive and compensation plans	-	(284)	665	-	-	381	-	-	381
Adjust investment in subsidiaries for repurchases, issuances and other	-	2,780	-	-	-	2,780	-	(262)	2,518

compensation plans																	
Stock-based compensation awards		-		2,011		-		-		-		2,011		-		-	2,011
Tax windfall (shortfall) from stock awards		-		(432)		-		-		-		(432)		-		-	(432)
Distributions to noncontrolling interests		-		-		-		-		-		-		-		(325)	(325)
March 31, 2014	**$**	**1,327**	**$**	**2,313,682**	**$**	**(722,658)**	**$**	**(938)**	**$**	**2,533,298**	**$**	**4,124,711**	**$**	**824**	**$**	**552,860**	**$ 4,678,395**

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 subsidiaries in which it has a controlling financial interest, 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, 2014.

TDS’ business segments reflected in this Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2015 are U.S. Cellular, TDS Telecom’s Wireline, Cable, and Hosted and Managed Services (“HMS”) operations. TDS’ non-reportable other business activities are presented as “Corporate, Eliminations and Other”, which includes the operations of TDS’ wholly-owned subsidiaries Suttle-Straus, Inc. (“Suttle-Straus”) and Airadigm Communications, Inc. (“Airadigm”). Suttle-Straus and Airadigm’s financial results were not significant to TDS’ operations. All of TDS’ segments operate only in the United States, except for HMS, which includes an insignificant foreign operation. See Note 12 — 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, 2015 and December 31, 2014, and the results of operations, cash flows, changes in comprehensive income and changes in equity for the three months ended March 31, 2015 and 2014. These results are not necessarily indicative of the results to be expected for the full year.

Recently Issued Accounting Pronouncements

On May 28, 2014, the FASB issued Accounting Standards Update 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"). ASU 2014-09 outlines a single comprehensive model to use in accounting for revenue arising from contracts with customers. This update has an effective date of January 1, 2017. However, on April 1, 2015, the FASB voted to propose a one-year deferral of the effective date of ASU 2014-09. If the proposal is adopted, TDS could elect to adopt the provisions of ASU 2014-09 effective January 1, 2018. Under this proposal, early adoption as of January 1, 2017 also would be permissible. TDS is evaluating the effects that adoption of ASU 2014-09 will have on its financial position, results of operations, and disclosures.

On August 27, 2014, the FASB issued Accounting Standards Update 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern* ("ASU 2014-15"). ASU 2014-15 requires TDS to assess its ability to continue as a going concern each interim and annual reporting period and provide certain disclosures if there is substantial doubt about the entity's ability to continue as a going concern, including management's plan to alleviate the substantial doubt. TDS is required to adopt the provisions of ASU 2014-15 effective January 1, 2016, but early adoption is permitted. The adoption of ASU 2014-15 is not expected to impact TDS' financial position or results of operations.

On February 18, 2015, the FASB issued Accounting Standards Update 2015-02, *Consolidation: Amendments to the Consolidation Analysis* ("ASU 2015-02"). ASU 2015-02 simplifies consolidation accounting by reducing the number of consolidation models. Additionally, ASU 2015-02 changes certain criteria for identifying variable interest entities. TDS is required to adopt the provisions of ASU 2015-02 effective January 1, 2016. Early adoption is permitted. TDS is evaluating the effects that adoption of ASU 2015-02 will have on its financial position, results of operations, and disclosures.

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On April 7, 2015, the FASB issued Accounting Standard Update 2015-03, *Simplifying the Presentation of Debt Issuance Costs,* which requires debt issuance costs to be presented in the balance sheet as an offset to the related debt obligation. TDS is required to apply the standards of this update effective January 1, 2016 on a retrospective basis. Early adoption is permitted. As of March 31, 2015, TDS had $60.0 million in debt issuance costs classified as Other assets and deferred charges that, upon adoption of the new standard, would be reclassified as an offset to Long-term debt.

Amounts Collected from Customers and Remitted to Governmental Authorities

TDS 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 TDS merely acts as an agent in collecting the tax on behalf of the imposing governmental authority. 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 $26.1 million and $31.0 million for the three months ended March 31, 2015 and 2014, respectively.

2. Fair Value Measurements

As of March 31, 2015 and December 31, 2014, 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.

The provisions of GAAP establish a fair value hierarchy that contains three levels for inputs used in fair value measurements. Level 1 inputs include quoted market prices for identical assets or liabilities in active markets. Level 2 inputs include quoted market prices for similar assets and liabilities in active markets or quoted market prices for identical assets and liabilities in inactive markets. Level 3 inputs are unobservable. A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. A financial instrument's level within the fair value hierarchy is not representative of its expected performance or its overall risk profile and, therefore, Level 3 assets are not necessarily higher risk than Level 2 assets or Level 1 assets.

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, 2015		December 31, 2014	
		Book Value	Fair Value	Book Value	Fair Value
(Dollars in thousands)					
Cash and cash equivalents	1	$ 635,120	$ 635,120	$ 471,901	$ 471,901
Long-term debt					
Retail	2	1,453,250	1,468,689	1,453,250	1,414,105
Institutional and other	2	537,362	530,975	537,471	518,322

The fair value of Cash and cash equivalents approximates the book value due to the short-term nature of these financial instruments. Long-term debt excludes capital lease obligations and the current portion of Long-term debt. 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 and 7.25% Senior Notes. TDS’ “Institutional” debt consists of 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 7.02% and 0.00% to 7.25% at March 31, 2015 and December 31, 2014, respectively.

3. Equipment Installment Plans

TDS offers customers the option to purchase certain devices under an equipment installment contract over a period of up to 24 months. For certain equipment installment plans, after a specified period of time, the customer may have the right to upgrade to a new device and have the remaining unpaid equipment installment contract balance waived, subject to certain conditions, including trading in the original device in good working condition and signing a new equipment installment contract. TDS values this trade-in right as a guarantee liability. The guarantee liability is initially measured at fair value and is determined based on assumptions including the probability and timing of the customer upgrading to a new device and the fair value of the device being traded-in at the time of trade-in. As of March 31, 2015 and December 31, 2014, the guarantee liability related to these plans was $67.8 million and $57.5 million respectively, and is reflected in Customer deposits and deferred revenues in the Consolidated Balance Sheet.

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TDS equipment installment plans do not provide for explicit interest charges. For equipment installment plans with a duration of greater than twelve months, TDS imputes interest.

The following table summarizes unbilled equipment installment plan receivables as of March 31, 2015 and December 31, 2014. Such amounts are presented on the Consolidated Balance Sheet as Accounts receivable – customers and agents and Other assets and deferred charges, as applicable.

(Dollars in thousands)	March 31, 2015			December 31, 2014	
Short-term portion of unbilled equipment installment plan receivables, gross	$	166,551		$	127,400
Short-term portion of unbilled deferred interest		(17,739)			(16,365)
Short-term portion of unbilled allowance for credit losses		(5,631)			(3,686)
Short-term portion of unbilled equipment installment plan receivables, net	$	143,181		$	107,349
Long-term portion of unbilled equipment installment plan receivables, gross	$	83,215		$	89,435
Long-term portion of unbilled deferred interest		(1,585)			(2,791)
Long-term portion of unbilled allowance for credit losses		(5,805)			(6,065)
Long-term portion of unbilled equipment installment plan receivables, net	$	75,825		$	80,579

TDS assesses the collectability of the equipment installment plan receivables based on historical payment experience, account aging and other qualitative factors. The credit profiles of TDS customers on equipment installment plans are similar to those of TDS customers with traditional subsidized plans. Customers with a higher risk credit profile are required to make a deposit for equipment purchased through an installment contract.

4. Income Taxes

TDS' overall effective tax rate on Income before income taxes for the three months ended March 31, 2015 and 2014 was 39.8% and 36.5%, respectively.

TDS incurred a federal net operating loss in 2014 largely attributable to 50% bonus depreciation applicable to qualified 2014 capital expenditures. TDS carried back this federal net operating loss to prior tax years. As a result of the carryback, together with recovery of federal estimated taxes paid in 2014, TDS received a $99.7 million federal income tax refund in the three months ended March 31, 2015.

5. 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:

	Three Months Ended March 31, 2015		Three Months Ended March 31, 2014
(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	$	145,728	$	18,242
Adjustments to compute diluted earnings:			
Noncontrolling interest adjustment		(1,270)		(165)
Preferred dividend adjustment		12		-
Net income attributable to common shareholders of TDS used in diluted earnings per share	$	144,470	$	18,077
Weighted average number of shares used in basic earnings per share:			
Common Shares		100,990		101,821
Series A Common Shares		7,179		7,167
Total		108,169		108,988
Effects of dilutive securities:			
Stock options		368		303

Restricted stock units		359			381
Preferred shares		50			-
Weighted average number of shares used in diluted earnings per share		108,946			109,672
Basic earnings per share attributable to TDS shareholders	$	1.35		$	0.17
Diluted earnings per share attributable to TDS shareholders	$	1.33		$	0.16

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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.

	Three Months Ended March 31, 2015	2014
(Shares in thousands)		
Stock options	6,480	6,915
Preferred shares	-	57

6. Acquisitions, Divestitures and Exchanges

Divestiture Transaction

On May 16, 2013, pursuant to a Purchase and Sale Agreement, U.S. Cellular sold customers and certain PCS license spectrum to subsidiaries of Sprint Corp. fka Sprint Nextel Corporation ("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."

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. As of March 31, 2015, U.S. Cellular had received a total of $97.4 million pursuant to the Sprint Cost Reimbursement. For the three months ended March 31, 2015 and 2014, $15.7 million and $11.3 million, respectively, of the Sprint Cost Reimbursement had been received and recorded in Cash received from divestitures and exchanges in the Consolidated Statement of Cash Flows.

For the three months ended March 31, 2015 and 2014, as a result of the Divestiture Transaction, U.S. Cellular recognized gains of $4.4 million and $7.1 million, respectively, in (Gain) loss on sale of business and other exit costs, net.

Other Acquisitions, Divestitures and Exchanges

- In March 2015, U.S. Cellular exchanged certain of its unbuilt PCS licenses for certain other PCS licenses located in U.S. Cellular's existing operating markets and $117.0 million of cash. The licenses received in the transaction have an estimated fair value, per a market approach, of $43.5 million. A gain of $125.2 million was recorded in (Gain) loss on license sales and exchanges, net in the Consolidated Statement of Operations in the first quarter of 2015.

- An FCC auction of AWS-3 spectrum licenses, referred to as Auction 97, ended in January 2015. U.S. Cellular participated in Auction 97 indirectly through its limited partnership interest in Advantage Spectrum L.P. ("Advantage Spectrum").

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Advantage Spectrum was the provisional winning bidder of 124 licenses for an aggregate winning bid of $338.3 million, after its designated entity discount of 25%. Advantage Spectrum's bid amount, less the initial deposit amount of $60.0 million paid in 2014, was paid to the FCC in March 2015. These licenses are expected to be granted by the FCC during 2015. See Note 9 — Variable Interest Entities (VIEs) for additional information.

- In December 2014, U.S. Cellular entered into an agreement with a third party to sell 595 towers and certain related contracts, assets, and liabilities for $159.0 million. This transaction was accomplished in two closings. The first closing occurred in December 2014 and included the sale of 236 towers, without tenants, for $10.0 million. On this same date, U.S. Cellular received $7.5 million in earnest money. At the time of the first closing, a $4.7 million gain was recorded. The second closing for the remaining 359 towers, primarily with tenants, took place in January 2015, at which time U.S. Cellular received $141.5 million in additional cash proceeds and recorded a gain of $119.6 million in (Gain) loss on sale of business and other exit costs, net.

- In September 2014, U.S. Cellular entered into an agreement with a third party to exchange certain PCS and AWS licenses for certain other PCS and AWS licenses and $28.0 million of cash. This license exchange will be accomplished in two closings. The first closing occurred in December 2014 at which time U.S. Cellular received licenses with an estimated fair value, per a market approach, of $51.5 million, recorded a $21.7 million gain and recorded an $18.3 million deferred credit in Other current liabilities. The second closing is expected to occur in the second half of 2015. A license with a $22.2 million book value will be transferred and has been classified as "Assets held for sale" in the Consolidated Balance Sheet as of March 31, 2015. At the time of the second closing, TDS will recognize the deferred credit from the first closing and expects to record a gain on this part of the license exchange.

7. Intangible Assets

Changes in Licenses at TDS for the three months ended March 31, 2015 are presented below. There were no significant changes to Franchise rights, Goodwill or other intangible assets during the three months ended March 31, 2015.

Licenses			
(Dollars in thousands)			
Balance December 31, 2014		$	1,453,574
	Acquisitions (1)		339,657
	Exchanges (2)		43,485
	Other		522
Balance March 31, 2015		$	1,837,238

(1)	Amount includes payments totaling $338.3 million made by Advantage Spectrum to the FCC for licenses in which it was the provisional winning bidder in Auction 97. See Note 6 — Acquisitions, Divestitures and Exchanges, and Note 9 — Variable Interest Entities (VIEs) for further information.
(2)	Amount represents licenses received in the PCS license exchange. See Note 6 — Acquisitions, Divestitures and Exchanges for further information. Licenses disposed of in the exchange were previously removed from the License balance and reflected in Assets held for sale in the Consolidated Balance Sheet as of December 31, 2014.

8. 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.

Equity in earnings of unconsolidated entities totaled $34.6 million and $37.3 million in the three months ended March 31, 2015 and 2014, respectively; of those amounts, TDS' investment in the Los Angeles SMSA Limited Partnership ("LA Partnership") contributed $19.9 million and $21.2 million in the three months ended March 31, 2015 and 2014, respectively. TDS held a 5.5% ownership interest in the LA Partnership during these periods.

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.

	Three Months Ended March 31,	
	2015	2014
(Dollars in thousands)		
Revenues	$ 1,735,340	$ 1,625,765
Operating expenses	1,291,512	1,142,073
Operating income	443,828	483,692
Other income, net	4,470	1,835
Net income	$ 448,298	$ 485,527

9. 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

As of March 31, 2015, TDS holds a variable interest in and consolidates the following VIEs under GAAP:

- Advantage Spectrum and Frequency Advantage L.P., the general partner of Advantage Spectrum;
- 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 Advantage Spectrum, 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 the 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, 2015		December 31, 2014
(Dollars in thousands)				
Assets				
Cash and cash equivalents	$	11,670	$	2,588
Other current assets		234		278
Licenses		651,281		312,977
Property, plant and equipment, net		10,129		10,671
Other assets and deferred charges		247		60,059
Total assets	$	673,561	$	386,573